

CALIFORNIA STATE LANDS COMMISSION

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

Fiscal Year 1999-2000

CALIFORNIA STATE LANDS COMMISSION

Cruz M. Bustamante, Lieutenant Governor
Kathleen Connell, State Controller
B. Timothy Gage, Director of Finance

Paul D. Thayer, Executive Officer

Submitted to the Governor, the California Legislature,
and the State Teachers' Retirement System

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INTRODUCTION

The California State Lands Commission (CSLC), through its State School Lands Management Program (Program), manages approximately 478,000 acres of school lands held in fee ownership by the state and the reserved mineral interests on another 790,000 acres of school lands where the surface estate has been sold by the state.

Management of the Program is divided between the Land Management Division (LMD) and the Mineral Resources Management Division (MRMD) within the CSLC. The LMD has the responsibility for the Surface Management Program, under which all surface resources on school lands are administered, excluding mineral activities. The MRMD oversees the Geothermal and Minerals Programs under which the school lands geothermal, mining activities, and oil and gas leasing are administered.

Management guidelines directing the Commission's program are found in the Public Resources Code (PRC). PRC Sections 8700-8716 created the School Land Bank Fund and directed the lands be proactively managed to provide for an economic base and the generation of revenue for support of the public school system. PRC Section 6217.5 directs all net revenues derived from the use of school lands be deposited in the State Treasury to the credit of the Teachers' Retirement Fund, benefiting the State Teachers' Retirement System (STRS). The Commission serves as trustee for STRS. The trust creates a fiduciary relationship between the Commission (trustee) and STRS (beneficiary), and obligates the Commission to make the school lands productive (primarily in financial terms) for the retirees, beneficiaries and disabled membership of STRS. This fiduciary responsibility includes protection of the corpus of the trust asset as well as the generation of revenue.

In establishing the School Land Bank Act, the Legislature made specific findings and declarations emphasizing the development of school lands "into a permanent and productive resource base" and that "all transactions, including exchanges, sales and acquisitions [be implemented] for revenue generating purposes."

The Program's emphasis has been: 1) continuation of implementation of the California Desert Protection Act Exchange Program, 2) maximization of revenues from school lands assets, and 3) managing uses of the school lands while ensuring protection of the environment. The CSLC's management costs for the Program in Fiscal Year (FY) 1999-00 were \$1,048,339.60. Net revenue transferred to the California State Teachers' Retirement System (STRS) was \$4,432,927.75. Net revenue deposited to the School Land Bank Fund was \$3,836,237.56, resulting in a fiscal year end balance of \$34,806,765.95. (See "Financial Summary: Fiscal Year 1999-00" on page 31.)

The preparation of the *Annual Staff Report on the Management of State School Lands* is required by PRC 6477. However, Government Code Section 7550.5 (Chap. 970, Stats. of 1996) amended PRC 6477 so that no report was required

of the CSLC for FY's 1996-97 through 1998-99, but that beginning October 1, 1999, reports would again be required. For continuity purposes, a portion of this report has been devoted to a brief update of Program activity from FY 1996-97 through 1998-99, with a more detailed report format for FY 1999-00.

The major activities for each of the Program components for FY 1999-00, as well as activity summaries for FY's 1996-97 through 1998-99, are described in the following pages.

SURFACE MANAGEMENT PROGRAM

The objectives of this program are to actively manage uses on school lands to generate revenues, enhance local economies, assure ongoing viability of the resource, and protect the environment. This is accomplished by devising management and development techniques for optimum land management, which will result in maximizing the economic return to the STRS and School Land Bank Funds.

The Surface Management Program oversees all surface activities on school lands, excluding mineral activities. This includes surface leasing for various purposes such as rights of way for oil and gas pipelines, transmission lines, and grazing, in addition to the management of approximately 37,000 acres of timberland. The Surface Management Program is also responsible for the sale of school land parcels to public and private entities. Land sales produced revenue of \$2,053,381.56 this fiscal year. Accrued interest on the School Land Bank Fund for the fiscal year was \$1,782,856.00. Surface rentals and timber harvests generated \$965,330.00 of gross revenues. (See "Summary of Revenue Generated From Surface Management Program: Fiscal Year 1999-00" on page 10.)

Over the past five years, there has been a significant turnover of staff within the Surface Management section of the School Lands Program. Of the four staff in the Program, all have left either through retirement or separation as of November 2000. With the loss of experienced staff, LMD transferred two skilled employees from other units to continue the efforts of the Surface Management Program.

UPDATE: CALIFORNIA DESERT PROTECTION ACT OF 1994

On October 31, 1994, the California Desert Protection Act (CDPA) was signed into law by the President (Public Law 103-433). The CDPA designates 3.6 million acres located in southern California as wilderness to be administered primarily by the Bureau of Land Management (BLM), and 4 million acres as additions to the National Park Service (NPS) system. The purpose of the CDPA is to set aside areas in the California desert to protect the natural, cultural, scenic, and historical values, and to provide for the public enjoyment. The Act provides for the exchanging out of California school lands inholdings within these designated areas for other federal lands.

The process to compensate the state for the monetary impact of the CDPA on school land parcels is clearly defined. The CSLC will receive compensation for the "taking" of its fee and mineral interests on a value-for-value basis determined by fair market appraisals. Compensation for the state's assets may be made in various forms, e.g., cash, exchange for other lands, and/or by periodic payments of identified income streams. There are no provisions in the CDPA, however, to compensate the CSLC for staff time or contracts needed to implement the Act. Funding allocated for the Surface Management Program has remained relatively stable since the inception of the CDPA.

