

Annual Staff Report
on the
Management of State School Lands
Fiscal Year 2014-15



California State Lands Commission
Gavin Newsom, Lieutenant Governor
Betty T. Yee, State Controller
Michael Cohen, Director of Finance

Jennifer Lucchesi
Executive Officer

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 on March 3, 1853 by an Act of Congress (Ch. 145, 10 Stat. 244) for the purpose of supporting public schools. These lands consisted of the 16th and 36th sections of land in each township, save lands reserved for other public purposes, lands previously conveyed, e.g., rancho lands, sovereign lands, and swamp or overflowed lands, and lands known to be mineral in character. A supplementary act in 1927 expanded the grant to include minerals (Ch. 57, 44 Stat. 1026). No federal patents to the State were required under the grant; title to the lands was vested in the State upon approval of the U.S. Township Survey Plats.

Indemnity School Lands (also known as Lieu Lands) - When a Section 16 or Section 36 was not granted to California because of an exception, the State was given the opportunity to select replacement lands from the United States (Ch. 81 19 Stat. 267). Each transaction involved several steps. First, the State filed a list with the federal government describing the lands lost, which were known as base lands. Second, the State filed a list with the federal government describing other federal lands selected in place of the base lands. When the federal government approved replacement lands, it issued the State a Clear List. California'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; no patents were issued by the federal government.

For this Annual Report, the term *school lands* is used to describe lands obtained under the Act of 1853 and indemnity school lands obtained through the Clear List application process.

The **Annual Staff Report on the Management of State School Lands** is prepared pursuant to Public Resources Code § 6477, which requires the State Lands Commission to report annually to the Legislature and the Governor on the management of school and lieu lands.

CALIFORNIA STATE LANDS COMMISSION

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

Fiscal Year 2014-15

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INTRODUCTION AND EXECUTIVE SUMMARY

The California State Lands Commission (CSLC) manages approximately 462,890 acres of school lands held in fee ownership by the State of California 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 original school lands were sold by the State during the first 130 years of statehood.

Management of the School Lands Program is divided between the Mineral Resources Management Division (MRMD) and the Land Management Division (LMD). The MRMD is responsible for geothermal, solid minerals, and oil and gas leasing on school lands and for geothermal resource development, mining activities, and oil and gas development. The LMD is responsible for managing surface activities on school lands.

School lands were placed into a statutory trust in 1984 when the Legislature enacted the School Land Bank Act (Act) and created the School Land Bank Fund. The CSLC is the trustee of the Fund. Sections 8700 through 8716 of the Public Resources Code establish management guidelines for school lands. The Act states that school lands and attendant interests are to be proactively managed and enhanced to provide an economic base in support of public schools. The Act further requires the CSLC to take all action necessary to fully develop school lands, indemnity interests, and attendant mineral interests into a permanent and productive resource base. Public Resources Code § 8701 contains findings and declarations that emphasize developing school lands into a permanent and productive resource base and underscore that all transactions, including exchanges, sales, and acquisitions, should be implemented for revenue generating purposes.

Public Resources Code § 6217.7 requires that all net revenues, monies, and remittances from the sale of school lands be deposited into the State Treasury to the credit of the School Land Bank Fund. Public Resources Code § 6217.5 requires, with one exception, that all net revenues, monies, and remittances from school and lieu lands (i.e., royalties, rents, and interest generated from promissory notes) are deposited into the State Treasury to the credit of the Teachers' Retirement Fund, which benefits the State Teachers' Retirement System (STRS).

The CSLC's emphases in administering the School Lands Program is: 1) maximizing revenues from school lands and reserved mineral interests to benefit STRS; 2) protecting the corpus of the trust; and, 3) protecting the environment and complying with the California Environmental Quality Act.

Net revenue transferred to STRS during fiscal year 2014-15 was \$6,537,256.66, a decrease of 25.1 percent compared to fiscal year 2013-14. The decrease in net revenue was primarily attributable to three factors: 1) Gross revenues from the Solid Minerals program declined \$961,077.19 from the prior year, largely because of lower production from the Mesquite Gold Mine and lower demand for aggregate (sand and gravel) resources, 2) royalties from oil and gas leases declined \$1,065,129.49 from the prior year because of lower production and lower oil prices, and 3) overall expenses increased

because of staff's heavy time and resource commitment to participation in the Desert Renewable Energy Conservation Plan.

Management expenses in fiscal year 2014-15 totaled \$1,217,436.18, an increase of 2.7% from the prior year. The School Land Bank Fund's fiscal year-end balance was \$2,414,004.17, an increase of \$1,683,995.89 over the prior year. This amount does not include a \$59,000,000 loan to the General Fund that is required to be repaid by June 30, 2016. For a summary, see the table entitled "Financial Summary: Fiscal Year 2014-15" (page 33).

On a somber note, the September 2015 Valley Fire not only burned more than 76,000 acres and damaged or destroyed more than 2,000 structures in the town of Middleton and surrounding communities of Lake County, but also damaged five geothermal facilities on school lands operated by Calpine in the Geysers Geothermal Field. The damage to the geothermal facilities significantly reduced the geothermal energy produced at this field. The damage is still being assessed and it is unknown how long it may take for full production to resume. Governor Brown declared a State of Emergency and President Obama declared the Valley Fire a major disaster, providing federal funding for assistance. Consequently, revenues from geothermal energy may be significantly impacted in fiscal year 2015-16. Additional information about the impacts of the September 2015 Valley Fire on school lands will be included in the fiscal year 2015-16 report.

GEOTHERMAL, SOLID MINERALS, AND OIL & GAS PROGRAMS

The MRMD is responsible for leasing and management of the Geothermal, Solid Minerals, and Oil & Gas Programs within school lands. These programs strive to maximize royalty revenues while protecting the environment and ensuring the highest levels of public safety. Historically, the majority of annual revenues to STRS from school lands can be attributed to the management of the mineral interests. For a summary of this year's revenues, see the table entitled "Summary of Revenue Generated from Geothermal, Solid Minerals, and Oil & Gas Programs – Fiscal Year 2014-15" (page 21).

FISCAL YEAR 2014-15 ACTIVITIES

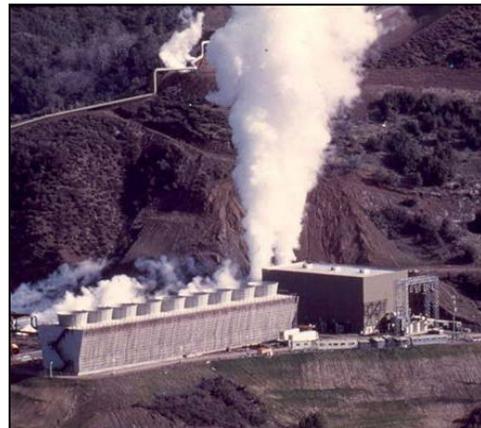
GEOTHERMAL PROGRAM

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 management and planning staff. Drilling proposals require a technical review by engineering staff. Drilling and production operations require documentation 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 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 revenue totaled \$5,352,254.23 for fiscal year 2014-15, a 3.5% decrease from the prior year.

An important development over the past year is MRMD staff's ongoing and proactive analysis of the geothermal potential of state school lands. This includes a review of all parcels with varying interests (fee, reserved mineral interest and 1/16th interest) located within and near 21 known Geothermal Resource Areas established by the United States Geological Survey in California. Isotherm maps, Division of Oil, Gas, and Geothermal Resources well data, and all other available information are being analyzed for each parcel within the various known Geothermal Resource Areas. Proximity of these parcels to electric transmission lines and power plants is also being reviewed. This effort will help determine whether opportunities exist for new



geothermal exploration and development to maximize school land revenues and achieve California's renewable energy goals. This study will be concluded in the first half of fiscal year 2015-16.

