

# THE CONSERVATION FUND

*America's Partner in Conservation*

March 21, 2011

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Wildlife Conservation Board  
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## Response to March 15, 2011 letter from the Mendocino Redwood Company

Dear Mr. Donnelly:

I have reviewed the Mendocino Redwood Company's ("MRC") March 15, 2011 letter regarding purported inadequacies in the appraisal used to support The Conservation Fund's 2006 purchase of 16,300 acres of redwood/douglas fir forest in Mendocino County ("Big River II") from Hawthorne Timber Company. As the non-profit organization that led the effort to acquire these properties with the support of the Wildlife Conservation Board, the State Coastal Conservancy, the State Water Board and a prominent California foundation, we write now to address MRC's mischaracterization of the appraisal that supported this transaction. As the following analysis demonstrates, the Big River II appraisal was subjected to extensive prior review that was rigorous and thorough. It documents a very cost-effective outcome for the people of California.<sup>1</sup>

Background. The Big River II appraisal was subjected to an extraordinary level of review. The appraisal was prepared by a member of the Appraisal Institute in accordance with the Uniform Standards of Professional Appraisal Practice - in this case, Chris Bell of Appraisal Associates ("Bell Appraisal"). The Bell Appraisal incorporated an expert timber appraisal prepared by Gene Forsburg of Buena Vista Services ("Forsburg Timber Appraisal"). Although not required by applicable procedures, the Bell Appraisal was, in turn, reviewed by a qualified independent appraiser - in this case, Mark Warren of Warren & Schiffmacher, LLC, also a member of the Appraisal Institute ("Warren Review"). The Warren Review incorporated a review of the Forsburg Timber Appraisal prepared by Stanley Richards of Natural Resource Management Corporation ("Richards Review"). The Bell Appraisal and the Warren Review were thereafter reviewed and approved by the Department of General Services. Finally, in accordance with Control Section 9.45 of the Budget Act of 2005, prior to closing the project was reviewed by the Joint Legislative Budget Committee, the Department of Finance and the Legislative Analyst's Office.

With no analysis other than a short list of "items of note", Sandy Dean, the author of the MRC letter, asserts that the appraisal "demonstrates significant shortcomings" and "fails to credibly defend the price

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<sup>1</sup> Please see attached table "Large North Coast Conservation Transactions (2003-2011)". The Big River II properties are managed by The Conservation Fund. They remain in production and on the tax rolls. Since 2007, logs have been sold to various local mills. The property has been certified as a "well-managed forest" by the Forest Stewardship Counsel and documented as a "Forest of the Future" by the USDA Office of Ecosystem Markets.

paid....” However, a review of the above-referenced appraisals and reviews reveals that the concerns raised in Mr. Dean’s “items of note” are unfounded.

Mr. Dean’s items can be distilled to three basic themes. 1. Harvest levels are unrealistic in light of the properties’ sensitive locations. 2. Publicly funded conservation transactions make poor comparable sales. 3. The “dual use” of the property (timber and real estate sales) is unaddressed. We take each in turn.

Item 1. Harvest levels are unrealistic in light of the properties’ sensitive locations.

Response. The Forsburg Appraisal took the character of the neighborhood into account in determining its estimate of harvestable volumes and the appropriate discount rate for the future cash flows derived therefrom. Further, the Richards Review found that the Forsburg assumptions about volumes, growth and harvest levels were “very conservative”.

The Forsburg Appraisal at page 8 states that “I consider that the subject property, due to its location and characteristics, has relatively high risk of regulatory problems but that risk related to volume recovery has been adequately accounted for by other adjustments I have made”.

The Richards Timber Review at page 3 states that “[t]he assumed annual growth rate of 3% is too low. A more realistic growth rate would have been in the range of 4.0% to 4.5%. The appraiser told the reviewer that he intentionally chose the conservative growth rate....The reviewer estimates that the physical growth which is included in the annual harvest volume *is understated by 25% to 33% per year.*” (Emphasis added.)

Finally, the Richards Timber Review concludes at page 6 that “[t]he appraiser was conservative in estimating each of the variables which are included in the analysis. While such conservatism may have been appropriate for selected components, being conservative to very conservative on each and every one of the value elements results in a serious *understatement* of value.” (Emphasis added.)

Conclusion: The Forsburg Appraisal’s express consideration of the heightened regulatory risk associated with the properties’ location, together with the very conservative assumptions used to establish inventories, harvestable volumes and growth rates clearly refute Mr. Dean’s assertion that the assumed harvest levels were unrealistic.

Item 2. Publicly funded conservation transactions make poor comparable sales.

Response. This is demonstrably inaccurate. Of the five comparable sales used in the Bell Appraisal, the lowest price per acre was The Conservation Fund’s 2004 purchase of 23,570 acres of forestland for \$17,500,000 (\$742/acre) with funding from the State Coastal Conservancy, the Wildlife Conservation Board and private foundations.

Any concern about the use of conservation transactions in the comparable sales analysis was specifically addressed in the Bell Appraisal at page 38: “Often, [conservation organizations] purchase property at a discounted price, with the seller receiving a tax benefit as a charitable donation/contribution. This was reportedly the case with Sale No. 3, which was sold to the Conservation Fund.... The sales price was \$17,500,000... Thus, the sales price of Comparable No. 3 is adjusted upward to the reported market value.<sup>2</sup> *There is some concern that conservation groups are driving the market to ever increasing prices. However, looking at the comparables included in this analysis does not support that theory.*” (Emphasis added.) The Warren Review agreed, stating at page 6 that the adjusted comparable sales approach used by Bell “leads to reasonable value conclusions of \$750 per acre (land value only)...”

