

Funding and Financing for Community-Owned Forests

White Paper

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**NORTHWEST
COMMUNITY
FORESTS**



Sustainable
Northwest

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I. Introduction

Whether you are a local resident interested in protecting your drinking water source, county commissioner committed to promoting economic development and quality of life, or nonprofit leader dedicated to conserving working forests, the community forest model offers a template for ownership, management, and governance tailored to your specific needs.

Written for a broad audience, this white paper will interest community members, conservation advocates, and policy makers. This paper also offers a glimpse behind the curtain for funders and donors. Its purpose is to share case studies of how a few community forest efforts in the Pacific Northwest have solved key challenges related to project funding and financing, and how project financing efforts needs to evolve to accommodate interests in growing the community forest model across the region that spans northern California to the Canadian border.

The first part of this paper describes the scale and extent of changes in timberland ownership generally, outlines the history of community forestry, and gives a broad overview of challenges and potential solutions. The second part dives deeper into challenges and potential solutions in the context of the Pacific Northwest. The third part contains three case studies. In our first case study, we share the story of Mt. Adams Resource Stewards, where a rural community takes on a community forest project one small bite at a time. In the second, the Nisqually Story, strong partnerships between land trust, tribal, and agency leaders leads to timely community ownership funded by federal, state, and county sources. In the third, the Usal Redwood Forest uses commercial debt to buy forestland at scale.

Table 1. Case Study Comparison

NAME	LOCATION	SIZE	COST
MT. ADAMS RESOURCE STEWARDS	SE Washington	400 acres	\$850,000
NISQUALLY LAND TRUST	Central Washington	2,000 acres	\$8,000,000
USAL FOREST	Northern California	49,767 acres	\$65,000,000

i. Challenges Posed by Changing Patterns of Timberland Ownership

Since the mid-1980s, the nation's private forests have undergone a dramatic shift in ownership.¹ Previously, most private timberlands were owned by vertically-integrated timber and fiber companies. Today, over 60 million acres of private timberlands are owned by investors and managed through Real Estate Investment Trusts (REITs) and Timberland Investment Management Organizations (TIMOs). Although TIMOs and REITs represent only 1% of private landowners, they own up to 22% of all private timberland in the United States.²

Across the Pacific Coast Region (excluding Alaska), private corporate ownership of forest and woodlands made up an estimated 15.983 million acres (18.6%) out of 85.928 million acres total.³ These private industrial timberlands are among the most productive tree farms in the world due to the favorable growing conditions and commercial value of their timber.

Practitioners note that five factors that influenced changes in forestland ownership.⁴ First, vertically integrated forest products companies learned they could increase profits by spinning off their property management activities and instead specializing in sawmilling. Second, leveraged buyouts led by corporate raiders like Sir James Goldsmith, who orchestrated the sale of assets belonging to Crown Zellerbach and Diamond International, created an atmosphere of uncertainty and risk for companies that might have preferred to retain timberlands. Third, new accounting rules under US GAAP undervalued standing timber assets, making it less advantageous for public companies to hold these assets on their books. Fourth, new creativity in corporate law and the significant tax savings from avoiding taxation at both the corporate and individual level, led timber investors to establish limited liability companies, limited partnerships, or real estate investment trusts. Finally, institutional investors began committing capital to forestland purchases after they discovered that timberland provided a low-risk strategy to diversify portfolios with an asset negatively correlated to the stock market.

The shift in ownership to TIMOs and REITs has had a variety of impacts on regional economies and landscape ecology across the United States. Vertically integrated forest products companies were once known for their strong local connections and a need for a consistent and predictable log supply. The forest products industry is now faced with

¹ Binkley, Clark S. 2007. The Rise and Fall of the Timber Investment Management Organizations: Ownership Changes in US Forestlands. Pinchot Institute for Conservation. <https://www.pinchot.org/files/Binkley.DistinguishedLecture.2007.pdf>

² Butler et al, quoted in Smith, Eric, Lydia Olander, Paul Trianosky, and Andrea Bedell-Loucks. 2016. "Engaging Large Forest Owners in All-Lands Conservation: All-Lands and Large Ownerships—A Conservation to Advance Engagement Workshop, May 8, 2016, Durham, NC." NIP 16-02. Durham, NC: Duke University. <http://nicholasinstitute.duke.edu/publications>

³ Note: Federal ownership made up 46,339,000 acres (53.9%). Butler, Brett J., Jaketon H. Hewes, Brenton J. Dickinson, et al. 2016. USDA Forest Service National Woodland Owner Survey: National, Regional, and State Statistics for Family Forest and Woodland Ownerships with 10+ Acres, 2011-2013. NRS-RB-99. Newtown Square, PA: U.S. Department of Agriculture, Forest Service, Northern Research Station. <https://www.fs.usda.gov/treesearch/pubs/50674>, accessed January 24, 2018.

⁴ For an excellent overview of these issues, see Stein, Peter. 2011. Trends in Forestland OWNERSHIP AND CONSERVATION <http://www.lymetimber.com/media/Stein,%20Forest%20History%20Today-%20Trends%20in%20Timberland%20Ownership.pdf>

increasing uncertainty, especially regarding log supply, and market access to consistent tree size, species composition, and milling infrastructure.

At the same time, environmental groups protest the loss of high conservation value forests to development.⁵ A report by the Washington Department of Natural Resources notes that timberland (excluding national forests) in western Washington declined from 7.7 to 7 million acres from 1978-2001 with conversion for real estate development primarily driven by “the often dramatic disparity between the economic value of forested land for timber production and the much higher value for development.”⁶ The building boom in 2001-2007 and the post-recession recovery 2009-2017 have only intensified the pressure on forestlands near high-growth cities like Seattle and Tacoma. Combined with broader economic, demographic, and political trends, these factors have contributed to the decline of natural resource based economies in the region.⁷

The TIMO/REIT financial model quite usually requires an exit sale to achieve the expected return on investment. Land value appreciation now makes up two thirds of the returns from timberland and MetLife Agricultural Finance predicts weak returns from timber operations and log sales in the near term.⁸ This makes the sale of the property a critical milestone in the lifetime of the investment fund – a period often as short as only five to ten years – leading to further property turnover and fragmentation.⁹ Some experts predict fundamental changes to timberland markets. Jim Hourdequin, CEO of Lyme Timber, notes that investor expectations “have not panned out over the past 10 years.”¹⁰ If investors begin to value timberland based on current income (EBITDA multiples) instead of capital appreciation assumptions, then the cost of timberland might once again be coupled with standing timber and biological growth.

