

Investment and Development Fund Report

Fiscal
Year

2018-19

Annual review of
Investment and Development Fund
investments on state trust lands

Colorado State
Board of Land
Commissioners



COLORADO
State Land Board

INTRODUCTION

The Colorado State Board of Land Commissioners (State Land Board) presents its annual Investment and Development (I&D) Fund report. As required by Section 36-1-153, C.R.S., this report details FY 2018-19 investments made using I&D funds and the resulting impact on trust assets managed by the State Land Board. The State Land Board is permitted to transfer up to \$5 million of School Trust revenue per year to the I&D Fund to make investments in School Trust assets that anticipate an increase in the value of, and/or income from these assets. Of the \$5 million authorized. The State Land Board may spend up to \$1 million of I&D funds annually on asset maintenance.

This report covers:

- Summary of I&D Fund Investments
- Description of New Investments
- Discussion of Ongoing/Active Investments
- Discussion of Completed Investments

SUMMARY OF INVESTMENT PROGRAM RESULTS FOR FY 2018-19

During the past year, the State Land Board Commissioners approved the use of \$443,500 of I&D funds to support one new project:

- Sherman Creek Ranch Improvements, Phase 2

In addition to the above project, nine investments from previous years continued into this year and six previous-year investments were completed. The State Land Board anticipates that these new and ongoing investments will increase annual revenues by an average of \$82,950 and increase asset value by \$80,000. The six completed investments increased average annual revenue by \$765,000 and increased value by \$4.6 million. **Tables 1** provides additional fiscal detail on all projects. The remainder of this report discusses in greater detail the new investment, ongoing State Land Board I&D investments approved in previous fiscal years, and projects completed this year.

Table 1: Active and Completed I&D Fund Project Analyses

INVESTMENT and DEVELOPMENT FUND
Active Project Analysis Summary as of June 30 2019

| Project Name | Investment Purpose | Year of Investment | Gross Revenue/Value | | | | Benefit | | |
|--|--------------------|--------------------|------------------------|---------------------|---------------------------------|-----------------------------------|--|------------------------------|-------------------------|
| | | | Beginning Income/Value | I&D Funds Allocated | Amount Invested I&D Funds Spent | Estimated Ending Income/Value (1) | Avg. Gross Annual Revenue Increase Over Period | Estimated Net Value Increase | Maintenance Benefit (2) |
| Sherman Creek Ranch Improvements Phase 2 | Maintenance | 2019 | | \$443,500 | \$0 | | | | \$443,500 |
| Chico Basin Ranch Improvements | Maintenance | 2017 | | \$640,168 | \$240,096 | | | | \$640,168 |
| National Hoe Farm Reclamation | Maintenance | 2017 | | \$225,000 | \$203,558 | | | | \$225,000 |
| Chancellor Ranch Assets | Revenue | 2018 | | \$820,000 | \$631,764 | | \$82,950 | | |
| Crow Hill Demolition | Maintenance | 2018 | | \$90,000 | \$79,836 | | | | \$90,000 |
| Lowry Range Asset Management Plan | Value/Revenue | 2018 | \$0 | \$80,000 | \$75,300 | \$80,000 | | \$80,000 | |
| Bohart Ranch Improvements | Maintenance | 2016 | | \$380,579 | \$113,102 | | | | \$380,579 |
| Bald Mountain Commission | Value | 2017 | \$1,573,000 | \$120,000 | \$0 | \$1,693,000 | | \$0 | |
| Brett Gray Infrastructure Improvements | Maintenance | 2016 | | \$997,000 | \$200,931 | | | | \$597,000 |
| Obtain Legal Access State Parcels | Value | 2016 | \$0 | \$300,000 | \$0 | | | | \$300,000 |
| Personnel and Planning (FY 2018-19) | | | | | \$423,046 | | | 12-18% average | |
| | | | \$1,573,000 | \$3,696,247 | \$1,967,635 | \$1,773,000 | \$82,950 | \$80,000 | \$2,376,247 |

