



Minnesota's School Trust Lands

Biennial Report

Fiscal Years 2020 – 2021

About This Report

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As requested by Minnesota Statutes, section 3.197: This report cost approximately \$10,000 to prepare, including staff time and data collection.

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Executive Summary

Minnesota's school trust lands comprise over 2.5 million acres of land including surface and mineral rights, and an additional 1 million acres of severed mineral rights distributed across much of the state though heavily concentrated in the northeast portion of the state. Title to the school trust lands is vested in the State of Minnesota, in trust, for the benefit of public schools. The Department of Natural Resources (DNR) manages the school trust land as this property portfolio includes many natural resources including but not limited to forests, agricultural and grazing lands, riparian shores, wetlands, sand, gravel, and large deposits of minerals.

The Permanent School Fund (PSF) is a trust, established in the Minnesota State Constitution, Art. XI, sec. 8 and designated as a perpetual source of revenue for Minnesota's K-12 public schools. The DNR manages the physical lands as a trustee and this obligation imposes fiduciary responsibilities on the department when managing state-owned, school trust assets. It is important to note the DNR does not manage non-trust assets for the benefit of the PSF. The State Board of Investment manages the financial assets in the PSF worth approximately \$1.94 billion as of June 30, 2021.

The Legislature directs DNR to manage the school trust assets in specific ways. The statutory goal of the PSF, outlined in Minnesota Statutes, section 127A.31 and stated as follows: "The legislature intends that it is the goal of the permanent school fund to secure the maximum long-term economic return from the school trust lands consistent with the fiduciary responsibilities imposed by the trust relationship established in the Minnesota Constitution, with sound natural resource conservation and management principles and with other specific policy provided in state law."

The DNR generates revenue through mineral lease rental fees, mineral lease royalties, timber and forest product sales, surface lease rentals, land sales, utility crossings, easements, and other contract receipts. The DNR transfers revenues and other income, less expenses allowed under state law, from these management activities into the PSF in accordance with applicable statutes.



DNR MANAGEMENT ACTIVITIES PROVIDED \$56.45 MILLION IN TRANSFERS TO THE PERMANENT SCHOOL FUND DURING THE FY 20-21 BIENNIUM, A 48% INCREASE FROM THE PREVIOUS BIENNIUM TRANSFERS OF \$39.69 MILLION.

In FY 20 (7/1/19 – 6/30/20), the total distribution to the PSF was \$28.48 million from management activities involving mineral leasing, timber sales, forest products, surface uses, land sales, and water crossing licenses. Mineral leasing accounted for \$23.73 million of the transfer to the PSF. Timber sales, forest products, and surface leasing, less statutorily allowed expenses, contributed approximately \$4.39 million. Land sales and water crossing license revenue supplied an additional \$360,260 in transfers.

In FY 21 (7/1/20 – 6/30/21), the total distribution to the PSF was \$27.97 million from management activities involving mineral leasing, timber sales, forest products, surface uses, land sales, and water crossing licenses. Mineral leasing accounted for \$25.74 million of the transfer to the PSF. Timber sales, forest products, and surface leasing, less statutorily allowed expenses, contributed approximately \$1.91 million. Land sales and water crossing license revenue supplied an additional \$315,202 in transfers.