It is important to note that the TIMO/REIT model has also contributed successes to forestland conservation. A small number of investment groups emerged in the early 2000s with the mission of buying threatened timberlands and ensuring their protection in partnership with public agencies and conservation groups. These include Lyme Timber, EFM (formerly known as Ecotrust Forest Management),¹¹ the Conservation Fund, and specialized programs within The Nature Conservancy, The Trust for Public Land, and others. Some

⁵ For an excellent synthesis of these issues, see Forestland for Sale: Challenges and Opportunities for Conservation over the Next Ten Years http://www.osiny.org/site/DocServer/Whitepaper_Mahoosuc_FINAL_web.pdf?docID=2721

⁶ http://file.dnr.wa.gov/publications/em_fwflanduse.pdf

⁷ A future paper will consider the regional differences in funding available between Washington, California, and Oregon. Although Oregon has strict land use laws and a relatively small population, the community forest conversation is also highly relevant in the state.

⁸ Campbell Global, 2016. Timber Trends Issue 170, August 2016. US Timberland Values Positive after Weak Start to 2016. <https://www.campbellglobal.com/education-research/view-timbertrend-document/170>

⁹ Hickman, C. 2007. TIMOs and REITs. https://www.fs.fed.us/cooperativeforestry/library/timo_reit.pdf

¹⁰ <http://www.lymetimber.com/media/2017-05-05%20Hourdequin%20RISI%20London%20Talk%20with%20charts.pdf>

¹¹ For example, Ecotrust Forest Management’s first fund of \$30M reported a 10.6% gross return, with a 1.25% fee between 2004 and 2012, while a commonly referenced timberland investment index reported an 8.17% return during the same period. <https://www.scoop.it/t/timber-invest/?tag=investment+policy>

employ forest management practices that are certified to rigorous third party standards, such as the Forest Stewardship Council (FSC), or less intensive Sustainable Forestry Initiative and American Tree Farm methodologies. Returns are also supported within this niche through the recruitment of concessionary investments, New Market Tax Credit structuring, and other approaches that ultimately stack capital to enhance overall performance of a timber fund.

But the larger problem persists, as these groups tend to offer only interim ownership or bridge loans - the perpetual solution being framed as an exit sale to:

- a) Public ownership and management by state and federal agencies or Tribes, or
- b) Private preservation by non-profit land trusts.

This perpetual solution is the subject of the following sections that describe the challenges and opportunities offered by the Community Forest model.

ii. Solutions Offered by the Community Forest Model

The Community Forest model is gaining popularity in the West as both a potential solution to concerns surrounding the sustainability of forest management and the desire for communities to have a greater voice resource management.¹² Community forests have a long history in the northeastern U.S., where municipally-owned town forests provided a variety of benefits ranging from timber and fiber, recreation, clean water, and other ecosystem services.

Community-based forestry in the United States experienced resurgence with the Seventh American Forest Congress in 1996 and subsequent work of the ‘Communities Committee’ continuing through 2008. In 2007, the Community Forest Collaborative, a partnership between the Trust for Public Land, The Quebec-Labrador Foundation, and the Northern Forest Center, published a manual titled “Community Forests: A Community Investment Strategy.” This work carried through the 2011 publication of “Community Forests: Needs and Resources for Creating and Managing Community Forests,” supported in part by the U.S. Endowment for Forestry and Communities.¹³

Today, the Northwest Community Forest Coalition, which represents over thirty groups – community-based organizations, land trusts, municipalities, counties and regional NGOs – is advancing community forest efforts across the Pacific Northwest.

According to the common definition of the NWCFC:

Community Forests are working forests owned and managed by a local government or by a community-based organization on behalf of a community.

- I. Community Forests provide local control over and enjoyment of the monetary and non-monetary benefits offered by local forest resources.
- II. The acquisition and management structure ensures collaboration and community participation in and responsibility for management decisions.
- III. The community has secure and reliable access to forest benefits that support and reinforce community priorities.
- IV. The conservation values of the forestland ecosystem are permanently protected.

¹² Another significant issue in the West is the decline of timber revenues to counties. Since more than half of the timberland in the West is publicly owned, land trusts in the region have not been as successful in securing funding for timberland conservation as their counterparts in the eastern and lake states. Although some might argue for ‘local control’ (i.e. distributing National Forests to state or county ownership), our purpose is not to endorse this approach, but instead offer a strategy for conservation of private forestland.

¹³ Community forests in New England were recognized as having four critical elements: 1) local ownership and management; 2) community participation in management; 3) secure access to value and benefits of the forest by the community; and 4) conservation values of forests are permanently protected (Definition from the Northern Forest Center).

The NWCFC’s website hosts a map that indicates many forests owned by local jurisdictions, as well as proposed community forests.¹⁴ Still, the Northwest is limited in examples of community forests that meet this definition. Community Forests in the Northwest will progress through both the emergence of new community forest projects and the expansion of existing community forest projects consistent with their respective goals.

iii. Challenges to Scaling Impact

Establishing a new community forest is an endeavor fraught with many challenges, which touch on social, political, community-capacity and financial issues.¹⁵ The proceedings of the third annual Pacific Northwest Community Forest Forum in May 2016 highlighted the need for additional technical resources and investment infrastructure to support the acquisition, financing, and management of timberland by communities.

In a 2017 memo, the Northwest Community Forest Coalition shared five major challenges facing community forest projects:

1. The high cost of timberland in the Pacific Northwest;
2. Limits in the requirements, amounts, and goals of public and private funding for forest acquisition;
3. The sensitivity of finding a balance between conservation and earned income to both repay financing and assure ‘working forest’-related benefits in the long-term;
4. Transaction costs and capacity to close deals; and
5. The effort for overcoming strategic, stakeholder, and governance issues for effective advocacy.¹⁶

Of all the challenges, stakeholders consistently identify funding and finance of community forest acquisition as the most significant barrier.