To date, three CDPA land exchange transactions are complete. The first, 5,646 acres valued at \$992,686.00, was transferred to the BLM in September of 1996. The second, 800 acres valued at \$144,000.00, was completed in June of 1997. The third and most recent, an exchange of 57,309 acres, was facilitated by the CSLC's acquisition and subsequent sale to the city of Pomona of a 100-acre federal government surplus parcel located in the city of Pomona. The resulting transaction was completed in November 1997 and was valued at \$13,155,120.00. While the previous transactions were "all cash", and resulted in deposits to the School Land Bank Fund, the Pomona sale was accomplished by the CSLC carrying a note secured by a deed of trust. Principal reduction payments made on the note are deposited to the School Land Bank Fund while interest payments are transferred to the STRS Fund.

Negotiations are continuing on a fourth CDPA transaction. This transaction will be structured similarly to the city of Pomona sale referenced above, but will involve federal surplus land in the City of Downey. It is anticipated the transaction will involve over 100,000 acres of CSLC school lands and have a total value of \$20 million.

Upon the completion of the City of Downey land exchange, there will be approximately 85,000 remaining acres of CSLC lands within the designated areas for the CSLC to transfer to the BLM.

SUMMARY OF FISCAL YEARS 1996-97 THROUGH 1998-99 ACTIVITIES

Summaries of the revenue generating surface management activities for FY's 1996-97 through 1998-99 are provided in a table format on the following three pages.

SUMMARY OF REVENUE GENERATED FROM SURFACE MANAGEMENT PROGRAM: FISCAL YEAR 1996-97

STRS FUND

Surface Rentals & Timber Harvests:

Surface Rentals:	\$ 315,356.27
Timber Harvests:	\$ 53,216.03
TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$ 368,572.30

SCHOOL LAND BANK FUND

Land Sales:

Todd Land Sale (94 ± acres) Revenue generated:	\$ 6,650.00
Cadiz Land Company/Pergola Property Land Sale (1,280 acres) Revenue generated:	\$ 252,021.00
Bradley, Trustees, Land Sale (43.61 acres) Revenue generated:	\$ 13,105.00
Camp Land Sale (80 ± acres) Revenue generated:	\$ 55,555.00
Southern California Edison Land Sale (12.38 acres) Revenue generated:	\$ 8,400.00
Bureau of Land Management/Pomona Land Exchange/Sale – Principal reduction payment Revenue generated:	\$ 1,136,686.00
Kern River Gas Transmission & Mojave Pipeline Companies Revenue generated in lieu of mitigation lands:	\$ 729,217.40
Miscellaneous Revenue Processing and patent Fees:	\$ 722.00
Total:	\$ 2,202,356.40
Accrued Interest on the School Land Bank Fund:	\$ 869,492.70
TOTAL GROSS REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$ 3,071,849.10

SUMMARY OF REVENUE GENERATED FROM SURFACE MANAGEMENT PROGRAM: FISCAL YEAR 1997-98

STRS FUND

Surface Rentals & Timber Harvests:

Surface Rentals:	\$ 209,428.92
Timber Harvests:	\$ 7,277.01

Total:	\$ 216,705.93
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Interest Income from Investments:

Total interest earned from note held on land sale transaction to city of Pomona:	\$ 235,900.00
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TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$ 452,605.93
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SCHOOL LAND BANK FUND

Land Sales:

California Department of Parks & Recreation Land Sale - Ocotillo Wells State Vehicular Recreation Area (160 acres) Revenue generated:	\$ 18,000.00
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Bureau of Land Management/Pomona Land Exchange/Sale – Principal reduction payment Revenue generated:	\$ 5,775,596.00
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Miscellaneous Revenue Residual interest earned on Kern River Gas Transmission & Mojave Pipeline Co. Land Sale completed in FY 1996-97:	\$ 16,196.22
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Total:	\$ 5,809,792.22
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Accrued Interest on the School Land Bank Fund:	\$ 1,179,578.20
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TOTAL GROSS REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$ 6,989,370.42
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SUMMARY OF REVENUE GENERATED FROM SURFACE MANAGEMENT PROGRAM: FISCAL YEAR 1998-99

STRS FUND

Surface Rentals & Timber Harvests:

Surface Rentals:	\$ 226,889.45
Timber Harvests:	\$ 3,800.00

Total:	\$ 230,689.45
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Interest Income from Investments:

Total interest earned from note held on land sale transaction to city of Pomona:	\$ 464,654.00
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TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$ 695,343.45
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SCHOOL LAND BANK FUND

Land Sales:

Scaroni Ranch Land Sale Revenue generated:	\$ 4,145,600.00
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Bureau of Land Management/Pomona Land Exchange/Sale – Principal reduction payment Revenue generated:	\$ 1,539,184.00
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Total:	\$ 5,684,784.00
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Accrued Interest on the School Land Bank Fund:	\$ 1,356,768.60
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TOTAL GROSS REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$ 7,041,552.60
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FISCAL YEAR 1999-00 ACTIVITIES

CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM (STRS) FUND REVENUES

The total revenue deposited into the STRS fund this fiscal year was \$1,353,924.96. This money was generated from the following transactions:

Surface Rentals

Rent received from approximately 140 revenue generating leases totaled \$178,615.17.