Ironically, of the five comparable sales used in the Bell Appraisal, the highest price paid per acre was for MRC’s 2003 Willow Creek sale of 3,373 acres to the Sonoma County Open Space District for \$18,125,000 (\$5,373/acre). In today’s dollars, it remains among the highest prices paid per acre for conservation lands on the North Coast. (Please see attached Table “Large North Coast Conservation Sales”).

Conclusion: The comparable sales used in the Bell Appraisal demonstrate a range of values, with the Big River II value being comfortably in the middle of that range.

Item 3. The “dual use” of the property (timber and real estate sales) is unaddressed.

Response. This assertion is belied by the extensive attention paid to this issue in the Bell Appraisal and the Warren Review.

In its summary of the appraisal problem, the Bell Appraisal addresses this issue at the outset, stating at page 16 that “[t]he main valuation problem for this property is the limited number of recent sales similar to the subject, *the unproven development potential of the subject* and the indicated price fluctuation evident in the neighborhood over the past several years.” (Emphasis added.)

In the detailed analysis of this issue, the Bell Appraisal notes that the Big River properties had a recent history of parcel sales, noting that “[t]he subject properties have been in the Hawthorne Timber ownership [the seller of the Big River II lands] since acquired in December 1999... . [T]here have been several sales of smaller residential parcels in the subjects’ immediate neighborhoods, *including recent sales of lands adjacent to the subject properties*. Several of these sales were owned by Hawthorne Timber as portions of their industrial timber lands. *Timber was harvested from the properties which were then sold as rural residential development properties*. This has been a growing trend as the timber market continues to decline and the rural residential market continues to expand. The most recent sales from Hawthorne Timber are located adjacent to the subject Salmon Creek tract [a component of the Big River II sale], and are scheduled to close escrow in May 2005”. (Emphasis added.)

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<sup>2</sup> \$34,631,000.

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At page 32, the Bell Appraisal states that based on discussions with Gene Forsburg “[i]t is concluded that the subject property could continue to be used as a commercial timber forest while a long-term rural subdivision occurred. Rural parcels of about 160 acres in size could be logged and then split off and sold as rural residential homesites, as has been occurring on and around the subject parcel. Thoughtful logging practices could actually improve many of the rural parcels by opening up viewsheds and developing access roads and homesites, while leaving trees that enhance the aesthetics of the parcels.”

In support of this conclusion, the Warren Review at page 8 notes that “[i]t’s relevant to note as well that a *significant understatement of the harvestable timber [as found in the Richards’ Review] supports the appraiser’s “dual use” hypothesis*; leaving stream zones unharvested, for example, enhances the desirability of to-be-created subparcels for residential use.” (Emphasis added.)

Finally, the Warren Review reached the following conclusion regarding the dual use issue: “There is clearly disagreement among timber valuation professionals as to the appropriate way to deal with highest and best use if conversion of timberlands to residential use is contemplated. The appraiser has addressed the issue and provided reasonable support for his conclusion, which meets USPAP’s required tests.”

Conclusion. Mr. Dean’s assertion that the dual use issue was “unaddressed” rings hollow. The excerpts above indicate that the appraisers and reviewers were keenly aware of the challenges inherent in valuing dual use lands and took pains to reconcile the timber and development values in a prudent and reasonable manner.

Whatever the merits of Mr. Dean’s broader points about the appropriate use of Proposition 84 funds, or how appraisals should be prepared and reviewed, his cursory dismissal of the adequacy of the Big River II appraisal does not support his case.

Please let me know if there is more information you need to ensure the continued prudent administration of WCB’s Forest Conservation Program.

Sincerely,



Chris Kelly

California Program Director

cc: Natural Resource Secretary John Laird

Finance Director Ana J. Matasantos

John McCamman, Chairman, Wildlife Conservation Board

Jim Kellogg, Member, Wildlife Conservation Board

Karen Finn, Program Budget Manager

Sam Schuchat, Executive Officer, State Coastal Conservancy

Sandy Dean, Chairman, Mendocino Redwood Company

Lawrence Seltzer, President and Chief Executive Officer, The Conservation Fund

## Large North Coast Conservation Transactions (2003-2011)

<u>Project</u>	<u>Date</u>	<u>Purchase Price</u>	<u>Acres</u>	<u>Public Grant\$/Acre</u>	<u>Seller</u>
Willow Creek	2003	\$20,785,000	3,900	\$5,329	MRC <sup>1</sup>
Garcia River	2004	\$17,500,000	23,790	\$420	Coastal Forestlands <sup>2</sup>
Big River II	2006	\$48,000,000	16,300	\$960	Hawthorne <sup>2</sup>
Jenner Hdlts.	2009	\$36,000,000	5,630	\$5,684	Gualala Redwoods <sup>2</sup>
Usal (CE)	pending	\$25,500,000	50,000	\$455	RFFI <sup>2</sup>
Gualala (CE)	pending	\$20,000,000	13,900	\$1,366	Coastal Ridges <sup>2</sup>

1. Transferred to State Parks

2. Privately owned, on the tax rolls

CE = conservation easement, all others are fee transactions