These challenges play out differently for the small projects typically seen by land trusts, such as donation of a 40-acre estate or purchase of a 200-acre wildlife corridor, and the larger, industry scale acquisitions of 1,000 to 50,000 acres worth \$5 million to \$100 million.

iv. Strategies for “Small” Forest Acquisition

Smaller community forest projects can successfully realize an acquisition with existing grant programs and a motivated community. What constitutes “smaller” depends on the resources

¹⁴ <http://nwcommunityforests.org/about-the-coalition/>

¹⁵ For an excellent overview of the enabling conditions leading to community forest establishment, see the TNC/UW study Urgenson, L., J. Belsky, D. Churchill, B. Borman, J. Bakker, S. Israel, E. Alvarado. April 4 2017. Enabling Conditions and Barriers to Community Forest Development in the Pacific Northwest. Prepared for The Nature Conservancy Washington and Montana State Chapters by the University of Washington and University of Montana.

¹⁶ <http://nwcommunityforests.org/wp-content/uploads/2017/12/SNW-Funding-and-Finance-Problem-Statement.pdf>

of a given community and its partners. The case studies of the Mt. Adams and Nisqually Community Forests tell the story of “small” acquisitions.

Project proponents may work with an intermediary, such as a conservation-oriented TIMO to purchase and hold the property until the groups secure take-out funds. Another option is to pursue a short-term loan (typically 3-5 years) through specialized programs. The Conservation Fund¹⁷ manages one of the most widely used and affordable programs. Portland-based Craft3¹⁸ has also developed options for an Oregon-specific lending tool for land conservation.

Common take-out funding sources include state and federal grants, commercial and concessionary loans, contributions from private foundations and capital campaigns, conservation easements, commercial timber harvest, harvest of non-timber forest products, and ecosystem service payments.¹⁹ At this scale, pre-acquisition diligence costs can present a formidable barrier. To be eligible for public funding, a community often needs to complete a full timber inventory and stand assessment, consult with specialized legal counsel, and demonstrate active community support for the project. Smaller land trusts often rely on philanthropic sources for this pre-development work, whereas regional organizations such as The Nature Conservancy and the Trust for Public Land have internal resources for project development.²⁰ Table 2 outlines a few of the most commonly-used programs and sources.

¹⁷ <https://www.conservationfund.org/our-work/conservation-loans>

¹⁸ <https://www.craft3.org/Borrow/conservation-loans/conservation-bridge-fund>

¹⁹ Note: The UW/UM/TNC study (Urgenson et al. 2017) highlights ‘diverse funding streams’ as Theme 8, summarizing lessons-learned from ps. 80-90.

²⁰ In the Northeast, communities can apply to the Open Space Institute for both project development funding as well as acquisition funding <https://www.openspaceinstitute.org/funds/community-forest-fund>

Table 2. Typical funding sources for acquisition strategies of a smaller scale that are almost always used in some combination to satisfy matching requirements for particular grant programs

Public	Private
Federal	Individual donors
USFS Community Forest Program	Family foundations or funds with connections to the community (sometimes housed at community foundations, such as the Oregon Community Foundation)
USFS Forest Legacy (typically easement)	MJ Murdock Charitable Trust
DOD REPI (easement)	Acres for America (NFWF)
North Am. Wetlands Conservation Act	Conservation Alliance
State	Corporate sponsors with an interest in the project
Washington Salmon Recovery Funding Board	
Washington Wildlife and Recreation Program	
Oregon Watershed Enhancement Board	

Table 3. Sources of Conservation Finance^{21,22,23}

1. Charitable donations
a. Including development offset commitments from for-profit corporations
2. Program related investments (PRI) by charitable foundations
3. Municipal debt (taxable or tax-exempt)
a. General obligation bonds for conservation purposes, passed by ballot initiatives
b. Revenue bonds for specific acquisitions
4. Commercial or municipal debt “subsidized” by a charitable foundation offering a collateralized guarantee to help the acquiring entity access lower-cost credit
5. Larger-scale equity placements (partnering with private capital)
a. Can be “subsidized” through the New Market Tax Credit program
6. Smaller-scale equity investments by community members
7. Ecosystem service payments as an additional revenue stream (e.g. mitigation banking, conservation banking, potential carbon payments, etc.)

²¹ In New England, the Open Space Institute administers the *Community Forest Fund*, a regional granting program that administers funding for community forest acquisition. To-date, OSI reports that the fund has helped preserve over 30,000 acres across 15 community forests. By awarding both capital grants and capacity building grants (<\$30,000) the fund helps leverage significant state and federal match. The fund has raised more than \$2 million to support projects in Maine, New Hampshire, and Vermont.

²² Statutory authority for the Community Forest Bond already exists in Oregon <http://www.usforestcapital.com/portfolio-items/passing-legislation-to-create-a-forest-conservation-bonding-tool/>

²³ Shillinglaw, B., P. Morgan and M. Vaughan. April 13-14, 2007. Financing Community-Based Conservation of Working Lands: Workshop Proceedings. Stanford Law School. <http://docplayer.net/12976757-Financing-community-based-conservation-of-working-land.html>

v. Strategies for Getting to Scale: Moving the Needle

It is common for many Pacific Northwest communities to strive for acquisitions at a scale much larger than the aforementioned sources are able to support in order to have a more significant impact on economic, social and conservation values. Managing forestland at scale (5,000-50,000 acres) offers advantages during the acquisition process as well as in day-to-day operations. First, when deals reach \$20M, diligence, transaction, and closing costs once again approach the 2-4% of the total cost that stakeholders expect from a real estate deal. Second, a forest at this scale produces enough timber, jobs, and other ecosystem services to support ongoing management and stewardship activities.

To overcome the limitations of philanthropy and grant programs, far more sophisticated strategies have emerged. Over the years, practitioners have developed networks to share a taxonomy of conservation finance and best practices. The field of “conservation finance” has sought to connect the private capital markets with investment opportunities that yield conservation gains. The Conservation Finance Network’s ongoing series, the *Conservation Finance Toolkit*,²⁴ offers in-depth resources for practitioners interested in learning more about specific approaches to financing more complex land conservation projects.

The inability to overcome these acquisition funding challenges have not only contributed significantly to the lack of success for a large number of community forest projects, it has also been a roadblock for the emergence of community forest projects at a “meaningful scale” - enough acres of forestland under management in a community-based structure to allow for communities and stakeholders to experience and assess desired changes that are expected from the community forest endeavor.²⁵

For example, one of the first attempts at a community forest acquisition in the Northwest - an effort by the Evergreen Forest Trust, a non-profit established to pursue purchase of what at the time was Weyerhaeuser’s Snoqualmie Tree Farm - formed around a projected \$185M price tag. In another case, the proposed Skyline Community Forest in central Oregon was stalled in 2015 when the property sold to another buyer for \$63M. While the Redwood Forest Foundation’s case study shares the story of a success at this scale, the fact remains that major challenges emerge with larger scale acquisitions.