Geothermal Leases at the Geysers (CSLC Lease No. PRCs 4596, 4596 "A", 4597, 5206, 6422, 7845, 7179, 8556, 8844 and 8950)

Background: The Geysers has operated commercially for 55 years and is the largest geothermal energy project in the world. The field generates more than 800 megawatts of electricity annually from approximately 28,000,000 pounds of steam, enough to supply over 900,000 homes for a year. Steam production has been relatively stable since 1995, because of consolidating field operations and increased water injection into the reservoir. The injection water is piped to the field from nearby reclamation plants in Lake County and the city of Santa Rosa in Sonoma County.

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 through the indemnity selection process in the 1980s. Geysers Power Company LLC and CPN Wild Horse Geothermal LLC, both subsidiaries of Calpine Corporation, hold these leases. Geysers Power Company LLC owns and operates 17 of the 22 electrical-generating units at The Geysers.



In May 2013, Calpine applied to amend State Geothermal Lease PRC 8556 to hold that portion of the lease identified by Parcel 3, with injection rather than production. Staff reviewed the application and supporting documents and determined that it would be advantageous to allow Parcel 3 to be held by injection. Staff negotiated a rent increase with Calpine for the 480 acres from \$10 per acre to \$250 per acre. The increased rent will remain for the duration of the injection term of ten years, plus two 5-year extensions. The rent will not decrease to \$10 per acre unless there is future production on this parcel. In June 2014, the CSLC approved this lease amendment. Subsequently, Calpine forked and extended the Aidlin 10 well from their private lease holding into State lands so that it penetrates and bottoms into Parcel 4 of this same lease, allowing Calpine to hold the lease until production ceases.

Update: In order to consolidate and phase out an antiquated power plant, Calpine decommissioned the Bear Canyon power plant in March 2014 and constructed a supplementary pipeline diverting the steam from the PRC 5206 wells to the Quicksilver power plant (aka, Unit 16).

As mentioned above, the Valley Fire impacted Calpine's operation significantly and is likely to affect its future production and revenue.

Geothermal Lease in Imperial County (CSLC Lease No. PRC 9115.2)

Background: On February 21, 2014, the CSLC approved a Negotiated State Geothermal Resources Lease to Imperial Wells Power, LLC (IWP) to explore and develop geothermal resources on 40 acres of school lands located within the Wister Wildlife Management Area. The proprietary lease, issued on behalf of the California Department of Fish and Wildlife, prohibits surface occupancy. The surface disturbances from project components are located in Section 12 of Township 11 South, Range 13 East, and Sections 7 and 18 of Township 11 South, Range 14 East, SBM, Imperial County. The royalty is 3% of the value of electricity generated from geothermal resources attributable to the leased land, or 10.5% of the gross revenue received from the sale of steam. The minimum annual royalty is \$100 per acre or \$4,000. The annual land rent is \$50 per acre until the leased land becomes part of a producing geothermal unit and production royalties are accruing to the State; at which time the rent is reduced immediately to \$1 per acre.

Update: On January 15, 2015, IWP submitted a full quitclaim deed for the above lease, stating they believe the leased lands are not commercially productive. This quitclaims back to the State all of the lessee's right, title, and interest for the lands. The quitclaim action was accepted by the CSLC at its February 20, 2015 meeting. Although no production or royalty accrued to the State during the nearly one year duration of the lease, STRS received \$2,000 for the land rental.

Geothermal Leasing Proposed in Imperial County (CSLC File No. W 40978)

Background: 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 (CDPR) in the Truckhaven area west of the Salton Sea in Imperial County. A portion of the land is located within CDPR's Ocotillo Wells State Vehicular Recreation Area. Pursuant to Public Resources Code § 6924, CSLC staff coordinates its leasing with CDPR to ensure that exploration and development does not unreasonably interfere with using the lands for the purpose they were acquired, which is off-highway vehicle recreation.

CSLC staff has attempted to have these lands explored 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 twice for lease by competitive bid, the last of which was in 2007. Both nominations were from Ormat Nevada, Inc. but each time Ormat withdrew its nomination when requested to fund an environmental review. In 2011, Ormat sold its private and federal lease interests to Iceland America Energy, which subsequently sold the leases to NGP.

The State parcels at Truckhaven are interspersed with federal lands managed by the BLM and with 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. Upon failure by the three lessees to form a unit agreement, BLM cancelled all three of the geothermal leases on September 9, 2013, making the lands available for a subsequent lease sale that BLM held in September 2014.

Update: Alternative Energy Resources Inc. (AER), formally known as NGP, was the applicant for the State Geothermal Negotiated Lease application, and was the successful bidder for four sections of land nominated for the September 2014 BLM lease sale. Following the BLM lease sale, AER sold all their interest in the Truckhaven area to Ormat.

Ormat applied to the CSLC on February 24, 2015, under ORNI 5 LLC (ORNI), for a Negotiated Geothermal Lease. Staff closed AER's application and accepted a Negotiated Lease application from ORNI. As of March 19, 2015, the ORNI application is incomplete and staff is awaiting a full project description. Staff has informed CDPR of the lease application and is coordinating with CDPR staff because the application includes approximately 1,394 acres of land CDPR owns.

Geothermal Prospecting Permits

Deep Rose Development, LLC (CSLC Lease No. PRC 8949)

Background: In June 2013, CSLC staff issued a two-year extension 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 completing the last mile of an 8-mile road that will be used to construct a well pad for the drill rig. Drilling will follow completion of the road construction.

The State parcel is surrounded by the Haiwee Geothermal Lease Area, a collection of federal parcels that may be offered for lease by the BLM. If the area contains geothermal resources in commercial quantities, development will likely include state and federal lands.

Update: In March 2015, CSLC staff notified Deep Rose of their August 31, 2015 permit expiration date and provided instructions for applying for a new permit. Staff anticipates that Deep Rose will apply for a new permit prior to the August deadline.

Entiv Organic Energy (CSLC Lease No. PRC 8998)

Background: In June 2012, the State approved a two-year permit 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 parcel, until 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 goal was 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, under the prospecting permit, Entiv deepened well 9-A to a depth of 1220' and observed elevated temperatures that were evaluated to determine if commercial production was viable.

Update: In January 2014, Entiv informed staff they had discovered geothermal resources in commercial quantities and would like to exercise their right for a preferential lease. On November 6, 2014, Entiv submitted an application for a preferential Geothermal Lease. As of December 5, 2014, the application was incomplete and CSLC staff is waiting for

Entiv to complete their application, including providing evidence that the parcel can be commercially developed.

High Valley, LLC (CSLC Lease No. PRC 9001)

Background: In 2012, the CSLC approved a two-year permit for High Valley, LLC (High Valley), a subsidiary of the US Renewables Group. The permit includes 1,383 acres of school lands located north of The Geysers Geothermal Field. High Valley planned to reopen one or more wells drilled during the 1980s and drill new exploratory wells to confirm the presence of geothermal resources and evaluate their commercial potential.

Update: No activity took place during fiscal year 2014-15. On September 9, 2014, High Valley notified staff that they wished to terminate their prospecting permit, together with the Kelsey North and South applications. On September 17, 2014, CSLC staff acknowledged the termination of the permit and applications. On November 3, 2014, CSLC staff released the security bond back to High Valley after conducting a final inspection of the property. The land is now unencumbered and available for permitting or leasing.

SOLID MINERALS PROGRAM

Revenue from the Solid Minerals program totaled \$712,156.66 in fiscal year 2014-15. This was a 57.4% decrease from the prior year's revenue of \$1,673,233.85. The primary reason for this decrease was the production decline from the State's interest at the Mesquite Gold Mine. Production has also decreased from the State's aggregate leases, decreasing the royalty revenue.

The Solid Minerals program staff manages four leases totaling 1,036 acres, one 1/16th reserved mineral interest parcel totaling 560 acres, and four mineral prospecting permits totaling 1,898 acres. Four of the mineral prospecting permits will expire during the first quarter of the next fiscal year, but all the permittees express interest in applying for permit extensions. During this fiscal year, two State Leases (PRCs 736 and 6735) completed reclamation and were closed.