Completed Project Analysis Summary for FY 2019

| Project Name | Investment Purpose | Year of Investment | Gross Revenue/Value | | | | Benefit | | |
|---|--------------------|--------------------|------------------------|---------------------|----------------------------------|-------------------------|---|--------------------|-------------------------|
| | | | Beginning Income/Value | I&D Funds Allocated | Amount Invested- I&D Funds Spent | Ending Income/Value (1) | Avg. Gross Annual Revenue Increase Over Analysis Period | Net Value Increase | Maintenance Benefit (2) |
| Hydrate | Revenue | 2016 | | \$550,000 | \$550,000 | | \$585,250 | | |
| 1278 Lincoln Improvements (all phases included) | Value | 2015-16 | \$2,415,400 | \$1,412,000 | \$1,273,515 | \$8,479,779 | | \$4,652,379 | |
| Sherman Creek Ranch Improvements Phase 1 | Maintenance | 2009 | | \$350,000 | \$293,723 | | | | \$350,000 |
| Stock Well | Revenue | 2017 | | \$47,500 | \$42,873 | \$15,480 | \$15,480 | | |
| Lowry Ranch | Revenue | 2014 | \$18,407 | \$420,000 | \$420,000 | \$164,508 | \$164,508 | | |
| Asset Allocation Study | Value | 2018 | \$0 | \$85,000 | \$85,000 | | | \$0 | |
| | | | \$2,433,807 | \$2,864,500 | \$2,665,111 | \$8,744,767 | \$765,238 | \$4,652,379 | \$350,000 |

(1). For all revenue enhancement projects, the amount represented is the first year revenues received from the investment. For value enhancement projects, the number is the estimated value at the completion of the analysis period.

(2). For maintenance projects, any benefit is equal to outlay, unless there is a revenue component that is directly attributable to the maintenance outlay.

NEW INVESTMENTS IN FY 2018-19

Sherman Creek Ranch Improvements, Phase 2

This is a two-part project continuing improvements made to the Sherman Creek ranch in Phase 1. Part one of the new investment creates agriculture and recreation improvements that will maintain lease revenue with revenue increases anticipated over time. The second project improves the ecological condition and function of streams and irrigation ditches on the ranch. The funding provided by the State Land Board for the second project will be

| Project Summary | |
|-------------------------------|------------------|
| Status | Ongoing |
| Estimated Benefit | \$443,500 |
| Year of Investment | 2019 |
| Investment Assumptions | |
| I&D Fund | \$443,500 |
| Other | \$72,000 |
| Total State Land Board | \$443,500 |

matched with grant funds from not-for-profit partners.

ONGOING INVESTMENTS IN FY 2018-19

Chico Basin Ranch Improvements

The Chico Basin Ranch property is an 86,211 acre parcel spanning El Paso and Pueblo Counties. This expenditure is categorized to funds allowed for asset maintenance and is realized across a five-year plan developed with the lessee to prioritize a list of infrastructure improvements that are necessary to maintain and potentially increase the value of the ranch. Improvements will be made on the water distribution systems, fencing and facilities infrastructure.

| <i>Project Summary</i> | |
|-------------------------------|------------------|
| Status | Ongoing |
| Estimated Benefit | \$640,168 |
| Year of Investment | 2017 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$640,168 |
| Other | N/A |
| Total State Land Board | \$640,168 |

National Hog Farm Reclamation

In 1989 the State Land Board issued a 50-year commercial lease to National Hog Farms, Inc. consisting of 5,528 acres of state trust land. In 2000, Colorado voters passed amendments to the constitution that strictly limited the operations of these facilities on state trust land. As a result, National Hog Farms ceased operations at the facility and stopped making payments on their lease. Due to liability concerns, the State Land Board was reluctant to cancel the lease until the resulting contamination of area groundwater was remedied. At that point the State Land Board forgave

| <i>Project Summary</i> | |
|-------------------------------|------------------|
| Status | Ongoing |
| Estimated Benefit | \$225,000 |
| Year of Investment | 2017 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$225,000 |
| Other | N/A |
| Total State Land Board | \$225,000 |

delinquent rent and took possession of remaining site infrastructure in exchange for National Hog Farms retaining liability for any environmental contamination issues. This maintenance expenditure is being used for the purpose of completing site cleanup.