Communities seeking to acquire forestlands have demonstrated grit, persistence, and creativity in solving these funding and finance challenges. The following section seeks to discuss funding challenges as a whole and highlight specific strategies to create solutions.

²⁴<https://www.conservationfinancenetwork.org/2017/11/27/launching-the-conservation-finance-network-toolkit>

²⁵ Scale challenges were recognized at the 2015 Northwest Community Forest Forum by Tom Tuchmann (US Forest Capital), in commenting that from his experience, most community forest projects struggle to fundraise beyond \$5 million, and the capital necessary for many desired community forest transactions greatly exceeds that amount.

II. Three Case Studies

i. Mount Adams Resource Stewards (MARS)

The Mt. Adams Story: When a rural community takes on a community forest project, one small bite at a time (project that relied entirely on grants/donations to achieve purchase over a protracted timeframe)

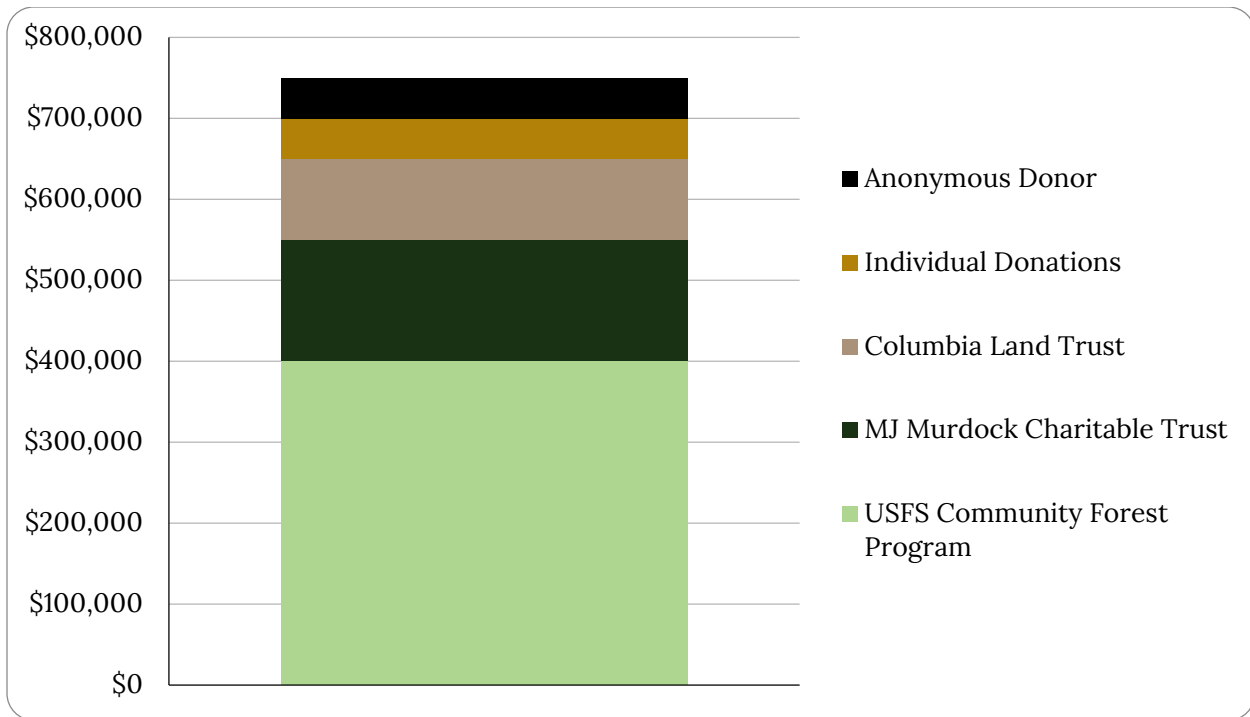
Mt. Adams Resource Stewards (MARS) is a community-based forestry organization that was established in the shadow of Washington's second highest mountain in 2004. MARS is governed by a ten-person board with representation from area business, natural resource, and conservation leaders that oversee activities that range from work with federal forest collaborative groups to developing local markets for woody biomass. The non-profit's founding was in large part due to concerns that many area residents had with changes in ownership to the Klickitat Tree Farm - a historic private forest once comprising over 100,000 acres that straddles Washington's southern Cascade foothills. The tree farm had shaped the identity of several small, unincorporated towns in western Klickitat County since the 1930's while serving as the economic backbone for the area.

A series of ownership changes beginning in 2000 left the Klickitat Tree Farm fragmented into different properties reflecting how one TIMO managed the forest for six different clients. In 2006, one of the clients opted to sell their stake - approximately 15,000 acres - after owning the property for just one year. Until this time, MARS had slowly been organizing efforts around an interest in acquiring portions of the Klickitat Tree Farm for community-based ownership through the non-profit. But the rate of ownership and management changes coupled with transaction costs in the tens of millions of dollars provided no clear opportunity for engagement. The 2006 sale opened a door as a smaller TIMO, Conservation Forestry LLC (CF), was the successful bidder and indicated an openness to working with MARS and other conservation interests in the region. In fact, it was a major part of their business model.

Subsequent years involved more intensive organizing for MARS, including a trip to visit New England community forests involving twelve local representatives and stakeholders, a site prioritization process through open public meetings, and development of a vision and management plan for prospective community forest properties.

ii. *The first campaign*

By 2010, MARS and CF had identified a small initial sale opportunity: a 100 acre tract of land featuring second growth forest, wetlands and most of an old mill pond that had been the site of a mill until around 1930. The price? An affordable \$50,000 largely due to CF's desire to offload any liability associated with the aging, earthen dam that formed the pond. For MARS, the property had been prioritized by the community and it checked out through the due diligence process. Community members and MARS supporters raised the funds through over 80 individual donations that ranged from \$50 to \$10,000 in several months, and the sale closed in 2011.