In addition to managing mineral prospecting permits and leases, CSLC staff responded to numerous mineral inquiries and addressed abandoned mine hazards that could threaten the public and wildlife.

Mineral Extraction Leases

U.S. Borax (CSLC Lease No. PRC 736)

Background: 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 continued 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 a CSLC staff inspection conducted in 2007, all remaining hazardous materials were removed from the underground workings. Since 2006, U.S. Borax continues to work on re-vegetation and minor earthwork.



Update: On April 24, 2014, OMR and Inyo County determined during a joint inspection that reclamation was completed in accordance with the Lead Agency approved Reclamation Plan #89-2. A confirmation letter is expected from OMR and Inyo County soon. Staff periodically visits the site to monitor the two bat gates and two air grates and check for vandalism.

Hanson Aggregates (CSLC Lease No. PRC 7301)

Background: Hanson Aggregates (Hanson) holds a 102-acre lease near Lakeside in northern San Diego County for the Vigilante Aggregate Mine. Revenue from this lease totaled \$7,500 in fiscal year 2014-15 and 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 continued weak demand.



On September 1, 2011, the CSLC renewed and amended the lease term through June 30, 2021. Hanson's new lease has a higher royalty rate of 6.5% of the gross sales. One impediment to the resumption of operations is a large waste pile of fine material that Hanson has been unable to sell.

Update: There are no significant updates for the Vigilante Aggregate Mine; the mine is currently idle.

Western Mesquite Mines (CSLC Lease No. PRC 8039)

Background: In October 2002, the CSLC issued Western Mesquite Mines Inc. a mineral extraction lease on 658 acres of school lands to expand their approximately 5,000 acre Mesquite Gold Mine complex northward, on the south flank of the Chocolate Mountains in Imperial County. Mining on the parcel commenced in the fall of 2011, and the State received its first royalty production payment in January 2012.



In 2012, the lease was amended and renewed through September 30, 2022, providing for a sliding scale royalty of 6 to 9 percent of the gross revenue depending on the price of gold.

Update: Staff conducts periodic site inspections to verify the mining and production process and proper payment of royalty. The total revenue generated for the 2014-15 fiscal year was \$526,074.54, a significant decrease from the prior fiscal year. In fiscal year 2014-15, the royalty percentage averaged approximately 6%, with the price of gold ranging from \$1,176 to \$1,307 per ounce.

Western Mesquite Mines Inc. produced during the first half of the 2014-15 fiscal year, but mining on the parcel last occurred in November 2014. Unless gold prices rally

significantly, resumption of mining on the State portion of the Mesquite Mine is not expected.

Gold ore already placed on the heap leach pad will continue to be recovered, and royalty will continue to be paid to the State on the nearly 5,000 ounces remaining to be leached and processed. As monthly sales are made, the State is paid at a rate proportional to their ownership of the heap leach pad. Since the State's ore is no longer being added to the heap leach pad, the State ownership proportion is decreasing. The State, however, should see revenues from the mine continue for several years, with revenue and future mining highly dependent on future gold prices.

Vulcan Lands, Inc. (CSLC Lease No. PRC 8253)

Background: Vulcan Lands, Inc. (Vulcan) holds a 160-acre lease at its Black Angel Quarry southwest of Barstow in San Bernardino County. Periodic inspections reveal continued activity with large stockpiles of sorted aggregate.



Update: During this fiscal year, Vulcan's production decreased by 55%. Vulcan claims that competition from four other quarries in the market region has significantly impacted sales. Revenue generated for the fiscal year totaled \$151,687.40.

Granite Construction, Ludlow Pit (CSLC Lease No. PRC 8272 - Expired)

Background: 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.



Update: Since the County's conditional use permit is valid, staff periodically monitors the site for any mineral production or shipments.

Protech Minerals (CSLC Lease No. PRC 8322 - Expired)

Background: 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 with Steve Suitt (a contractor for San Bernardino County) the CEQA lead agency, and OMR to determine if reclamation was complete. While there has been substantial reclamation, the County identified additional grading necessary prior to approving a final



closure. Reclamation was not concluded during fiscal year 2014-15 and remains outstanding.

Update: Staff will continue working with San Bernardino County mining geologist George Kenline and OMR staff until reclamation is complete.

Hi-Grade Materials (CSLC Lease No. PRC 8831)

Background: 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. Royalty in fiscal year 2014-15 was \$26,874.32, which is a decrease attributed to an additional quarry acquired by Hi-Grade.



In September 2013, the San Bernardino County Planning Department approved Hi-Grade's Conditional Use/Mining Permit and Reclamation Plan, which permitted the mining of all 116 acres of leased State school lands. This revision will allow mining to continue for several decades.

Update: In March 2015, CSLC staff received an application for Hi-Grade's mineral extraction lease renewal that staff is currently processing. The existing lease expires on June 30, 2016.

Granite Construction, Palm Desert Pit (CSLC Lease No. PRC 7945)

Background: 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.

Update: During the 2nd quarter of fiscal year 2013-14, Granite notified CSLC staff that they will cease mining the State's Palm Desert parcel. No production has occurred since December 2013, and consequently no royalties have accrued.

Bureau of Reclamation (CSLC Lease No. PRC 6735)

Background: The United States 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 when the lease expired. One month later, with passage of the California Desert Protection Act, the quarry was included in the Dead Mountains Wilderness Area. In 2000, the BOR submitted an application for a new 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.



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 the mine was deemed out of compliance with the Surface Mining and Reclamation Act (SMARA). In 2012, BOR abandoned its effort to permit the mine and sought to complete final reclamation under SMARA. In April 2014, San Bernardino County approved a Grading Plan that would permit critical work to eliminate overstep slopes.

Update: Work commenced in November 2014 and finished in June 2015. CSLC staff is awaiting written confirmation from the County and OMR that final reclamation is complete.

Eagle Crest Pumped Energy Storage Project (State Clearinghouse House #2009011010)

Background: 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 leased to Kaiser Steel Corporation between 1980 and 2002. The project involves flooding the upper and lower pits and pumping water from the lower east pit to the upper pit at night when electrical usage is low. The water would then 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 provided 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, the CEQA lead agency for the project, petitioning the SWRCB not to certify the EIR due to cited deficiencies and because the project would preclude the State from developing the iron ore resource. In July 2013, the SWRCB certified the EIR and issued a water quality certification pursuant to Section 401 of the Clean Water Act. In September 2013, the SWRCB received timely petition from three parties, including Kaiser, to reconsider its water quality certification. In June 2014, the Federal Energy Regulatory Commission approved the project.



Update: The license states “Because of site access restrictions during development of its license application, the license requires Eagle Crest, prior to commencing construction, to conduct certain site-specific investigations and design monitoring programs to protect environmental resources. These investigations include hydrologic, hydraulic, geotechnical and hydrogeological surveys, as well as soil testing and sensitive species surveys.” These studies are believed to be ongoing. It was reported that Kaiser recently sold part of the old iron mine to Eagle Crest Energy. If the pumped water storage project is built, resumption of mining of iron ore at the Kaiser Eagle Mountain Mine will not occur for the foreseeable future. Iron ore prices, like many other commodities, softened in 2015 due to global economic challenges.

Mineral Prospecting Permits

Robert G. Wetzel (CSLC Lease No. PRC 9026.2)

Background: On October 19, 2012, the CSLC approved a mineral prospecting permit for Robert G. Wetzel (Wetzel) to conduct geologic mapping and hand sampling on approximately 633 acres of State fee-owned lands described as Section 16, Township 15 North, Range 10 East, SBM, San Bernardino County, approximately 10 miles northeast of Baker.



Following favorable results, on June 22, 2013, the CSLC approved an extension and amendment through October 31, 2014 to allow drilling six exploratory holes. On December 19, 2012 and January 4, 2013, staff conducted site inspections, met the permittee, and reviewed the proposed drill sites.

Update: Wetzel had insufficient funds for the approved drilling during the one-year extension term. On February 20, 2015, the CSLC approved the second and final extension to complete the work.