Timber Sale (Fourthwater Creek Fire Salvage Sale)

In 1999, the CSLC authorized staff to conduct an emergency fire salvage sale, known as the Fourthwater Creek Fire Salvage Sale, to salvage dead timber that resulted from a fire that burned through a 200-acre parcel of school lands within the boundaries of the Plumas National Forest. Over 95 percent of the standing timber was killed. The revenue derived from the sale of the salvaged timber offset costs of the salvage operation and restocking costs. Net revenues received totaled \$786,714.83.

Income from Investments

The CSLC authorized staff to carry notes for the cities of Shasta Lake and Pomona for two separate land sale transactions. Interest on the city of Shasta Lake's note for this fiscal year totaled \$16,834.96. The city of Pomona's interest payment was in the amount of \$371,760.00. The total revenue received from these payments was \$388,594.96.

SCHOOL LAND BANK FUND REVENUES

Revenue from the sale of school land parcels totaled \$2,053,381.56 from the following transactions:

California Department of Parks and Recreation

This sale to the California Department of Parks and Recreation (CDPR) in Imperial County involved five school land parcels totaling 2,642.70 acres. The land was incorporated into the Ocotillo Wells State Vehicular Recreation Area. Revenue generated from this transaction totaled \$800,000.00.

City of Shasta Lake

This transaction conveyed two parcels of school land in Shasta County totaling 135 acres to the city of Shasta Lake for the purchase price of \$275,000.00. The

property will be used for the city to maintain its existing water distribution lines on the property and for the possible expansion of an existing regional park. The CSLC agreed to carry a note secured by a deed of trust for the city of Shasta Lake. A down payment was made in the amount of \$55,992.56.

Lassen County

One 6.4-acre parcel of school land in Lassen County was sold to Lassen County for the purpose of road access. Revenue generated from this transaction totaled \$2,975.00.

Bureau of Land Management/CDPA

The city of Pomona made a principal reduction payment in the amount of \$1,194,164.00.

Miscellaneous Revenue

Miscellaneous processing and patent fees in the amount of \$250.00 were received and deposited into the Fund.

**SUMMARY OF REVENUE GENERATED FROM SURFACE
MANAGEMENT PROGRAM: FISCAL YEAR 1999-00**

STRS FUND

Surface Rentals & Timber Harvests:

Surface Rentals:	\$ 178,615.17
Timber Harvests:	\$ 786,714.83

Total: \$ 965,330.00

Interest Income from Investments (interest earned on notes held on land sale transactions):

City of Shasta Lake:	\$ 16,834.96
City of Pomona	\$ 371,760.00

Total: \$ 388,594.96

TOTAL GROSS REVENUE GENERATED TO STRS FUND: \$ 1,353,924.96

SCHOOL LAND BANK FUND

Land Sales:

Lassen County Land Sale (6.4 acres) Revenue generated:	\$ 2,975.00
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California Department of Parks & Recreation Land Sale - Ocotillo Wells State Vehicular Recreation Area (2,642.70 acres) Revenue generated:	\$ 800,000.00
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City of Shasta Lake Land Sale Revenue generated:	\$ 55,992.56
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Bureau of Land Management/Pomona Land Exchange/Sale – Principal reduction payment - Revenue generated:	\$ 1,194,164.00
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Miscellaneous Revenue Processing and patent fees:	\$ 250.00
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Total: \$ 2,053,381.56

Accrued Interest on the School Land Bank Fund: \$ 1,782,856.00

**TOTAL GROSS REVENUE GENERATED TO SCHOOL
LAND BANK FUND: \$ 3,836,237.56**

FISCAL YEAR 2000-01 PLANNED ACTIVITIES

POTENTIAL CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM (STRS) FUND REVENUES

Income from Investments

As a result of the last CDPA land exchange/sale transaction, income generated from the interest earned on the note that the CSLC is holding for the city of Pomona has been, and will continue to be, responsible for much of the income growth of the STRS Fund. The anticipated closing of the City of Downey transaction, early in 2001, should support further growth in this investment income category.

The potential also exists for additional timber income in the upcoming year. As in years past, the inevitable fire, high wind, or insect/disease infestation may yield income from timber salvage and sanitation operations. The extent of this potential income is unknown at this time.

Barstow Property

The CSLC acquired approximately one acre of land abutting school lands with commercial development potential from the California Department of Transportation (Caltrans) in April of 2000. The CSLC now holds a potential development site of approximately 34 acres at the intersection of Interstate 15 and L Street in Barstow. Staff anticipates commencing the Request for Proposal (RFP) process to develop this property. From the development, staff expects to produce a significant income stream to the STRS Fund.

POTENTIAL SCHOOL LAND BANK FUND REVENUES

Bureau of Land Management/CDPA

The exchange activity for the CDPA is ongoing and should continue for several more years. The following two items are current CDPA exchanges:

City of Downey

Negotiations are continuing on a proposed four-party exchange between the BLM, General Services Administration (GSA), CSLC, and the City of Downey. The CSLC will take title to approximately 98 acres of federal GSA surplus land (a former NASA site) in exchange for comparable value of school lands, in accordance with the CDPA. The City of Downey will purchase the acquired land from the CSLC pursuant to the School Land Bank Act for \$20 million. The current proposal includes an \$18 million note and deed of trust to be carried by CSLC, with the interest earned on

this note being deposited into the STRS Fund. The \$2 million principal down payment will be deposited into the School Land Bank Fund.

44 Parcel Exchange

As part of the on-going CDPA land exchange program, efforts are being made to identify federal mineral potential lands to be exchanged for CSLC inholdings. One such exchange consists of 44 federally owned parcels in Kern County that include oil and gas mineral potential. These BLM administered parcels will be exchanged for CSLC inholdings of comparable value contained within national parks, preserves, or BLM wilderness areas.