Chancellor Ranch Assets

This project funds maintenance improvements that the State Land Board strategically aligned with a new lease of Chancellor Ranch. The State Land Board issued a Chancellor Ranch lease RFP in late 2015. As directed, RFP respondents submitted bids with an understanding that the State Land Board would invest in the existing improvements on the ranch (fences, water lines and wells, etc.) and repairs to the three homes on site. Upon award of the lease and further investigation by State Land Board staff, it was determined that the homes were in such poor condition that repair and renovation was not feasible and the proper course of action was to demolish the homes. This investment is being used to build two ranch staff residential homes that will replace the homes that were demolished.

| <i>Project Summary</i> | |
|-------------------------------|--------------------------------|
| Status | Ongoing |
| Estimated Benefit | \$82,950 avg annual revenue |
| Year of Investment | 2018 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$820,000 |
| Other | N/A |
| Total State Land Board | \$820,000 |

Crow Hill Demolition

The property is part of an original Section 16 held in the School Trust. It is located directly southeast of U.S. Highway 285 approximately 45 miles southwest of Denver. Improvements on the property include a small house, a large barn, and five outbuildings. All of the improvements are in very

| <i>Project Summary</i> | |
|-------------------------------|----------|
| Status | Ongoing |
| Estimated Benefit | \$90,000 |
| Year of Investment | 2018 |
| <i>Investment Assumptions</i> | |

poor condition. The structures present a nuisance and carry a risk of injury to staff, lessees or trespassers. Regular vandalism and graffiti occurs on the buildings. These funds are being used to remove these structures from the property.

| | |
|-------------------------------|-----------------|
| I&D Fund | \$90,000 |
| Other | N/A |
| Total State Land Board | \$90,000 |

Lowry Range Asset Management Plan

The Lowry Range is a 25,955-acre state trust land property in unincorporated Arapahoe County near the southeastern edge of the greater Metropolitan Denver area. Lowry Range is one of the last large contiguous undeveloped parcels along Colorado’s Front Range. The property’s size, location, significant natural values, and economic value make it unique among State Land Board assets. As a result, more than 21,000 acres (81%) of the Ranch is designated into the Stewardship Trust. The State Land Board has prepared an updated Asset Management Plan for the property to guide leasing and asset management decisions on the property. The plan establishes management priorities and enables the State Land Board to achieve its planned goals in a complex and dynamic financial, environmental, and social context. This expenditure will be used to fund the execution of this plan.

| <i>Project Summary</i> | |
|-------------------------------|---|
| Status | Ongoing |
| Estimated Benefit | \$80,000 in value from \$80,000 in investment |
| Year of Investment | 2018 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$80,000 |
| Other | N/A |
| Total State Land Board | \$80,000 |

Bohart Ranch Infrastructure Maintenance

This project funds maintenance on the 48,000-acre Bohart Ranch located in El Paso County. Due to

| <i>Project Summary</i> | |
|------------------------|-----------|
| Status | Ongoing |
| Estimated Benefit | \$380,579 |

deferred maintenance items, the ranch required substantial investment to bring the property up-to-date and to provide efficient use of its inherent natural resources. This project represents a five-year plan to improve water infrastructure, livestock fences and facilities.

| | |
|-------------------------------|------------------------------------|
| | in value from \$380,579 investment |
| Year of Investment | 2016 |
| Investment Assumptions | |
| I&D Fund | \$380,579 |
| Other | N/A |
| Total State Land Board | \$380,579 |