The initial success and subsequent community response that came through MARS' ownership and management of the property- dubbed the Mt. Adams Community Forest's Mill Pond Tract- quickly inspired a second undertaking. In 2012, MARS and CF signed an option agreement for MARS to purchase the second priority property of lands held by CF: the Pine Flats Tract - 300 acres of highly visible mature ponderosa forest adjacent to a national wildlife refuge and along the county highway linking Glenwood and the neighboring town of Trout Lake. CF set the price at \$800,000 with an initial option for one year. The fundraising process began in earnest immediately, and seemed to be perfectly timed with the US Forest Service's new Community Forest Program's (CFP) first grant cycle - a program that MARS had worked with partners across the nation to shape for years that included a presentation to the Washington Office of the USFS on how the program could work for non-profit ownership, such as that reflected in the Mt. Adams Community Forest structure. The CFP's grants, capped at \$400,000, required at least a 1:1 match of non-federal funds. Unfortunately, in spite of slow but steady progress in raising matching funds from individual donors, MARS was unsuccessful with the CFP's inaugural round of grant making. As the one year deadline on the option approached it became clear that MARS would not have the funds raised in time.

iii. A second close

After some serious soul searching, MARS representatives requested a one-year extension. CF agreed, with the option extension carrying a price tag of an additional \$10,000. Within months, things started to fall into place. An anonymous donor in the local community donated \$50,000. Friends at Columbia Land Trust led a support campaign that raised nearly \$100,000. And the MJ Murdock Charitable Trust granted MARS \$150,000. Combined with smaller foundation grants and many more individual donations, the halfway point was

achieved. Somewhere along the way, US Forest Service CFP representatives communicated to MARS that the Pine Flats proposal was next in-line to be funded and would be covered in the new fiscal year. After over two years of fundraising for a MARS board and staff of two, the Pine Flats Tract of the Mt. Adams Community Forest was closed on in July of 2014.

In late 2015, Conservation Forestry offered the remainder of their Klickitat ownership at auction. MARS unsuccessfully attempted to work with a timber company based in the area that was the successful bidder. Conversations with the company provided MARS a small window to try and secure financing or an interim purchaser of two pieces of what CF had owned. MARS explored the possibility of partnering with a conservation-minded TIMO that would purchase and hold a 2,500 acre tract of the property for resale to MARS, but was unable to reach an agreement that MARS felt provided them a viable path forward. Within several weeks, the terms proposed to MARS by the new owner had been significantly modified, effectively killing the opportunity.

Since, MARS' desire has been to expand on its fundraising capabilities and has been exploring ways by which alternative, interim ownership structures that could house debt and/or private equity from local and regional impact investors interested in the project could enable future community forest properties to be acquired and held until MARS has secured necessary funding. This line of thinking stemmed from a belief that with MARS working more directly with an associated structure for housing an investment they could more efficiently manage a transaction to reduce costs to investors while more creatively designing the final outcome for the project, generating higher income. Net returns to investors would appropriately address risk concerns and a portion of fees for project management would be returned to the community forest project. Another auction of former Klickitat Tree Farm lands led to some exciting progress along these lines. But the attempt fell short due to the time constraints associated with the timberland auction process and the sheer amount of capital necessary to be raised.

Until challenges associated with larger transactions - for MARS, in excess of a million dollars - can be resolved, the Mt. Adams effort continues to focus on cobbling together smaller properties to slowly build the community forest. As of late 2017, MARS is negotiating the purchase of a third property of a couple hundred acres that will add onto the Mill Pond Tract and continue to utilize the fundraising model mixing individual donations with public and foundation grants that has thus far proven successful at this scale.

ii. Nisqually Community Forest

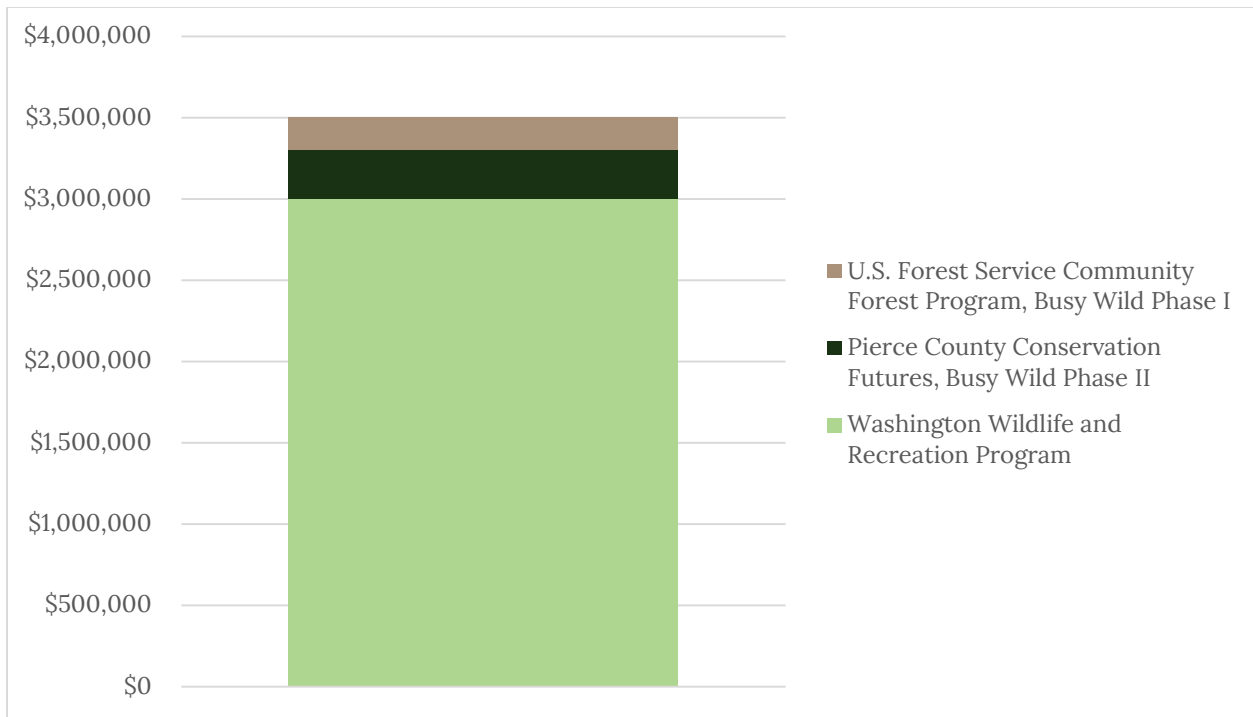
The Nisqually Story - Three Successes and Two Lessons. Strong partnerships between land trust, tribal, and agency leaders leads to timely community ownership funded by federal, state, and county sources.