Gerald W. Baughman (CSLC Lease No. PRC 9145.2)

Update: On August 15, 2014, the CSLC approved a one year mineral prospecting permit to Mr. Gerald W. Baughman to prospect for precious minerals on a 480-acre school land parcel. Following positive results, the permittee indicated his intent to apply for an extension. Without an extension, the permit will expire on August 31, 2015.

Green Materials International, LLC (CSLC Lease No. PRC 9138.2)

Background: Green Materials International, LLC, (Green Materials) submitted an application for a mineral prospecting permit on October 11, 2014, to prospect for Xenotime, a rare earth mineral, and other minerals on approximately 640 acres of fee-

owned school lands. The parcel is in Music Valley and includes all of Section 16, Township 2 South, Range 10 East, SBM, in Riverside County, adjacent to Joshua Tree National Park. Green Materials purpose for seeking a prospecting permit is to conduct geological mapping, hand sampling, and use of a hand-held Geiger counter to determine if the parcel contains commercial rare earth deposits. Studies by the California Division of Mines and Geology, the United States Geological Survey, and others indicate that Music Valley contains rare earth deposits. On June 19, 2014, the CSLC approved Green Materials permit. It is effective through June 30, 2015. Green Materials applied for a mineral prospecting permit extension on June 5, 2015. CSLC staff is currently processing the application.

Ronald Martin (CSLC Lease No. PRC 9164.2)

Update: On October 14, 2014, the Commission issued a one year mineral prospecting permit to Mr. Ronald James Martin to prospect for precious metals on fee-owned school lands described as Section 36, Township 25.5 South, Range 40 East, MDM, in Kern County. Staff conducted a site inspection on March 18, 2014 and discovered abandoned mine features, including shafts and adits, located north of the parcel on BLM lands.

All permits require a royalty of twenty percent of the gross value of all minerals produced, extracted, shipped, used or sold. Under Mr. Martin's prospecting permit, the State received a royalty payment of \$20.10 for placer gold recovered from dry washing. Dry washing is a simple technique in which the high specific gravity of gold is used to physically separate it from sand and gravel.

Abandoned Mine Lands

Background: Staff continued to inventory and remediate abandoned mine features located on school lands that may threaten the public and wildlife. Staff participates in meetings with local, county, state, and federal agencies, as well as contractors, environmental groups, and the public to share information on assessment and remediation of physical and chemical hazards associated with abandoned mines.

A 2009 report by the California Natural Resources Agency summarized an inventory of chemical and physical hazards on lands managed by the State, including school lands. The Resources Agency directed the OMR to prioritize and coordinate the remediation of these sites. The OMR and the Department of Toxic Substances Control determined that chemical hazards on lands managed by CDPR were the highest priority for remediation. The report states that 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.

Update: During fiscal year 2014-15, staff continued to inventory abandoned mine sites and focused on the initial stages of cooperative remediation work plans with OMR. In October 2014, MRMD staff conducted an abandoned mine land contractor walkthrough of the Iron Horse, Fremont Peak, Shadow Mountains, Pacific Fluorite, and Gunsight abandoned mine sites to solicit a closure bid for bat gates, cupolas and cable netting.

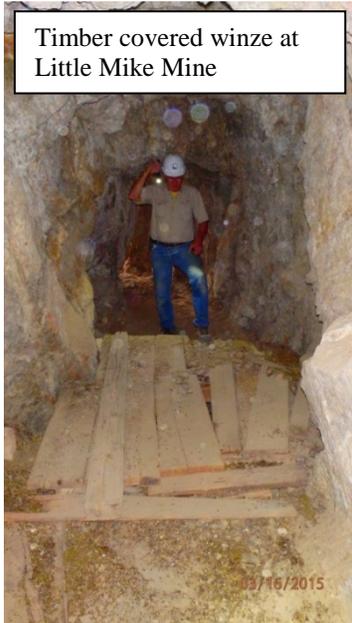
These previously inspected sites were evaluated for the degree of visitation by the public and the possible hazards present. Two contractors participated in the walkthrough and one submitted a bid.



Fence installation near Leiser Ray Mine

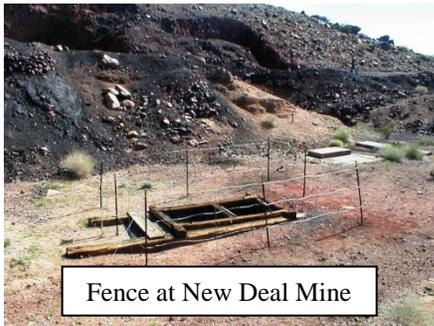
In December 2014, with the assistance of OMR staff, MRMD staff conducted site inspections and installed fences at the Leiser Ray, Shadow Mountains and Pacific Fluorite mines. One fence was installed on a timbered mine shaft at the Leiser Ray Mine, and another shaft was earmarked for future fencing. At the Shadow Mountain and Pacific Fluorite mines, two mine shafts were

fenced at each site. Other mine features within the vicinity of each site were re-inspected for signs of public visitation, wildlife usage, and their potential candidacy for professional contractor remediation closures in the future.



Timber covered winze at Little Mike Mine

In March 2015, with the assistance of OMR staff, MRMD staff conducted a further abandoned mines lands inventory and installed warning signs and fences at the Little Mike, Riggs, and New Deal mines. The Little Mike Mine is located near the town of Baker and had two mine features that were inventoried and photographed. Both of the primary features on this site, which comprise an adit and a shaft, were earmarked for future closures. The mine contains a winze covered with timbers that could present a hazard to the public. The Riggs Mine was determined to be within a fairly remote region that receives little public visitation. At the mine site, staff noted the high degree of difficulty in reaching the mine features and determined that the installation of warning signs was sufficient for ensuring public safety at this time.



Fence at New Deal Mine

In addition, OMR and MRMD staff augmented and installed fencing and warning signs for four mine shafts at the New Deal Manganese Mine near the southern end of Death Valley National Park. Mine features other than adits and shafts were also fenced and warning signs were installed, such as a large “gloryhole” excavation found at the eastern edge of the mine site.



In June, 2015, the remediation work order and contract was finalized and issued to Frontier Environmental Solutions, Inc. (FES) for the closure of 13 mine features at five sites: Pacific Fluorite, Iron Horse, Shadow Mountain, Fremont Peak, and Gunsight mines. The cost of the contract is \$181,895, and it prescribes the installation of (1) culvert, (3) bat gates, (6) cupolas, and (3) cable nets. FES completed a culvert bat gate at the Fremont Peak Mine on June 19, 2015 and a bat gate at the Gunsight and Shadow Mountain mines on June 24, 2015.