Bald Mountain Transaction Commission

The Board owns 237 acres five miles west of the City of Boulder. In 2015, the Board directed Staff to pursue the disposal of state trust land encumbered to the County by the Bald Mountain Open Space Park. Subsequent discussions with County representatives determined that the County is only interested in acquiring approximately 146 acres of state trust land. Staff believe the highest and best use of the remaining 91 acres is low density residential development, consistent with the use and character of surrounding properties. Staff recommended that the services of a real estate broker familiar with both this area and the sale of vacant lots for residential development be retained to assist the Board in disposing of these remaining parcels. This I&D investment pays the broker commission.

| | |
|-------------------------------|--|
| Project Summary | |
| Status | Ongoing |
| Estimated Benefit | \$120,000 in value from \$120,000 investment |
| Year of Investment | 2017 |
| Investment Assumptions | |
| I&D Fund | \$120,000 |
| Other | N/A |
| Total State Land Board | \$120,000 |

Brett Gray Ranch Infrastructure

This project funds maintenance on the 49,000-acre Brett Gray Ranch located in Lincoln County. Due to deferred maintenance items, the ranch required substantial investment to bring the property up-to-date and to provide efficient use of site resources. This is a five-year plan to improve water infrastructure, livestock fencing and facilities.

| <i>Project Summary</i> | |
|-------------------------------|---|
| Status | Ongoing |
| Estimated Benefit | \$597,000 increase in value from \$597,000 investment |
| Year of Investment | 2016 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$597,000 |
| Other | N/A |
| Total State Land Board | \$597,000 |

Obtain Legal Access to Trust Parcels

The goal of this project is to acquire legal access to state trust properties that currently lack it. The State Land Board has more than 100 parcels without legal access. The inability to access these properties reduces their value and limits the ability to lease them through competitive bidding. This investment provides initial funding to pursue access to 20 to 30 properties. Based on independent appraisals, the State Land Board believes that gaining access to parcels will generate property value increases of between 12 and 18 percent.

| <i>Project Summary</i> | |
|-------------------------------|---|
| Status | Ongoing |
| Estimated Benefit | Potential 12-18% increase in land value |
| Year of Investment | 2016 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$300,000 |
| Other | N/A |
| Total State Land Board | \$300,000 |

PRIOR INVESTMENTS COMPLETED IN FY 2018-19

Hydro-Ax

The State Land Board generates significant revenue by leasing state trust land for grazing livestock and recreational hunting. Many of the landscapes that support these uses are impacted by increased dominance of invasive juniper on what was historically grassland or grass savannas. Juniper and Piñon pine encroachment can substantially alter the benefits of precipitation on rangeland and can reduce plant cover and productivity. Desirable forage grasses are often the most severely affected.

Historically, the State Land Board has hired independent contractors to remove encroaching juniper and perform sagebrush treatment. However, this approach is inadequate given the scale of the problem and the number of properties that need to be treated. The most efficient way to enhance wildlife habitat and restore the productivity of the land is with mechanical treatments. This method is expected to save \$585,000 in annual costs compared to independent contractors.

| <i>Project Summary</i> | |
|-------------------------------|-------------------------------|
| Status | Complete |
| Estimated Future Benefit | \$585,250 annual cost savings |
| Year of Investment | 2016 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$550,000 |
| Other | N/A |
| Total State Land Board | \$550,000 |

1278 Lincoln Improvements

| <i>Project Summary</i> |
|------------------------|
|------------------------|

These investments provided improvements to the 1278 Lincoln commercial property to encourage new leasing. The 31,000 square foot building had been vacant since August 2014 when a 25-year tenant vacated. While structurally sound, the building’s systems and interior space required complete replacement. This investment makes needed updates and pays for leasing commissions. When improvements are complete, the value of the building is expected to be \$8.5 million.