Reaching from the glaciers of Mount Rainier to the Puget Sound, the Nisqually River Watershed encompasses landscapes and ownerships ranging from national park to private industrial timberlands, the Nisqually Tribe, and Joint Base Lewis-McChord. Privately owned timberlands have historically made up a significant part of the landscape, with large holdings by Weyerhaeuser and other prominent corporations producing logs for domestic industry and export. Today with increasing urbanization along the I-5 corridor between Olympia and Tacoma, ecosystem function, recreation opportunities, and salmon habitat are increasingly seen as priorities for investment.

The Nisqually Community Forest was created through multiple phases from 2011 to the present day. Nisqually watershed stakeholders, including the Nisqually Land Trust, Nisqually Indian Tribe, Nisqually River Foundation, and Northwest Natural Resource Group, convened in 2011 to discuss the future of the watershed's industrial forests. The National Park Service "Rivers, Trails, and Conservation Assistance Program" lent much-needed support for community outreach and planning. The 26-member advisory group was very deliberative in considering goals and ownership structures. In 2013, the group completed its vision report. In 2014 an ownership entity was incorporated and a board of directors created. In 2014, the Tribe completed its Nisqually Steelhead Trout Recovery Plan and identified Busy Wild Creek as a highest-priority area for habitat conservation. In 2014 and 2015 the Nisqually Land Trust and the Nisqually Indian Tribe, using a strategy that identified community forestry as tool for steelhead recovery, won local, state, and federal grant funding to support acquisition of the Nisqually Community Forest's first properties, on Busy Wild Creek (see below). In 2015 the Nisqually Community Forest received 501(c)3 nonprofit status and in the following two years acquired 1,280 acres along Busy Wild Creek, with another 640 acres likely to be acquired in 2018.

iii. Three Successes

The ecological goals of community forestry in the Upper Nisqually are inspired by another challenge to scale: different habitat requirements of Chinook salmon and steelhead trout. Whereas grant money for salmon recovery may be adequate to buy back properties in estuarine and low-level locations with level land, upstream stream reaches ideal for steelhead habitat often have steep slopes. Despite Washington's generous forest practices setbacks of 150 feet, this buffer does little to protect streams on extremely steep slopes with unstable soils. As a result, grant money for conservation can hardly match up to the scale of the properties that would need to be preserved to make a significant impact for steelhead habitat. The goal of increasing buffers and extending rotation length is compatible with community forestry - where working forest conservation goals are integrated with the salmonid recovery program.



At the time, Hancock Timber Resource Group had received a permit to log properties along Busy Wild Creek, but agreed to instead work towards a property sale to the Land Trust, for eventual incorporation into the community forest. Hancock’s business plan for the properties on the Busy Wild included logging and sale.

By successfully closing its Phase I, Busy Wild, acquisition of 640 acres, Nisqually Land Trust positioned itself favorably to acquire these additional properties when they came up on the open market in following years.

Funding sources for Phase I acquisition included the “large cap” category of the Puget Sound Acquisition and Restoration Fund (PSAR, administered by the Washington State Recreation and Conservation Office, RCO), the Washington Wildlife and Recreation Program (RCO), the Washington Salmon Recovery Fund (RCO), Pierce County Conservation Futures (County), and the U.S. Forest Service Community Forest Program[1] (Federal). All of these grant programs are highly competitive, but the RCO PSAR funding is especially so, with three rounds of review and ranking. The \$7 million Nisqually proposal focused on community forestry as a salmon recovery tool and was ranked first in the state. It was also the only PSAR large-cap ask funded by the Washington legislature[JK2] .

In 2017, the community forest acquired its next 640 acres, doubling the size of the forest to 1,280 acres. The vision is to eventually create a working forest of 20,000 to 30,000 acres.

These experiences, and the Land Trust’s 28-year history of land conservation, have built a strong pool of knowledge. Nisqually commissioned Yellow Book Appraisals for each section, with robust cruises and deep analysis of prices and markets. In developing connections with

people who are expert, Nisqually has developed a good feeling of the market, with anecdotal evidence and a broad agreement in general terms of where the market will go.

The Nisqually Land Trust is currently working to add a third section to the community forest. Fee title ownership will likely be held by the Nisqually Tribe and the Land Trust will provide grant funds to match the Tribe's contribution. The repatriation of timberlands and ongoing partnership to pilot community forestry as a salmon recovery tool offers a compelling example of innovation.

iv. Lesson #1

One of the most interesting lessons from the Nisqually story comes from a deal that the Nisqually Community Forest was unable to complete. On a different property, the company Conservation Forestry had bought land from Hancock and held it for 7 years. From the date that Conservation Forestry put the land on the market, Nisqually had 8 weeks to submit a competitive bid. After searching for a partner with adequate financial capacity, Nisqually was able to arrange for a bid in partnership with Lyme Timber and The Conservation Fund. However, the national office at the Conservation Fund (which is a nonprofit conservation organization, and not related to Conservation Forestry, which is a for-profit timber-investment-management organization, or TIMO) had other priorities and it was unclear whether the organization could commit sufficient resources. Initially, the innovation that had enabled the partnership was a loan guarantee from the Conservation Fund that could back Lyme Timber's bid. Finally, it came down to the final week and the parties needed to know with certainty that Nisqually could arrange take-out funding over time. With Washington State's competitive grant cycles, relying on public take-out funding would take time and patience.

Ultimately, the winning bid came in at \$25 million for 5,000 acres. This well outmatched the \$19 million maximum bid that the Conservation Fund's commitment of \$6 million would have helped to underwrite. At \$5,000/acre, this was an incredibly high bid for timberland with significant areas in riparian zones and young, pre-merchantable timber. The winning bidder, Hampton Lumber, drove prices high not to speculate on timberland, but to secure a supply for their mills. Many forest products companies are now worried about losing a log supply for their mills, and with nine mills and over 1,600 employees, Hampton has a strong motivation to secure their future log supply.²⁶

Despite the many impact investors seeking timberland in Washington State, two factors make structuring a deal highly challenging. First, the story above illustrates the need for more easement and related programs that could give private investors the security of a public or nonprofit take-out over the five to seven year life of a fund. Second, high expectations around rates of return have made it difficult to find partners for a bid.

