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John Donnelly

We greatly appreciate you and the board members of the WCB giving consideration to review of appraisals for conservation deals on the north coast. In addition, we want to reiterate that we believe conservation easements and fee acquisitions can play an important role in protecting the environment, and we support their use especially when arresting development is of paramount importance, or when these tools can be used to protect pristine forestlands or forestlands with unique habitat that are otherwise threatened or likely to be lost.

As we have described, we have questions about the ecological merits of significant state funding to arrest development in Mendocino County, because we see such greater ecological gains available from lower cost restoration activities. If the WCB would adopt ecological goals for its efforts, it would be easier to sort through these competing uses of funds. In the meantime, we think it is of great importance that the prices paid for fee acquisitions or conservation easements are transparent and supported by market based assumptions.

The Big River II appraisal, released after the completion of the transaction, demonstrates significant shortcomings with the current process. The transaction was appraised by 2 independent appraisers (one for the overall property and a second for the underlying timber value), was reviewed by the Department of General Services, and also received a second level review by another independent appraisal. Even with all this review, the final appraisal product fails to credibly defend the price paid (see attachment for items of note in the Big River II appraisal).

You have asked us if we have ideas on how to improve the appraisal process. What follows is our best thinking, based on consideration of these issues since 2007 --

SUNSHINE – Multiple levels of review for Big River II failed to produce an appraisal that stands up to critical review by the public. As we have discussed, regulating good judgment is very challenging, especially in an appraisal process which contains a large number of assumptions and subjective judgments. Most government processes in California operate with a long established and firm policy of substantial disclosure to the public, accompanied by an opportunity for public comment, before taking action. At least as it relates to hard to value assets or significant expenditures of state money (say more than \$10 mm), the WCB should make appraisals supporting purchases available to the public in draft form before the appraisal is sent to the Department of General Services for review. In this way, DGS would have the benefit of public comments before attempting to judge the credibility of assumptions contained in appraisals. Of note, the types of conservation deals completed on the north coast in the last ten years have had essentially no competition, and so additional public disclosure is something selling landowners will find reasonable. While some may claim that disclosure will discourage landowners from selling to the state, this concern rings hollow when there is only one buyer with money at the table.

REALISTICALLY VALUE FOREST REAL ESTATE – Real estate value, or development value associated with timberlands, needs to be carefully valued using market based assumptions. Market based assumptions include:

1. cost and time necessary to subdivide land;
2. cost to providing county and/or fire marshal approved reliable access;
3. cost to install utilities (water, septic and power);
4. comparable transactions for the sale of subdivided parcels;
5. significant discounts associated with remote parcels or parcels made up of steep terrain;
6. enough time for reasonable estimates of demand to absorb the land for sale, particularly for larger tracks of land; and
7. appropriately high “discount rates” to reflect the speculative nature of selling development land over time (an activity that is far riskier than selling logs, unless all development plans are complete and the amount of land sold is modest relative to demand)

VALUE TIMBER BASED ON REALISTIC HARVEST AND REGULATORY ASSUMPTIONS – Timber harvesting in California is regulated by Cal Fire and the Forest Practice Rules, and also by Department of Fish and Game, US Fish and Wildlife, National Marine Fisheries Service, the State and North Coast Regional Water Quality Control Board, several other agencies to a lesser degree and importantly the public as well. Timber appraisals need to take into account the constraints beyond just the Forest Practice Rules, because the cumulative effect of all the regulatory oversight required for timber harvesting is far more restrictive than just the Forest Practice Rules. On the north coast, Endangered Species Act compliance and Water Quality Control Board required road standards add substantial additional costs to timber harvesting that need to be considered. The cumulative effect of regulatory oversight and public interest in forest management especially need to be considered if harvests in excess of forest growth are contemplated. Independent validation of timber volumes is also a factor that needs to be considered.

OTHER –

1. To the extent that an appraiser wishes to consider both real estate value and timber value, some discounting must be made to realistically account for the dual use proposed for the land, in addition to the need for market based assumptions associated with realization of development value.
2. As a matter of general practice, and especially on the north coast, state funded conservation deals should be excluded from comps.

As we have talked about in the past, the appraisal process is technical and involves lots of judgment. We believe this process needs to be significantly improved, in the public interest. Above all else, we think the process should be changed to allow for public review and comment before appraisals are analyzed and judged by DGS.

Sincerely,



Sandy Dean
Chairman

Cc: John McCamman
Ana Matosantos
Jim Kellogg
Karen Finn

Big River II appraisal – items of interest, and questions

1. Timber appraisal contemplates a rate of harvest in excess of growth for 20 years in the midst of a neighbor filled and environmentally sensitive portion of Mendocino County, and the question of discounting a timber appraisal for the conflict of dual use (timber and real estate sales) is unaddressed.
2. Poor comps – 3 out of 5 comps were largely state funded conservation deals. One of these three was for a dramatically different location (an hour from the Golden Gate Bridge vs. 3 hours from the Golden Gate Bridge for Big River II).
3. \$16.6 million of value (32% of the appraised value) is attributed to the land value beyond the timber; however, this fails to consider how or when (if ever) this land value will be realized. A discussion is needed on the investment required to make the land saleable and the rate of market demand for lots going forward.
4. Where is the impact analysis for the effect new neighbors would have on the remaining commercial timber operations and road use?
5. What is the effect the sale of underlying real estate might have on the ability to maintain harvest for 20 years?
6. What about the discounting of value that would be required for the realization of lot sales occurring over an extended period?