Amargosa Canyon

Negotiations are scheduled to begin with the BLM, the NPS, and a private third party regarding an exchange of a 640-acre school land parcel in the Amargosa Canyon area of Inyo County. This is not an exchange dictated by the CDPA. BLM is interested in this land for inclusion into the federal Amargosa Canyon Natural Area because the area is environmentally sensitive. Its inclusion would benefit the Natural Area by expanding its boundaries. To facilitate this exchange, the current proposal calls for the participation of a private third party who owns land within the Death Valley National Park boundary. This third party would acquire the school land parcel and then complete a land exchange with the BLM and NPS. This will result in eliminating the private inholding in Death Valley. NPS would have jurisdiction over the inholding. Additionally, the 640-acre school land parcel would be transferred to the BLM and administered by it as part of the Amargosa Canyon Natural Area.

Town of Apple Valley

Negotiations have commenced regarding the sale of 160 acres of school land in the Town of Apple Valley, San Bernardino County. The town seeks this land for development of a private regional distribution center that will bring a large number of jobs and growth to the local economy.

California Department of Parks and Recreation

A proposed three-party exchange in Mendocino County involves a privately owned 130-acre parcel sought by CDPR that is within the Standish Hickey State Recreation Area. The owner of the 130-acre parcel is seeking to exchange it for a 120-acre landlocked CSLC owned parcel near the town of Potter Valley. To facilitate this acquisition, a transaction is proposed in which the CSLC would receive cash for the 120-acre school land parcel of forested land, the CDPR would acquire the Standish Hickey inholding, and the private party would receive the 120-acre parcel.

Metropolitan Water District of Southern California (MWD)

MWD proposes to acquire a 200-acre parcel of school land in Riverside County. The purpose of this acquisition is to include this parcel into the Hayfield Groundwater Storage Program.

San Bernardino County

The San Bernardino County Public Works Department is interested in acquiring a road right of way along the north boundary of a 40-acre school land parcel in San Bernardino County. The county's preference is to purchase the fee interest over a 40-foot strip of land.

Dyer Mountain

A proposed ski resort in Plumas County includes a 480-acre school land parcel. Negotiations are currently under way for lease, exchange, sale or combination thereof.

Investment Studies

Staff has initiated investment studies to review and analyze potential investment alternatives for School Land Bank Funds. These studies will include analyzing agricultural land investments as well as financing a potential office building development along the north coast of California for the purpose of housing state agencies.

United States Forest Service

On June 30, 1987, the CSLC authorized a Memorandum of Understanding between the CSLC and the Pacific Southwest Region of the United States Forest Service (USFS). This agreement facilitated the exchange of forested lands to consolidate land holdings and benefit both agencies. Phase 1, which included CSLC holdings in southern California, was completed in 1990. Phase 2 has been delayed due to required federal cultural and archaeological studies. These studies have been recently completed and this second phase of the exchange can now move forward. In this phase, the CSLC will exchange northern California inholdings for approximately 1,640 acres of land containing an estimated 55 million board feet of timber in Butte County.

GEOHERMAL, MINERAL, AND OIL AND GAS PROGRAMS

The objectives of these three programs are to manage the development of geothermal, mineral, and oil and gas resources on state school lands, to maximize royalty revenue derived from them, and to ensure that environmental protection and public safety issues are considered.

With respect to the Geothermal Program, the state owns a reserved mineral interest in 7,500 acres of school lands at The Geysers geothermal field in Sonoma and Lake Counties of which 5,563 acres are currently under lease. As the largest such development in the world, The Geysers field is now celebrating its 40th anniversary of harnessing clean, environmentally-friendly geothermal steam to generate electrical power. The field has a capacity of 1,000 megawatts, enough to supply one million homes with electricity. About 25% of The Geysers' output is derived from the 5,563 acres of school lands under lease, with the balance from leases on federal or privately owned lands. Calpine Corporation, the largest independent power company in the U.S., owns and operates most of the steamfield and power plant facilities at The Geysers. Calpine is also presently the lessee of the current eight state geothermal leases at The Geysers, after having obtained all other geothermal lease interests by early 1999.

SUMMARY OF FISCAL YEAR 1996-97 ACTIVITIES

Geothermal Program at The Geysers

Royalty revenue increased to \$3,114,442.41, up approximately \$93,603 from the prior year. Much of the increase resulted from lessee Unocal Geothermal's strategy of offering steam to Pacific Gas and Electric (PG&E) at competitive market prices during off-peak hours to minimize curtailment. Another state lessee, Calpine, drilled a new well which boosted production and royalty from its state lease. The state's other lessee, Central California Power Agency (CCPA), shut down its operations in early 1996. Staff was unable to find a replacement lessee.

Staff continued its effort to assist operators in securing a supply of water for injection to recharge the geothermal reservoir and prolong its life. After 35 years of steam withdrawal, portions of the reservoir had become dried out and pressure depleted. The reservoir rock, however, still contains a tremendous amount of heat (450°F), and injection of water into the rock results in the creation of new steam.

Staff continued to follow the construction of the Southeast Geysers Effluent Pipeline (SEGEP) that would bring treated wastewater from Lake County to The Geysers which would eventually positively impact adjacent state leases by enhancing steam productivity and quality.