²⁶ <http://www.hamptonlumber.com/our-company/about-us/>

v. Lesson #2

A second story leaves us with new strategies in the toolkit for working forest conservation in Washington State. The Clean Water State Revolving Fund (CWSRF) capitalized through the EPA has been used in other places for forest conservation, but not yet in Washington State. A prominent community forest champion, Paula Swedeen with Washington Environmental Council (WEC),^[2] campaigned with the Washington Department of Ecology to make land conservation eligible for the Clean Water State Revolving Fund loan. In the meantime, Hancock put 16,000 acres in the watershed on the market with a 6-week turnaround on the bid. The property was estimated at \$40-\$50 million based on market comps and transaction experience. The group started scrambling. The Land Trust filled out the loan application and the Nisqually Tribe stepped in as the government entity needed to sponsor the loan.

Ultimately, Nisqually was not sure it could assemble the pieces in time to make a bid. After talking to most of the major conservation-finance organizations, they directly approached the new cohort of impact investors, none of which were prepared to assemble a bid of that scale on such a tight timeline. Other, hybrid, initiatives like The Nature Conservancy have designed impact vehicles that might be a better match, but they had not yet assembled the cash to bid. Finally, Nisqually talked to several private timber companies that have acted as “bridge” owners on conservation purchases, but all of them indicated that the deal was way outside the scale of what they could afford unless they had certainty about take-out financing.

What was originally valued at \$40-\$50 million is widely believed to have finally sold for well over \$60 million (the final sales price has not yet been released publically) - which would set a new record and bring up the average timber price in the region to at least \$3,750/acre (including large areas of non-harvestable land). At this price, the Land Trust fears that the new owners will be forced to maximize and accelerate harvest of merchantable timber in the upper watershed. This poses an existential threat to salmon stocks that are already within one or two bad years of extinction. The first few years of the community-forest project have seen timberland values grow to wildly speculative heights. Put in perspective with other real property trends, like the San Francisco real estate market where housing prices continue to rise, it may well be possible that these new high prices set the floor for future valuations.

This second story also illustrates the need for more readily-deployable tools and a long-term timeframe. The Community Forest and the Nisqually Tribe were ultimately successful in their application for a \$14 million loan at 1% interest - an ideal match for working forest conservation - but now need a place to put the money to work. Compared with the 10-year time horizon of most timber investment funds, the 100+ year perspective of the Land Trust and the Tribe offers a truly patient window for long-term restoration.

Although not specifically mentioned as a funding source for Busy Wild, the Nisqually Land Trust has been one of the first organizations in the U.S. to benefit from a direct carbon offset project with a corporate partner. In 2016, Microsoft purchased 38,000 carbon credits from

the land trust's Mount Rainier Gateway Reserve.²⁷ Should either Washington or Oregon pass cap and invest legislation in the 2019 session, specific set-asides for investing in forest health could offer much-needed funds for carbon.

Of the three sections, the Nisqually Land Trust plans to let the youngest stands grow for at least another 15 years before beginning timber operations. With a present need for pre-commercial thinning harvests to release large trees for healthy growth, Nisqually plans on transitioning forest stands from a 35-40 year to a 85-100 year rotation. Although the timberland might be "just ok" for growing trees, it makes excellent community land. A well-used cross country ski trail traverses the property and its location at the entrance to Mount Rainier contributes to the viewshed for the entire tourism corridor. The Land Trust will employ local contractors for restoration activities across the 1,280 acres now under community-forest management and continues to employ them across an adjoining 2,500 acres it manages strictly for wildlife habitat recovery. And it is hoping to increase the size of the forest to make a bigger impact on the regional economy.

²⁷ <http://nisquallylandtrust.org/land-trust-makes-history-with-microsoft-carbon-deal/>

iii. Redwood Forest Foundation Usal Redwood Forest

The Usal Redwood Forest - using commercial debt to buy forestland at scale at a unique moment in time.

The Redwood Forest Foundation, Inc.'s *Usal Redwood Forest* is a 49,767 acre community forest located in the Coastal Redwood Region of Northern California. Formerly forested with redwood trees, the region is now dominated by second-growth Douglas fir and tan oak. The property is held by the Usal Redwood Forest Company (URFC), a wholly-owned for-profit subsidiary of the parent nonprofit. The property is managed according to Forest Stewardship Council (FSC) standards.

RFFI was established in 1997 by a local forester and a county commissioner who sought collaborative solutions in the wake of the 'timber wars' that pitted environmentalists against loggers. At 49,767 acres, the Usal Forest is the largest²⁸ community forest on the West Coast and its establishment demonstrates the use of debt financing at scale. Nonprofits eligible for grants and donations typically have great difficulty accessing commercial banking and loan products. RFFI created a hybrid structure by filing to incorporate a for-profit subsidiary with the purpose of sustainable, working forest management - the Usal Redwood Forest Company (URFC).²⁹

iv. *A shared vision*

RFFI spent ten years building a shared vision around community forestry before identifying a suitable acquisition opportunity. Working with the Portland-based firm U.S. Forest Capital LLC³⁰ as its transaction advisor, RFFI was able to overcome its first hurdle: finding a property owner willing to sell to a conservation buyer. The property, located in Mendocino County just north of Fort Bragg, was owned by Hawthorne Timber Company and managed by The Campbell Group. With its 150-year history of timber harvest and its management by a professional company, the 50,635 acre property was well surveyed and had consistently generated financial returns. However, the seller was not interested in donating any part of the property. With an appraised value of \$65 million, the property was far more expensive than could be paid for with a single round of foundation or private fundraising. This presented a compelling challenge: how could RFFI acquire forestland at scale?