| | |
|-------------------------------|---------------------------------|
| Status | Complete |
| Estimated Future Benefit | \$2.9 million increase in value |
| Year of Investment | 2015-2016 |
| Investment Assumptions | |
| I&D Fund | \$3.1 million |
| Other | N/A |
| Total State Land Board | \$3.1 million |

Sherman Creek Improvements, Phase 1

This investment was used to make improvements to the existing ranch house and ranch infrastructure and to co-invest with the successful recreation lease bidder to develop recreation opportunities on the Sherman Creek property.

| | |
|-------------------------------|------------------|
| Project Summary | |
| Status | Complete |
| Estimated Benefit | \$350,000 |
| Year of Investment | 2017 |
| Investment Assumptions | |
| I&D Fund | \$350,000 |
| Other | N/A |
| Total State Land Board | \$350,000 |

Stock Well Installation

| |
|------------------------|
| Project Summary |
|------------------------|

Staff identified seven parcels of state trust land that were vacant, due in large part to the lack of a livestock water source. A strong demand exists for small grazing parcels in these regions and recent competitive bidding results suggest that these parcels would generate significant annual revenue, in excess of \$20 per animal unit month, if livestock water were available. Having developed a water source on each parcel, they will be offered to the public for competitive bidding. It is expected that this investment will increase revenue by \$15,480 annually.

| | |
|-------------------------------|-------------------------------------|
| Status | Complete |
| Estimated Benefit | \$15,480 increase in annual revenue |
| Year of Investment | 2017 |
| Investment Assumptions | |
| I&D Fund | \$47,500 |
| Other | N/A |
| Total State Land Board | \$47,500 |

Lowry Ranch

This investment funded the replacement and upgrade of agricultural infrastructure on the 26,000-acre Lowry Ranch property. These improvements include new corrals, fencing and a watering system.

Having made these improvements the State Land Board successfully leased the property to an agricultural lessee through an RFP process. The contracted lease rate is 65 percent greater than the State Land Board’s standard grazing lease rate for land in this region. This lease will generate a total of \$1.6 million in new revenue during its 10-year term.

| | |
|-------------------------------|-------------------------------------|
| Project Summary | |
| Status | Complete |
| Estimated Benefit | \$164,500 in average annual revenue |
| Year of Investment | 2014 |
| Investment Assumptions | |
| I&D Fund | \$420,000 |
| Other | N/A |
| Total State Land Board | \$420,000 |

Asset Allocation Study

This investment was used to hire Callan Associates to perform an asset allocation study looking at both the tangible assets and the financial assets of the ‘Whole Trust’ (land and minerals, commercial properties and the Public School Permanent Fund) and makes recommendations for long-term trust allocation and beneficiary distribution policy. The analysis looked at a variety of alternative asset allocation scenarios to determine ways to increase the value of all assets in the Whole Trust. Historic investment income from the Permanent Fund, for example, has reflected a very conservative asset allocation while more diverse portfolios have returned significantly greater returns. Relatively recent legislation has created a Board to pursue stronger returns from the Permanent Fund, and has provided the authority to invest Permanent Fund assets differently. Callan also evaluated the governance structure for the Board to determine opportunities to be more efficient and effective.

| <i>Project Summary</i> | |
|-------------------------------|---|
| Status | Complete |
| Estimated Benefit | \$85,000 increase in value from \$85,000 investment |
| Year of Investment | 2018 |
| <i>Investment Assumptions</i> | |
| I&D Fund | \$85,000 |
| Other | N/A |
| Total State Land Board | \$85,000 |

Program Costs

Program Expenditures

The statute establishing and governing the Investment and Development fund provides the flexibility to the State Land Board to hire staff and contract for services needed in the management of trust assets. The State Land Board has authorized spending to support 4.0 full-time employees and associated program expenditures to accomplish I&D Fund projects. In FY 2018-19, the State Land Board spent a total of \$423,046 on salaries, business planning and

property valuation activities. These expenditures support increasing the income and the value of all School Trust assets.