Staff also increased its active role in promoting a similar project, the Santa Rosa Geysers Recharge Project (SRGRP). SRGRP water would be distributed to a number of Unocal injection wells, the majority located on state leases, in the central and northern part of the field. The SRGRP pipeline was one option being considered by the city of Santa Rosa for the long-term disposal of its wastewater.

Mineral Prospecting and Lease Management

At the beginning of FY 1996-97, there were four active mineral prospecting permits all of which were for precious metals. Three of these four permits were adjacent to areas that either had current precious metal production or were in an area previously mined for gold and silver.

During this period, one mineral extraction lease was renewed to U.S. Borax. Two new mineral prospecting permits were issued, one each to Lot 42 Mining and Naxos Resources. Two permit extensions were granted, one to American Girl Mining and one to Viceroy Gold Corporation. Revenues generated from the mineral extraction leases totaled \$166,924.15.

During 1996-1997, an agreement was reached with Granite Construction to settle a 1/16th reserved mineral interest the state has in the Indio Quarry area of Riverside County. Negotiations occurred with Pacific Coast Minerals to re-establish a 1/16th mineral agreement for mining to occur at a feldspar quarry in San Bernardino County. Staff processed a quitclaim deed for an aggregate mineral extraction lease for Baldwin Contracting Company of Chico, California.

Also during this period, a settlement was reached in the trespass investigation with Kasler Construction Company in the amount of \$7,000.00 for unauthorized extraction of aggregate in San Bernardino County.

Mineral Evaluations for the California Desert Protection Act

Work continued on the mineral appraisal of approximately 630 state school land parcels enveloped in wilderness to be managed by the BLM and NPS as a result of the passage of the CDPA. During this fiscal year, 190 mineral evaluations were performed with a combination of office and limited field work.

Oil and Gas Revenues

Revenue from two school land oil and gas leases generated \$25,523.77 during FY 1996-97. This revenue remained consistent with that realized in FY 1995-96 of approximately \$21,000 with minor fluctuation due to oil prices.

SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL, MINERAL, AND OIL & GAS PROGRAMS: FISCAL YEAR 1996-97

STRS FUND

Geothermal Royalties and Net Profits:

Unocal Geothermal, Inc. leases at The Geysers: PRC's 4596, 4597, 6422, 6423	\$ 2,186,736.03
CCPA leases at The Geysers: PRC's 5217, 5820, 5821, 7751	\$ 508,300.08
Calpine Corp. leases at The Geysers: PRC's 5206, 7810	\$ 275,499.04
Net Profits from Calpine Corp. lease: PRC 5206	\$ 104,989.09
Silverado Geothermal, Inc. lease at The Geysers: PRC 7845	\$ 38,918.17
Geothermal Total:	\$ 3,114,442.41

Mineral Royalties:

Total from five leases in Inyo, Napa, Riverside, San Diego, and Yolo Counties:	\$ 166,924.15
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Oil and Gas Royalties:

Total from two leases, one in Kern County, and one in Ventura County:	\$ 25,523.77
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TOTAL GROSS REVENUE GENERATED TO STRS FUND: \$ 3,306,890.33

SUMMARY OF FISCAL YEAR 1997-98 ACTIVITIES

Geothermal Program at The Geysers

Royalty revenue increased to \$3,223,061.14, up from the previous year's revenue by \$108,618.73. The increase resulted primarily from the continued efforts of staff to support Unocal's steam marketing strategy. Additional revenue amounting to \$31,660.16 was collected as interest on royalties for prior production held in suspense during resolution of a steam-pricing dispute with Calpine.

In late 1997, the 26-mile SEGEP pipeline began operation, and staff began monitoring its impact on production operations at The Geysers. Staff also continued its work with geothermal operators and other agencies to promote the SRGRP. As a result, the city of Santa Rosa selected the SRGRP as its wastewater disposal option. Staff estimated that augmented water injection could yield an additional \$13 million in royalty from state leases from 2001 to 2020.

Mineral Prospecting and Lease Management

During this fiscal year, two mineral prospecting permit extensions were granted, one to Naxos Resources and one to Lot 42 Mining. The revenues generated from the existing mineral extraction leases amounted to \$130,544.96.

Mineral Evaluations for the California Desert Protection Act

During this fiscal year, 26 mineral evaluations were performed with a combination of office and limited field work.

Oil and Gas Revenues

The two school land oil and gas leases generated \$18,539.35 this fiscal year. This was down by approximately \$7,000 from the previous fiscal year.

SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL, MINERAL, AND OIL & GAS PROGRAMS: FISCAL YEAR 1997-98

STRS FUND

Geothermal Royalties and Net Profits:

Unocal Geothermal, Inc. leases at The Geysers: PRC's 4596, 4597, 6422, 6423	\$ 2,421,547.02
CCPA leases at The Geysers: PRC's 5217, 5820, 5821, 7751	\$ 0
Calpine Corp. leases at The Geysers: PRC's 5206, 7810	\$ 463,230.03
Net Profits from Calpine Corp. lease: PRC 5206	\$ 284,762.07
Silverado Geothermal, Inc. lease at The Geysers: PRC 7845	\$ 53,522.02
Total:	\$ 3,223,061.14
<u>Other Royalties:</u>	
Interest Earned on Disputed Geothermal Royalty	\$ 31,660.16
Geothermal Total:	\$ 3,254,721.30
<u>Mineral Royalties:</u>	
Total from five leases Inyo, Napa, Riverside, San Diego, and Yolo Counties:	\$ 130,544.96
<u>Oil and Gas Royalties:</u>	
Total from two leases, one in Kern County, and one in Ventura County:	\$ 18,539.35
TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$ 3,403,805.61

SUMMARY OF FISCAL YEAR 1998-99 ACTIVITIES

Geothermal Program at The Geysers

Royalty revenue increased to \$3,677,822.73, up from the prior year's total by \$454,761.59. The increase resulted primarily from the continued efforts of staff to support Unocal's steam marketing strategy and a new method for the valuation of the state's geothermal resources at The Geysers. The new method, designed by staff and later adopted on federal and private leases, was necessary because the lessee, Calpine, assignee of Unocal's leases, consolidated ownership and operations at the field in early 1999 by purchasing both the leasehold interests of Unocal and the power plant facilities of PG&E and others. The new method established the value of the steam for royalty purposes as a certain percentage of the gross proceeds derived from the sale of electricity generated from the steam. That percentage started out at 36%, but increases over a five year period to 42%.