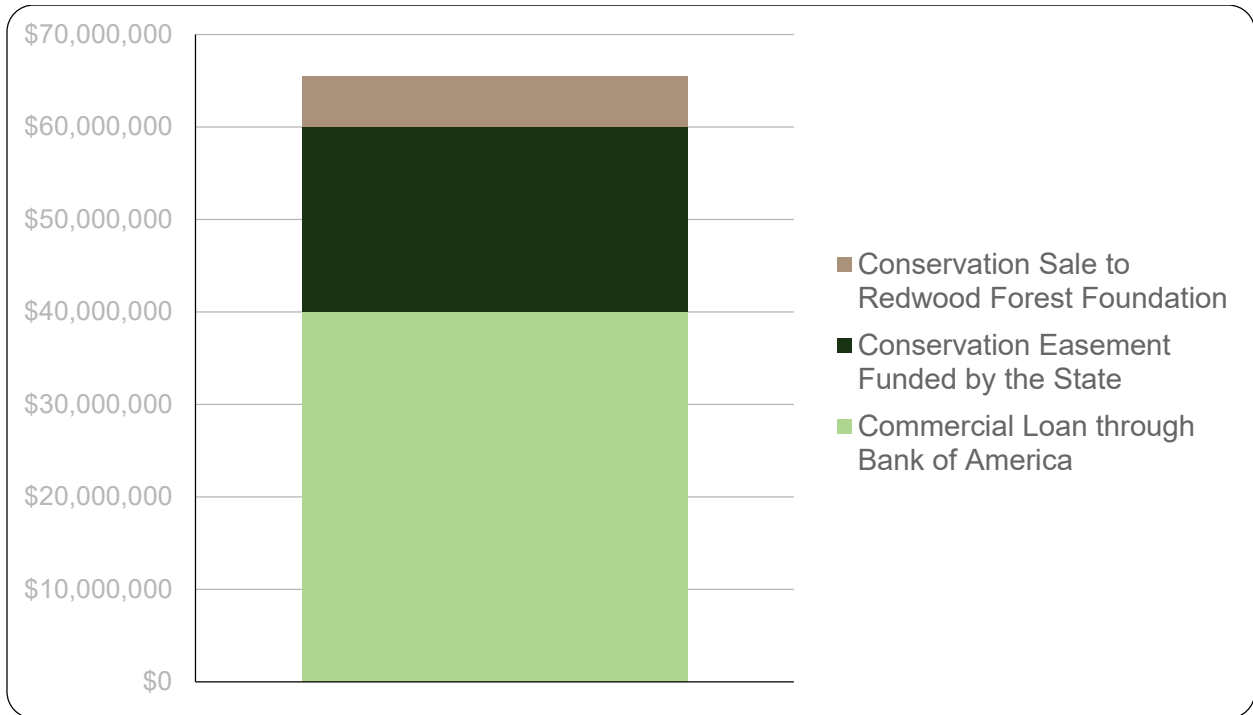
Because the property had a 100+ year history of harvest as timberland, the property was attractive from the point of view of underwriting and commercial real estate lending. In addition, the timber management firm was well known and respected within the financial

²⁸ The Usal is the largest *non-state-owned* community forest. The Teanaway Community Forest is 50,241 acres and was acquired by Washington State for \$100 million in 2013. http://www.dnr.wa.gov/publications/em_tcf_managementplan.pdf

²⁹ Source notes: RFFI's website <http://www.rffi.org/> has all of this information in an easy-to-read format, including a PDF of its Forest Management Plan. In conjunction with the newspaper articles written about the project, the Usal Forest is one of the most well-documented examples of Community Forest establishment.

³⁰ <http://www.usforestcapital.com/>

community, making financing easier to arrange. The loan from Bank of America was structured to allow for an 8-year period without logging. The debt financing consisted of 2 tranches, enabling the complex transaction and timeline. The first had typical debt characteristics and the second tranche had equity-like characteristics.



v. *Combining multiple sources of funding*

Initial repayment was then funded through the sale of conservation easements, carbon credits, and timber. The loan from Bank of America was structured creatively to enable URFC to negotiate and close on the entire property first - before selling the conservation easement and carbon credits. This contrasts with other examples where a bridge buyer like TPL or TNC purchases the property and patiently waits before the local community forest entity or agency has raised the funds. The structure allowed RFFI to compete to acquire the property using the bridge loan that would be repaid from proceeds of the easement sale.

The Usal Redwood Forest is a success story from the perspective of combining multiple sources of conservation finance. The Conservation Fund acquired the conservation easement for \$20,000,000 funded in part by California’s Wildlife Conservation Board approval of \$19,500,000 in funding. A portion of the property, the Shady Dell grove of candelabra redwoods (957 acres) was sold to the Save the Redwoods League for \$5.5 million. This sale of a ‘preservation parcel’ allowed the board to recoup some of their initial investment, while divesting of a forest stand that no one wanted to see logged. By 2017, RFFI had registered over 4 million tonnes of carbon offsets. A new forest product - biochar - produces revenues through the business North Coast Biochar. Biochar also provides a market to help subsidize restoration treatments that remove tanoak.

vi. Enabling conditions

U.S. Forest Capital, LLC's Tom Tuchmann notes several defining characteristics that enabled the deal to move forward. First, the governance structure of RFFI created a reliable decision-making body that could negotiate on behalf of the community. Many 'community' efforts struggle because the community in question lacks an empowered entity with decision making authority. By inviting diverse stakeholders to sit on the board of RFFI, the organization created an organized, legally accountable structure for decision making. A corporation (either for-profit or non-profit) also holds a key ability not available to informal associations - capability to take part in real estate transactions. Prior to closing in 2007, the Redwood Forest Foundation began outreach so that the following year the Board could launch a series of community meetings hosted by the Community Advisory Group (15 local and regional residents including activists, artists, sawmill operators, foresters, recreation, and others). This process informed the drafting of a forest management plan to FSC standards.

Second, RFFI had a long-term commitment to managing for timber, but also had bought time to establish its forest management plan. The purchase was completed in 2007 and the financial crisis occurred the following year. The crisis underscored the point that all financial models are wrong the date they are completed. Most TIMOs have lumpier cash flows than projected, due to the cycles in the market, and in good years they have to cut hard to repay investors.

Hybrid legal structures can offer advantages and allow a community to buy land at scale, however they may complicate initial establishment. RFFI's corporate structure - a parent non-profit corporation with a for-profit subsidiary the Usal Redwood Forest Company - allows it to access financing and grants not available to a single entity, but does complicate filing and legal compliance. The nonprofit's initial application to the IRS was rejected because of the inclusion of timber harvesting as an activity. Today, the Usal Forest continues to be a regional role model and example of a large community forest. The foundation initially retained a well-known timberland manager to steward the property, however the long-term goal has always been to bring on its own forestry expertise. In 2017, RFFI hired a chief forester and will continue to grow its internal capacity.

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