OIL & GAS PROGRAM

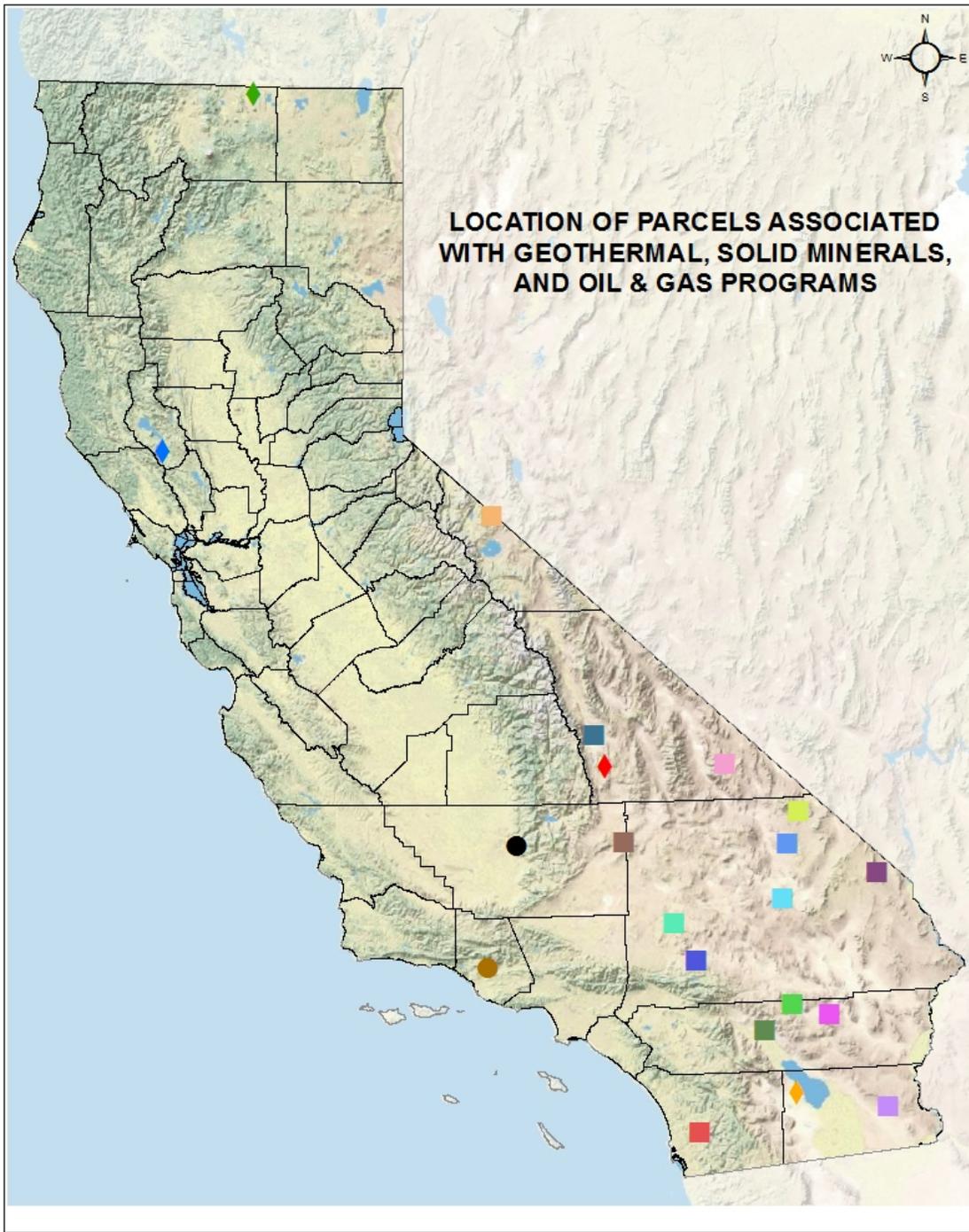
Revenue from the oil & gas program totaled \$1,427,217.09 in fiscal year 2014-15, a 42.7 percent decrease from the prior year. \$1,426,100.48 of that amount came from the 160-acre Round Mountain parcel (VA 5310) located northeast of Bakersfield in Kern County. This parcel is part of a unit operated by MacPherson Oil Company. Oil production from this parcel was 3,323,600 barrels, a 20 percent decrease from the previous year. Approximately ten percent of this reduction is due to decreased production; the remainder is logistical and related to the timing of the receipt mailing. The oil price averaged \$72.66 per barrel, 28 percent lower than the prior year. The balance of the revenue 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.

Background: The designations VA and LA stand for the Visalia and Los Angeles land districts of the previous California Surveyor General, which was a constitutional office until 1929. The sale of school lands was one function of that office. Transactions were typically identified with a district abbreviation and a number. The functions of the Surveyor General were transferred to the Division of State Lands within the Department of Finance in 1929, and to the CSLC in 1938.

Update: In March 2015, CSLC staff completed a financial and compliance audit of PRC VA 5310 covering July 1, 2010 through June 30, 2014. This audit focused on the verification of crude oil royalties paid to the State based upon the amount of oil produced and the price of the oil sold. While there were no material financial or compliance findings as a result of this audit, staff provided several recommendations to the lessee to improve their process for providing royalty information.

AB 982 (Skinner)/Desert Renewable Energy Conservation Plan

Further details about the Desert Renewable Energy Conservation Plan and CSLC's implementation of AB 982 (Skinner), Chapter 485, Statutes of 2012, and participation in the Desert Renewable Energy Conservation Plan (DRECP) are discussed in the Addendum to this report - *Report to the California State Legislature on the Status of School Land Consolidation Efforts in the California Desert - 2015*.



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
- Temo Oil Company: LA # 9252

Solid Minerals

- Bureau of Reclamation: PRC #6735
- Gary Goodson GMI, Music Valley: PRC# 9138
- Gerald Baughman: PRC #9145
- Granite Construction, Ludlow Pit: PRC #8272 - Expired
- Granite Construction, Palm Desert Pit: PRC #7945
- Hanson Aggregates: PRC #7301
- Hi-Grade Materials: PRC #8831
- Kaiser Resources: WO #40871
- Protech Minerals: PRC #8322 - Expired
- Robert G. Wetzel: PRC #9026.2
- Ronald James Martin: PRC #9164
- U.S. Borax: PRC #736
- US Borax, Owens Lake: PRC #5464
- Vulcan Lands, Inc.: PRC #8253
- Western Mesquite Mines: PRC #8039

Updated September 2015 by MRMD

**SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL,
SOLID MINERALS, AND OIL & GAS PROGRAMS -
FISCAL YEAR 2014-15**

Geothermal Royalties:

Regular PRC Royalties:	\$ 4,907,181.93
Supplemental PRC Royalties:	\$ 207,393.34
Fractional RMI Royalties:	\$ 193,616.53
Deposit to GRDA fund 034:	\$ 44,062.43
Total PRC/RMI Royalties:	\$ 5,352,254.23

Solid Minerals Royalties:

Royalties from leases:	\$ 712,136.26
Royalties from 1/16 th interest parcels:	\$ 0.00
Royalties from permits:	\$ 20.40
Solid Minerals Total:	\$ 712,156.66

Oil & Gas Royalties:

Oil & Gas Total:	\$ 1,427,217.08
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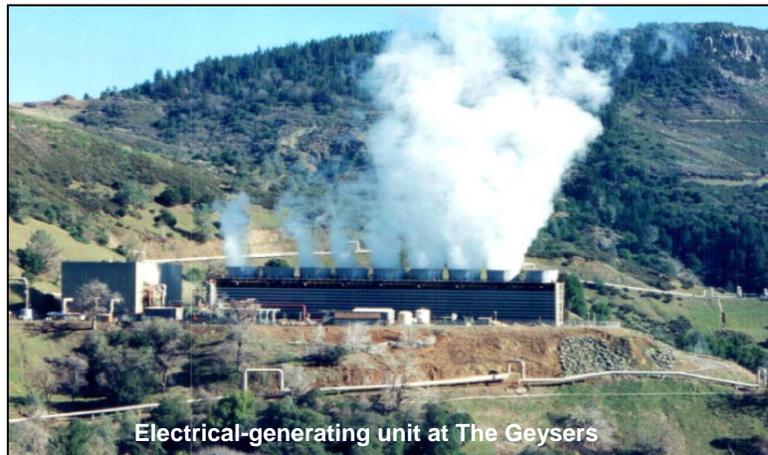
TOTAL GROSS REVENUE: \$ 7,491,627.97

FISCAL YEAR 2015-16 PLANNED ACTIVITIES

GEOTHERMAL PROGRAM

The Geysers

Staff forecasts that revenue from geothermal leases on school lands at The Geysers will be reduced during fiscal year 2015-16. Staff anticipates that steam production on developed leases will continue its slow, long-term decline, but note that electrical generation will be impacted in the short term by the destruction of 4-5



cooling towers in the Valley Fire. The Valley Fire has significantly affected the Geysers' future production. Prices for electrical power – underlain by those for natural gas – are expected to decrease slightly as global crude oil prices ease further. The continued scarcity of capital in light of preferential federal tax treatment for competing wind and solar generation will remain an obstacle to new exploration activity in the near term. Rig operations will be limited to maintenance and workovers.