With respect to water injection, staff continued to monitor the impacts of augmented water injection at The Geysers from SEGEP. Data provided by geothermal operators clearly showed a reduction in production decline rates, improvements in steam quality, and most importantly, an increase in electrical generation from the southeast part of the field. Staff began discussions with Calpine regarding its plans to utilize additional injection water from the SRGRP, particularly as it impacts the future productivity of state leases.

Mineral Prospecting and Lease Management

At the end of FY 1998-99, there were five active mineral extraction leases. During this past fiscal year, the leases generated \$199,906.19 in revenue from sand and gravel and borates extractions and lease rentals.

During this period, one mineral prospecting permit extension was granted to Lot 42 Mining and two new mineral prospecting permits were issued, one to Deloro Minerals and one to Santa Fe Pacific Gold Corporation. The permit to Santa Fe authorized drilling to determine the extent and possible value of precious metal mineralization on the newly acquired parcel adjacent to the existing Mesquite Gold Mine in Imperial County. The parcel was acquired from the BLM as part of the CDPA program.

Mineral Evaluations for the California Desert Protection Act

During this fiscal year, 28 mineral evaluations were performed with a combination of office and limited fieldwork. In April 1999, a Memorandum of Agreement was entered into between the CSLC and the BLM for the state to acquire 44 parcels of land from the BLM that have potential for the development of oil and gas

resources. In exchange, the CSLC will convey to the BLM inholdings within the confines of the CDPA of a mutually agreed-upon value. This acquisition is expected to be completed in FY 2001-02. In addition, the CSLC has expressed an interest to the BLM to acquire approximately 15,000 acres of other BLM lands that have potential for oil and gas development in exchange for CDPA lands of comparable value.

Oil and Gas Revenues

Revenues generated during this fiscal year amounted to \$15,098.08, down approximately \$3,400 from the previous fiscal year.

SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL, MINERAL, AND OIL & GAS PROGRAMS: FISCAL YEAR 1998-99

STRS FUND

Geothermal Royalties and Net Profits:

Unocal Geothermal, Inc. leases at The Geysers: PRC's 4596, 4597, 6422, 6423	\$ 2,571,135.02
CCPA leases at The Geysers: PRC's 5217, 5820, 5821, 7751	\$ 0
Calpine Corp. leases at The Geysers: PRC's 5206, 7810	\$ 314,324.08
Net Profits from Calpine Corp. lease: PRC 5206	\$ 728,681.21
Silverado Geothermal, Inc. lease at The Geysers: PRC 7845	\$ 63,682.42
Geothermal Total:	\$ 3,677,822.73

Mineral Royalties:

Total from five leases in Inyo, Napa, Riverside, San Diego, and Yolo Counties:	\$ 199,906.19
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Oil and Gas Royalties:

Total from two leases, one in Kern County, and one in Ventura County:	\$ 15,098.08
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TOTAL GROSS REVENUE GENERATED TO STRS FUND: \$ 3,892,827.00

FISCAL YEAR 1999-00 ACTIVITIES

Geothermal Program at The Geysers

Royalty revenue increased to \$3,926,966.09, resulting in a \$249,143.36 increase over the revenues generated in FY 1998-99. The increase is attributable to the new method for valuing steam resources on state leases, negotiated the prior year by staff, and efficiency improvements realized from Calpine's consolidation of steamfield and power plant operations at The Geysers.

On the downside, CCPA, holder of four leasehold interests in school lands, who shut down operations in 1996, obtained the California Energy Commission's final approval of a project closure plan, and began issuing contracts for the well abandonment, plant demolition and surface restoration work. Despite the actions of CCPA, staff held discussions with CCPA and Calpine on the possibility of re-directing steam from certain state wells that had been supplying the CCPA power plant to one of Calpine's power plants. Unfortunately, these discussions were not successful and staff reluctantly approved the plugging and abandonment of the seven steam wells drilled into CCPA's four state leases. CCPA submitted formal quitclaim deeds for its 1,450 acres of school lands leases.

Early in 2000, the city of Santa Rosa began construction of the 41-mile SRGRP pipeline, and Calpine began detailed plans for its injection water distribution system. Staff continued its discussions with Calpine concerning the optimal utilization of this injection water at The Geysers. The SRGRP plans to be operational in 2002.

Mineral Prospecting and Lease Management

Revenue for this fiscal year was \$149,529.98. At the end of the year, there were five mineral extraction leases, and one mineral prospecting permit. Santa Fe Pacific Gold Corporation's permit was extended for one additional year and assigned to Newmont Gold Company. Approximately 150 exploratory drill holes have been completed and a preferential lease application has been filed to develop a portion of the property as part of an expansion of the Mesquite Mine. The Imperial County Planning Department and the BLM are in the process of preparing a joint Environmental Impact Report/Environmental Impact Statement for the project.