Geothermal Permits

Staff will monitor the proposed exploratory drilling for Deep Rose's State Permit No. PRC 8949 in Inyo County and anticipates issuing Deep Rose a new prospecting permit. Successful drilling and discovery of commercial geothermal energy could lead to converting the permit into a lease, subject to CSLC approval.

Geothermal Applications

CSLC staff will process ORNI 5's Negotiated lease application in the Truckhaven area of Imperial County. ORNI 5 acquired all of AER's leasehold interest, including approximately 4,027 gross acres of federal and private leases. CSLC staff will participate in meetings with the BLM, CDPR and Imperial County to advance the application and assist in developing the geothermal resources.

CSLC staff is coordinating with Entiv to process their preferential lease application. In response to staff's December 5, 2015, incomplete letter, Entiv has sent updates regarding their meetings to move the application forward.

CSLC staff will continue to monitor and recommend to the CSLC amending and issuing new geothermal leases. Staff encourages new applicants and assists with answering inquiries regarding geothermal development.

SOLID MINERALS PROGRAM

Mineral Lease Management

During fiscal year 2014-15, the total royalty revenue generated was \$712,156.66, with \$526,000 (74 percent) produced by Western Mesquite Mines Inc. at the Mesquite Gold Mine. The reduction compared to the last fiscal year was due to reduced levels of gold and aggregate production and lower gold prices. According to the lessee, Western Mesquite Mines concluded mining on the State parcel on January 1, 2015. CSLC staff anticipates that the aggregate sales will pick up slowly as the economy improves, and the estimated school land revenue for the next fiscal year from solid minerals will be approximately \$600,000. This estimation is dependent on resumption of mining at the Hanson Vigilante Quarry in San Diego, commodity prices, and the ability of aggregate producers to secure competitive contracts.

As monthly sales are made at the Mesquite Mine, the State is paid proportional to its ownership of the heap leach pad. Since the State parcel is officially mined out, 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, because the State is paid when ounces are sold. The property was acquired under an exchange with the BLM as a part of the California Desert Protection Act of 1994. The federal government will receive an equal value of state inholdings within park and wilderness areas for all royalty revenues received.

The slow economy continues to affect aggregate mining in southern California. The State currently has three school land aggregate leases. While a production decline at the Hi-Grade Lucerne Valley Pit was modest, the Vulcan Black Angel Quarry was down over 50 percent. The good news is that Hanson plans to reopen the Vigilante Quarry near San Diego in the second half of the next fiscal year. Vulcan, at the Black Angel Quarry, anticipates stiff pricing competition to continue from surrounding quarries. Staff anticipates an increased demand for aggregate for road construction and housing as recovery from the recession continues and interest in investing in California's infrastructure mounts.

Mineral Applications

All four of the CSLC's mineral prospecting permittees have either applied or expressed their interest to apply for extensions of their permits to continue prospecting efforts. It is hoped that this effort will lead to commercial discovery of minerals and issuance of new mineral leases.

Staff will continue to field inquiries for, manage, extend, and issue new mineral prospecting permits. Staff encourages new applicants to request 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.

Abandoned Mine Lands

In fiscal year 2015-16, staff will continue overseeing and inspecting incomplete contract remediation work. Staff anticipates that the remaining mine features earmarked for contracted closures will occur during the fiscal year 2015-16 biologic window, which is weather-dependent and generally ends by Thanksgiving. Following completion of construction activities, CSLC staff will inspect the quality and integrity of the closures. Staff will also continue to inventory and assess previously unvisited abandoned mine features on school lands throughout the earlier part of the next year. A new list of prospective mine closures will be compiled as inspections occur in fiscal year 2015-16. Staff expects to install fences and warning signs as warranted.

Staff will continue to inspect the Crown Uranium and other mines that have received signage, fencing, bat gates, cupolas, backfills, or other protective measures to ensure their continued fortification against adverse weather and vandalism. Staff will continue participating in abandoned mine meetings that OMR convenes to share information concerning abandoned mine lands and efforts of local, state, and federal agencies. Additionally, MRMD staff is hoping to complete a comprehensive, statewide assessment of all hazardous mine features on school lands. This report will detail the number of applicable mine features and their present remediation status to aid staff in a comprehensive assessment the progress of abandoned mine remediation, which will enable efficient planning and timely mine closures.

OIL & GAS PROGRAM

Staff estimates that revenue from the two school lands oil & gas parcels will decline during fiscal year 2015-16 because of continued weakness in global energy demand (largely due to China's slowing economy) and the natural decline of the oil fields.

SURFACE MANAGEMENT PROGRAM

The Land Management Division is responsible for overseeing all surface activities on school lands. Surface activities include land exchanges, sale of school lands parcels to public or private entities, land acquisitions to enhance the resource base, and administering leases for purposes such as renewable energy production, agriculture, grazing, and rights-of-way for roads, oil and gas pipelines, and electrical transmission lines. The objectives are to generate revenue to benefit STRS, assure ongoing viability of the State's resources, protect the corpus of the trust, enhance local economic development, and protect the environment. For a summary of the revenues generated to STRS and the School Land Bank Fund through surface activities, please see the table entitled "Summary of Revenue Generated From Surface Management Program - Fiscal Year 2014-15" (page 29).

FISCAL YEAR 2014-15 ACTIVITIES

STATE TEACHERS' RETIREMENT SYSTEM FUND REVENUES

Surface Rental Income and Revenues

General surface leasing involves 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 462,890± acres of school lands are isolated landlocked parcels, many of which are non-revenue generating desert lands and lands inside national parks or federal wilderness areas. Approximately a quarter of the total school land acreage is leased for revenue-generating purposes.

Revenues deposited into the STRS fund from 141 revenue-generating surface leases in fiscal year 2014-15 totaled \$339,949.38, an increase of 29.4% from fiscal year 2013-14 and a total increase of more than 80% since fiscal year 2011-12. Surface rent rates are usually tied directly to land values, which are improving. CSLC surface leases typically require rent reviews every five years and these revisions reflect the higher land values. Several new right-of-way leases were also issued.

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

Loan to the General Fund

In fiscal year 2008-09, the Legislature borrowed \$59,000,000 from the School Land Bank Fund to help balance the state budget. This loan to the General Fund was part of the Budget Act of 2008 (Chapter 2, Statutes of 2009, Third Extraordinary Session). The loan must be repaid by June 30, 2016. During the term of the loan, interest accrues based on the rate used by the Surplus Money Investment Account.

Bureau of Land Management CDPA Land Exchange (CSLC File No. 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 BLM, and designated an additional four million acres in southern California for inclusion in the national park system. The purpose of the CDPA is to preserve areas in the California desert to protect their 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 as within the boundaries of the CDPA.

Section 707 of the CDPA authorizes exchanging school lands within CDPA designated areas for federal lands located outside of these areas. The CSLC is compensated for the exchange of its fee and mineral interests on a value-for-value basis, as determined by fair market appraisals. To date, five CDPA land exchange transactions have been completed, resulting 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 School Land Bank Fund.

Work continues on a sixth CDPA land exchange involving 69 parcels of school lands totaling approximately 38,434 acres. These parcels are within national parks, national monuments, and federal wilderness areas. Staff hopes that the sixth land exchange will be completed in fiscal year 2015-16 and will result in a deposit of \$7,994,925 into the School Land Bank Fund. For more information on this exchange, please see page 31.

Department of Parks and Recreation Land Sale (CSLC File No. SA 5763)

In fiscal year 2005-06, CDPR submitted an application to purchase 5,758 acres of school lands for a State Vehicle Recreation Area. The lands consist of nine full sections located in Imperial County, west of the Salton Sea. CDPR had previously completed an acquisition involving 4,000 acres of privately-owned land. The nine sections of school lands are in a checkerboard pattern amid this previously acquired property. Since originally proposed, the purpose of this sale was modified. CDPR is now proposing to use portions of these school lands as mitigation for a development project by San Diego Gas & Electric. CDPR will use approximately half of the transferred school lands to expand Anza Borrego State Park, and CDPR's Off-Highway Vehicle Division will use the remaining lands for a State Vehicle Recreation Area. This sale closed in August 2014 and added \$2,304,000 to the School Land Bank Fund.

United States of America Land Sale (CSLC File No. SA 5767)

On January 14, 2014, the United States, acting through the Department of the Navy, submitted an application to purchase portions of seven sections of school and indemnity lands as part of the expansion project for the Marine Corps Air Ground Combat Center at Twentynine Palms. The sale involves approximately 2,563 acres of school lands and is expected to generate \$806,500 for the School Land Bank Fund. The sale, which the CSLC authorized at its June 29, 2015 meeting, is slated to close before the end of 2015.

California Department of Transportation Land Sale (CSLC File No. SA 5770)

On June 26, 2014, the CSLC received an application from the Department of Transportation to purchase approximately 0.48-acres for the State Highway 247 widening project. This sale closed in November 2014 and \$3,100 was deposited into the School Land Bank Fund.

Accrued Interest on the School Land Bank Fund

A total of \$6,240.00 in interest was generated by the Surplus Money Investment Account to the School Land Bank Fund during fiscal year 2014-15. Interest accruals increased slightly from the previous year due to a higher Fund balance.

Expenses Charged to the School Land Bank Fund

Expenses during fiscal year 2014-15 totaled \$649,344.11. \$330,353.11 of this amount was charged to the Renewable Energy Program, and \$227,575.10 was charged to the Abandoned Mine Remediation Program. \$91,415.90 was charged to statewide administrative services.

**SUMMARY OF REVENUE GENERATED FROM SURFACE
MANAGEMENT PROGRAM - FISCAL YEAR 2014-15**

Surface Rentals:

Surface Rentals:	\$	339,949.38
Timber Sales:	\$	0.00
TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$	339,949.38

SCHOOL LAND BANK FUND

State Parks Land Sale (SA 5763)	\$	2,304,000.00
Caltrans Highway 247 Widening Project (SA 5770)	\$	3,100.00
Accounting Adjustment (SA 5761)	\$	20,000.00
Interest Income (SMIA)	\$	6,240.00

GROSS REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$	2,333,340.00
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EXPENSES:

Statewide Administrative Services (Pro Rata):	\$	-90,299.00
Statewide Administrative Services (Fi\$Cal):	\$	-1,000.00
Program 10 Statewide Administrative Services:	\$	-116.90
Program 10 & Program 20 - Renewable Energy:	\$	-330,353.11
Program 10 – Abandoned Mine Closure Program:	\$	<u>-227,575.10</u>

TOTAL EXPENSES:	\$	-649,344.11
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NET REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$	1,683,995.89
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FISCAL YEAR 2015-16 PLANNED ACTIVITIES

POTENTIAL STATE TEACHERS' RETIREMENT SYSTEM FUND REVENUES

Surface Rentals Income

Staff estimates that rent revenues from existing and new surface use leases on school lands parcels during fiscal year 2015-16 will increase over the prior year due to overall increasing land values. Additionally, staff expended considerable time and effort in the past year gaining approval for higher base rents which had not been revised since 1992. The new base rents became effective on July 1, 2014. The effects of these higher base rents will be seen as older leases undergo the five-year rent review process and are adjusted accordingly.

Timber Harvests

There is potential for income from timber salvage and sanitation operations in fiscal year 2015-16. 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 increase in public awareness and concern about climate change, as well as rising energy prices, staff expects more interest in the long-term leasing of school lands for renewable energy projects. Some projects may involve using wind as an energy source, and may require the installation and operation of wind turbines to generate electricity. Other renewable energy projects proposed on school lands may involve solar technology, such as photovoltaic cells and solar-concentrating systems.

WIND

Staff will continue processing an application for a wind energy lease, known as the Tule Wind Project. The 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 EIR/EIS prepared by the California Public Utilities Commission (as the lead agency under CEQA) and the BLM (as the Lead Agency under NEPA). In December 2011, the BLM issued a Record of Decision authorizing Phase I of the project, which is located primarily on federal lands. Separate authorization from the Bureau of Indian Affairs for development for Phase II of the project on the nearby tribal lands was obtained in December 2013. The proposed development of seven turbines on the school land parcel is included in the proposed

Phase II project. If the project is approved by the CSLC and a lease is issued to allow construction and operation of the wind turbines, staff anticipates significant revenue from this lease beginning in fiscal year 2017-18.

SOLAR

Staff will continue processing two applications for solar energy leases that together would cover approximately 4,641 acres of school lands. The proposed projects, Aurora Solar and Windhub Solar, will be subject to environmental review under CEQA. Both projects are moving forward with preliminary surveys pursuant to the preparation of Environmental Impact Reports. If these solar projects are successfully completed and leases are issued, staff anticipates significant revenue from the leases beginning in fiscal year 2017-18.

POTENTIAL SCHOOL LAND BANK FUND REVENUES AND ACTIVITIES

Applications for the projects discussed below are under consideration and will be processed in fiscal year 2015-16. Staff anticipates new requests for land exchanges and land sales will be submitted throughout the year.

CDPA/BLM Land Exchange (CSLC File No. AD 556)

Prior CDPA land exchanges between the CSLC and the BLM resulted in an unequal balance between the values of the lands 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 to eliminate the outstanding balance and complete the exchange. As part of the transaction, the National Park Service submitted a payment of \$56,492.29 to balance the transaction. This transaction, however, is stalled because the Government Accountability Office issued an opinion in December, 2010 questioning BLM’s authority to use funds from the sale of surplus federal property to complete exchanges with the CSLC. The legal basis for using funds from the sale of surplus federal property to complete the exchanges with the Commission remains unresolved. While the CSLC hopes to complete this transaction during fiscal year 2015-16, it remains uncertain if and when the legal dispute will be resolved. When completed as proposed, staff anticipates a total of \$7,994,925 will be deposited into the School Land Bank Fund.

Heinz Ranch Land Exchange (CSLC File No. 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 for deposit into the School Land Bank Fund. The applicant is attempting to acquire mineral rights, which are required as part of the exchange agreement.

Salvation Mountain, Inc. Land Sale (CSLC File No. SA 5769), Chasterus Foundation Land Sale (CSLC File No. SA 5771) and Slab City Community Group Inc. Land Sale (CSLC File No. SA 5768)

Among the 1,200± parcels of land held within the School Land Bank Fund is a 640-acre parcel near the Salton Sea in Imperial County known as “Slab City”. Originally under the jurisdiction of the CSLC, this parcel was condemned by the federal government and was developed and used for military purposes as part of Camp Dunlap. When Camp Dunlap was deemed to no longer be needed, the Department of Defense cleared the site and the entire parcel was quitclaimed back to the CSLC in 1961. However, numerous concrete building foundations were left in the ground. Over the years, the property slowly became a destination for tourists, intermittent campers, and transients and has experienced a long history of environmental, legal and social issues, including unauthorized occupancy and illegal dumping.

Included in the southwest quarter of the section is a tourist mecca known as Salvation Mountain, which was slowly constructed out of hay bales, stucco and paint over many years by a local resident named Leonard Knight. Since Mr. Knight passed away early in 2014, his monument has been preserved and maintained by the Salvation Mountain, Inc., a non-profit corporation.

Also included within the section and located along the northern perimeter of the parcel is an unauthorized development known as “East Jesus,” which is maintained by a non-profit corporation, Chasterus Foundation. This 30-acre site also was constructed over many years and includes an “artist colony” that purportedly teaches self-sufficiency and sustainable living.

Staff is currently processing three purchase applications: Salvation Mountain, Inc. (southwest quarter), Chasterus Foundation (30 acres), and Slab City Community Group Inc. (remainder of the section), and anticipated bringing these purchase applications to the CSLC for its consideration in fiscal year 2015-16.