The mineral exploration drilling program performed by Naxos Resources in the Death Valley Junction was not pursued further. Lot 42 Mining likewise allowed its mineral exploration permit to expire at the end of May for a mineralized property located in the Cargo Muchacho Mountains of Imperial County. Deloro Minerals completed a geologic mapping and surface-sampling program on a school land parcel north of Bodie State Park that appeared promising. A drilling program was proposed by Deloro to define the mineral potential of the parcel to

determine if any ore existed. Due to strong environmental opposition, Deloro withdrew its application.

A negotiated mineral extraction lease application was received for the mining of a small talc deposit in San Bernardino County in conjunction with adjacent federal mining claims. The county is currently processing environmental documentation.

An application from San Elijo Ranch was filed with the CSLC to modify the state's right of surface entry on a portion of a patented school land parcel in San Diego County as part of a large housing development.

Mineral Trespass Settlement

It was discovered that the Sigma Stone company's Black Angel Mine in San Bernardino County has been producing aggregate on a parcel where the state owns the minerals and the operator owns the surface. Following lengthy discussions with the mine owner, an application for a negotiated mineral extraction lease was filed with the CSLC and is being processed.

Mineral Evaluations for the California Desert Protection Act

Work continued, albeit at a slower pace, on mineral evaluations necessary for the CDPA exchange program. Only 14 mineral evaluations were completed in the fiscal year. Other CSLC work precluded satisfactory progress and a request was made and approved to hire one additional mineral engineer.

Oil and Gas Revenues

Revenues for the two existing oil and gas leases increased in FY 1999-00 to \$107,631.70, up substantially from the \$15,000+ earned the prior year. The increase resulted from oil prices more than doubling and production increasing more than threefold.

Approximately 99% of the revenue is derived from the 160-acre state school land parcel located in the Round Mountain Field of Kern County which has been producing since the 1920's. MacPherson Oil Company is the current operator. The second parcel located on seven acres in the Sulfur Crest area of the Santa Paula oil field of Ventura County produced approximately one percent of the revenue with approximately \$1,000 per year in royalties.

SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL, MINERAL, AND OIL & GAS PROGRAMS: FISCAL YEAR 1999-00

STRS FUND

Geothermal Royalties and Net Profits:

Calpine subsidiary leases at The Geysers: PRC's 4596, 4597, 6422, 6423	\$ 2,999,226.03
CCPA leases at The Geysers: PRC's 5217, 5820, 5821, 7751	\$ 0
Calpine Corp. leases at The Geysers: PRC's 5206, 7810	\$ 272,033.01
Net Profits from Calpine Corp. lease: PRC 5206	\$ 589,662.02
Silverado Geothermal, Inc. lease at The Geysers: PRC 7845	\$ 66,045.03
Geothermal Total:	\$ 3,926,966.09

Mineral Royalties:

Total from five leases in Inyo, Napa Riverside, San Diego and Yolo Counties:	\$ 149,529.98
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Oil and Gas Royalties:

Total from two leases, one in Kern County, and one in Ventura County:	\$ 107,631.70
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TOTAL GROSS REVENUE GENERATED TO STRS FUND: \$ 4,184,127.77

FISCAL YEAR 2000-01 PLANNED ACTIVITIES

Geothermal Program at The Geysers

Staff estimates the state's royalty revenue from its school lands geothermal leases at The Geysers will reach \$5 million in FY 2000-01. This is the highest total since FY 1993-94, and is a direct result of the new royalty method negotiated by staff which ties the steam's value to the value of the electrical power generated from it. To enhance the state's future royalty revenue, staff plans to work with Calpine on the following goals: (1) to develop state acreage already under lease but not fully developed, (2) to negotiate terms for re-leasing acreage quitclaimed by CCPA and adjacent unleased state acreage, (3) to improve the utilization of available steam resources through optimization of steamfield and power plant operations, (4) to facilitate the construction of a distribution system for SRGRP injection water, and (5) to select well conversion candidates for optimal injection benefits. Finally, staff plans to continue its on-going efforts to monitor all production operations and engineering projects on state leases and adjacent lands, verify all pricing and royalty calculations, and look for opportunities to increase royalty revenue from school lands at The Geysers geothermal field.

Mineral Prospecting and Lease Management

Staff expects increased revenue for this fiscal year resulting from major projects that began last year and as a follow-up to approximately 50 mineral inquiries and trespass investigations received during the year. Staff reached a settlement this year with Black Angel Mine for an aggregate trespass. Black Angel Mine will pay the state approximately \$65,000 over a 12-month period beginning January 1, 2001. In addition, the settlement will provide the state with a steady income stream of about \$50,000 per year from continued mineral royalties. It is anticipated that the Protech Minerals talc lease to be considered by the CSLC in the second half of the fiscal year will provide an additional mineral royalty of about \$10,000 per year. Staff also anticipates the CSLC to consider and approve, in the second half of this fiscal year, leasing of acreage acquired adjacent to the Mesquite Mine as part of the CDPA. Anticipated royalties are estimated to be approximately \$50,000 per year for a five-year period beginning with FY 2001-02.

Mineral Evaluations for the California Desert Protection Act

A newly hired Associate Mineral Resources Engineer will assist in accelerating progress on mineral appraisals for the CDPA exchange program. Over 100 mineral evaluations will be performed this year involving both office and field work. The 44 BLM tracts with oil and gas potential may be transferred to the state as early as the fourth quarter of this fiscal year or early in FY 2001-02.