United States of America Land Sale (CSLC File No. SA 5767)

Escrow was opened for this sale in September 2015 and the proceeds will be included in next year’s financial summary. The sale will generate \$806,500 for the School Land Bank Fund.

FINANCIAL SUMMARY: FISCAL YEAR 2014-15

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$	339,949.38
Geothermal.....	\$	5,352,254.23
Solid Minerals.....	\$	712,156.66
Oil and Gas	\$	1,427,217.08
GROSS REVENUES.....	\$	7,831,577.35
Less: Geothermal Resource Development Account (GRDA) Deposits	\$	<44,062.43 >
(Public Resources Code Section 3826)		
TOTAL.....	\$	7,787,514.92

EXPENSES: Net Management Costs

Land Management	\$	505,647.99
Geothermal.....	\$	591,118.44
Solid Minerals.....	\$	264,664.40
Oil and Gas	\$	0.00
Ownership Determination.....	\$	11,452.24
GROSS EXPENSES.....	\$	1,372,883.07
Less: Reimbursement Recovery	\$	<122,624.81>
TOTAL EXPENSES.....	\$	1,250,258.26

NET REVENUE TO STRS..... \$ 6,537,256.66

SCHOOL LAND BANK FUND

Balance as of July 1, 2014 (<i>after year-end accounting adjustment</i>).....	\$	730,008.28
Revenue from Land Sales	\$	2,327,100.00
SMIF Interest Earned Fiscal Year 2014-15	\$	6,240.00
Less: Expenses	\$	<649,344.11 >
BALANCE OF FUND AS OF JUNE 30, 2015.....	\$	2,414,004.17

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

ABBREVIATIONS AND ACRONYMS

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
CDFW	California Department of Fish and Wildlife
CDPA	California Desert Protection Act
CDOGGR	California Division of Oil, Gas, and Geothermal Resources
CDPR	California Department of Parks and Recreation
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
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
NPS	U.S. National Park Service
OMR	California Department of Conservation, Office of Mine Reclamation
REAT	Renewable Energy Action Team

RPS	Renewable Portfolio Standard
SDG&E	San Diego Gas & Electric
SMARA	Surface Mining and Reclamation Act
SMIA	Surplus Money Investment Account
STRS	State Teachers' Retirement System
USFWS	United States Fish and Wildlife Service
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 - 2015

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 § 8722, and progress made on a Phase 1 exchange proposal.

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 462,890 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

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(c) of Title 43 of the United States Code.

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

designating the Commission as trustee of the Fund. In enacting the School Land Bank 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 (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 and fiduciary 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.

Status of the DRECP and CDFW consultation

The DRECP Planning Area contains extensive school lands under the Commission’s jurisdiction, and full implementation of the DRECP will affect these lands and the

potential to generate revenue benefiting the State Teachers' Retirement System. Commission staff has actively participated in the DRECP planning process to ensure the Commission's interests and mandated school land development responsibilities are adequately represented in the Plan. Importantly, as required by Assembly Bill 982, this participation has provided 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/>). 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.

In March 2015, after an extensive 5 month public comment period on the draft DRECP and joint environmental impact report/environmental impact statement, the REAT agencies announced a new approach to completing the DRECP. Under the new approach, based on an initial review of public comments submitted by a diverse group of stakeholders, the agencies will proceed in a phased manner to approve the three fundamental components: the BLM Land Use Plan Amendment; federal General Conservation Plan; and the state Natural Community Conservation Plan. According to the REAT, the primary driving force for the decision was feedback from the counties within the planning area requesting additional time and closer coordination with state and federal agencies to ensure better alignment between county planning, renewable energy, conservation and the objectives of the DRECP. Other comments included the need to more clearly outline permitting efficiencies and conservation protections.

Under the phased approach, the agencies will start by completing the BLM Land Use Plan Amendment (LUPA) component of the DRECP that designates development focus areas and conservation areas on its lands, while providing additional time for the state and federal agencies to work with counties and other stakeholders to address issues and concerns with the General Conservation Plan and the Natural Community Conservation Plan components, including the proposed permitting processes. While this phased approach is a departure from the process as initially envisioned, the effect on the land exchange process is minimal, because the Commission and BLM staffs are able to use the existing and proposed designations in the DRECP LUPA to determine a list of parcels to exchange that will meet the mutual goals of adding national conservation lands to BLM's ownership in exchange for adding consolidated lands appropriate for renewable energy to the Commission's ownership.

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 initial proposal requested BLM-owned lands generally located adjacent to or near existing school lands and with high potential for successful development, or those which are located within areas designated in the administrative draft DRECP as Development Focus Areas (DFAs) and have reasonable development potential due to low biological resource conflicts and access to transmission. Commission staff sent a list to BLM of approximately 184,000 acres in 338 parcels of school lands and requested the BLM prioritize the list for acquisition in the exchange. Since then, Commission and BLM staffs have continued to meet regularly to refine the exchange and prioritize parcel selection.

In July 2015, BLM and Commission staffs reached consensus on a Phase 1 exchange proposal framework that consists of approximately 5,600 acres of BLM-owned lands, and approximately 61,000 acres of school lands. Consistent with Assembly Bill 982 and the MOA, the BLM lands include parcels with a high potential for large-scale renewable energy development, including an area with an operating solar facility, and the school lands consist of scattered inholdings located within currently designated BLM wilderness, as well as lands proposed for national conservation landscape designations under the DRECP LUPA. The State parcels are also prioritized according to mineral resource evaluations, with parcels of no or low mineral potential being the highest priority for exchange. This framework proposal was submitted to the BLM Office of Valuation Services, which resulted in a market valuation report that determined, based on a review of available and reported surface values for "solar potential," that the respective value ratio is expected to be about 10:1 (meaning that for every acre of BLM land offered to the Commission, the Commission will need to offer about 10 acres of school lands). Depending on the outcome of the formal land and mineral appraisals on the parcels listed in the exchange proposal, the Commission and BLM may need to make adjustments to the exchange parcel lists in order to equalize the exchange value, prior to moving forward with completion of the transaction. The next step is for the BLM to publish a Notice of Exchange Proposal in the federal register and for the Commission and BLM to execute an Agreement to Initiate a land exchange.

On October 1, 2015, the Commission held a public meeting at which it authorized, and then signed, a Memorandum of Intent with the BLM, represented by the State Director, that memorializes the parties' intent and commitment to expeditiously pursue and complete Phase 1 of the proposed series of land exchanges. This memorandum was a milestone in the exchange process and was important because of the complexity of the process before it could be completed. There are many components involved in completing a land exchange, especially one of this magnitude. Land exchanges typically take a few years to complete, even in the absence of issues or conflicts that may arise throughout the process. Land exchanges also require environmental review and public participation in accordance with the National Environmental Policy Act (NEPA) and the

California Environmental Quality Act (CEQA), as well as Congressional notification, review and approval by the Commission, Department of Justice, and national, state and field office levels of the BLM. In the Phase 1 land exchange, there will be four BLM field offices involved: Ridgecrest, Palm Springs, Barstow and Needles. Interested stakeholders and the public will have an opportunity to review and comment on the proposed land exchange as required by NEPA and CEQA.

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 Chapter 485. For fiscal year 2014-15, expenditures from the School Land Bank Fund attributable to developing the exchange proposal and conducting the necessary coordination with CDFW were \$326,161.32. Revenues resulting from leasing existing and consolidated school lands for the 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. BLM staff estimates the final DRECP LUPA will be released in November 2015 and the record of decision will be issued within the first quarter of 2016; the Phase 1 and potential future phases exchange proposal is included as Appendix Y of that document. Commission staff expects significant progress will be made toward completion of the land exchange by the end of 2016, depending on the duration of any additional permitting and environmental review processes. Because the proposed exchange includes a solar project that is already constructed and operating pursuant to a BLM right-of-way grant, immediately upon completion of the exchange and issuance of a lease to the operator, revenues benefitting the State Teachers' Retirement Fund should realize an increase of approximately \$4,000,000 annually.