Oil and Gas Revenues

It is expected that oil and gas revenues from the two school land leases will decrease slightly as oil prices are not anticipated to stay at their current high level. However, substantial royalties should be received in comparison to prior fiscal years as oil and gas leases benefit from higher energy prices.

The following four pages contain the Financial Summaries
of the entire Program for
FY 1996-97 through FY 1999-00.

FINANCIAL SUMMARY: FISCAL YEAR 1996-97

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$ 315,356.27
Timber	53,216.03
Geothermal	3,114,442.41
Minerals	166,924.15
Oil and Gas	25,523.77
TOTAL	\$ 3,675,462.63

Less: Geothermal Resource Development Account (GRDA) Deposits	<\$21,015.73>
(Public Resources Code Section 3826)	

TOTAL \$ **3,654,446.90**

Expenses: Net Management Costs

Land Management	\$ 585,301.49
Geothermal	299,041.92
Minerals	209,552.96
Oil and Gas (includes Elk Hills evaluation and legal services)	63,628.93
Ownership Determination	10,523.78
TOTAL	1,168,049.08

Less: Reimbursement Recovery	<15,005.58>
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TOTAL \$ **1,153,043.50**

NET REVENUES TO STRS FUND: \$ 2,501,403.40

SCHOOL LAND BANK FUND

Balance as of July 1, 1996	\$13,941,018.88
SMIF Interest Earned FY 1996-97	869,492.70
Revenue From Land Sales	2,202,356.40
Less: Real Estate Consultant Contracts	<11,601.95>

BALANCE AS OF JUNE 30, 1997 \$ **17,001,266.03**

FINANCIAL SUMMARY: FISCAL YEAR 1997-98

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$ 209,428.92
Timber	7,277.01
Geothermal	3,223,061.14
Minerals	130,544.96
Oil and Gas	18,539.35
Income from Investments (Interest Paid on Notes)	235,900.00
Interest Earned on Geothermal Suspense Fund	31,660.16
TOTAL	\$ 3,856,411.54

Less: Geothermal Resource Development Account (GRDA) Deposits	<\$25,675.55>
(Public Resources Code Section 3826)	

TOTAL \$ 3,830,735.99

Expenses: Net Management Costs

Land Management	\$ 557,515.49
Geothermal	337,096.17
Minerals	205,755.13
Oil and Gas	25,460.63
Ownership Determination	75,985.98
TOTAL	\$ 1,201,813.40

Less: Reimbursement Recovery	<9,903.39>
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TOTAL \$ 1,191,910.01

NET REVENUES TO STRS FUND \$ 2,638,825.98

SCHOOL LAND BANK FUND

Balance as of July 1, 1997	\$17,001,266.03
SMIF Interest Fiscal Year 1997-98	1,179,578.20
Revenue From Land Sales	5,809,792.22
Less: Real Estate Consultant Contracts	< 28,270.71>

BALANCE AS OF JUNE 30, 1998 \$23,962,365.74

FINANCIAL SUMMARY: FISCAL YEAR 1998-99

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$ 226,889.45
Timber	3,800.00
Geothermal	3,677,822.73
Minerals	199,906.19
Oil and Gas	15,098.08
Income From Investments (Interest Earned from Notes)	464,654.00
TOTAL	\$ 4,588,170.45

Less: Geothermal Resource Development
Account (GRDA) Deposits

<\$49,265.54>
(Public Resources Code Section 3826)

TOTAL \$ **4,538,904.91**

Expenses: Net Management Costs

Land Management	\$ 622,669.19
Geothermal	344,298.24
Minerals	199,327.61
Oil and Gas	6,821.98
Ownership Determination	30,804.44
TOTAL	\$ 1,203,921.46

Less: Reimbursement Recovery

<29,230.58>

TOTAL \$ **1,174,690.88**

NET REVENUES TO STRS FUND \$ **3,364,214.03**

SCHOOL LAND BANK FUND

Balance as of July 1, 1998	\$23,962,365.74
SMIF Interest Earned Fiscal Year 1998-99	1,356,768.65
Revenue From Land Sales	5,684,784.00

BALANCE AS OF JUNE 30, 1999 \$ **31,003,918.39**

FINANCIAL SUMMARY: FISCAL YEAR 1999-00

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$ 178,615.17
Timber	786,714.83
Geothermal	3,926,966.09
Minerals	149,529.98
Oil and Gas	107,631.70
Income from Investments (Interest Earned on Notes)	388,594.96
TOTAL	\$ 5,538,052.73

Less: Geothermal Resource Development Account (GRDA) Deposits	<56,785.38>
(Public Resources Code Section 3826)	

TOTAL \$ 5,481,267.35

Expenses: Net Management Costs

Land Management	\$ 570,129.82
Geothermal	284,213.44
Minerals	224,395.40
Oil and Gas	1,512.50
Ownership Determination	20,116.13
TOTAL	\$ 1,100,367.29

Less: Reimbursement Recovery	<52,027.69>
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TOTAL \$ 1,048,339.60

NET REVENUES TO STRS \$ 4,432,927.75

SCHOOL LAND BANK FUND

Balance as of July 1, 1999	\$31,003,918.39
SMIF Interest Earned Fiscal Year 1999-00	1,782,856.00
Revenue From Land Sales	2,053,381.56
Less: Purchase of Land (Barstow Parcel)	<33,390.00>

BALANCE AS OF JUNE 30, 2000 \$34,806,765.95