Financial Summary

Figure 1. School Trust Financial Summary

	Fiscal Year 2020	Fiscal Year 2021
Mineral Leasing Activity *		
Lease Revenues & ITC Interest (100%) Directly Deposited to PSF	\$ 145,360	\$ 131,491
Lease Revenues (80%) Directly Deposited to PSF	\$ 22,230,867	\$ 22,715,365
<i>Lease Revenue Deposited in PSF</i>	\$ 22,376,227	\$ 22,846,856
Minerals Management Account Transfer to PSF **	Fiscal Year 2020	Fiscal Year 2021
Minerals Management Account Revenues	\$ 6,330,506	\$ 8,375,800
Minerals Management Account Costs	\$ (2,942,813)	\$ (3,599,548)
Amount Over \$3M Distributed to PSF (71.1%), University Trust (9.7%), and Tax Forfeit (19.2%) <i>percentages are rounded</i>	\$ 1,021,606	\$ 1,374,213
<i>Distributed to PSF</i>	\$ 1,351,268	\$ 1,871,366
*** Quarter 4 Transfer to PSF	\$ 1,122,162	\$ 1,025,484
Mineral Management Total	\$ 23,727,495	\$ 25,743,706
Real Estate Activity	Fiscal Year 2020	Fiscal Year 2021
Land Sales & Condemnation Awards	\$ 229,536	\$ 174,217
Water Crossing Licenses & Disposition Leases	\$ 130,724	\$ 140,985
Real Estate Management Total	\$ 360,260	\$ 315,202
Timber and Surface Activity ****	Fiscal Year 2019 Activity for Transfer in Fiscal Year 2020	Fiscal Year 2020 Activity for Transfer in Fiscal Year 2021
Timber Sales Qualifying Revenues	\$ 12,601,775	\$ 10,390,212
Surface Uses Qualifying Revenues	\$ 1,183,001	\$ 1,119,407
Non Qualifying Revenues from Surface Uses	\$ 327,865	\$ 301,896
Subtotal	\$ 14,112,641	\$ 11,811,515
Less Forestry Certified Costs	\$ (9,029,383)	\$ (9,205,916)
Less DNR Appropriation Lands and Minerals	\$ (201,743)	\$ (215,000)
Less Dept of Admin Appropriation Trust Director	\$ (299,787)	\$ (300,213)
Less Dept of Admin Reimbursement for Trust Director for Costs	\$ (183,836)	\$ (170,029)
Less Perm School Fund Commission Reimbursement for Costs	\$ (8,385)	\$ (5,946)
Subtotal	\$ (9,723,134)	\$ (9,897,104)
Forest Management Total	\$ 4,389,507	\$ 1,914,411
Total to Permanent School Fund FY20	\$ 28,477,262	FY21 \$ 27,973,319

* Includes iron ore and taconite production, metallic minerals, dimension stone, industrial minerals, stockpiled ore extraction, peat mining and interest income.

** Minerals Management Account represents revenue and cost detail for mineral management of the entire 12 million acre mineral estate owned by the State of Minnesota. The school trust mineral estate is approximately 3.5 million acres of the 12 million acre mineral estate.

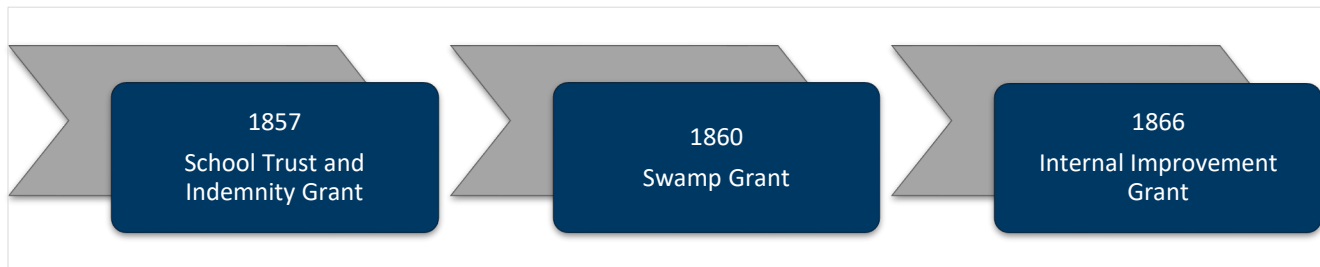
*** Minn. Stat. § 93.2236 states for values over \$3 million in Q4 of any fiscal year the transfer will be done in the following fiscal year.

**** Includes timber sales, timber damages, construction aggregate leases, state forest campgrounds, easements, surface leasing and land crossing licenses.

History of School Trust Lands

Lands set aside in trust for the support of schools are a long established tradition in the United States. The roots of this extend back to colonial practice and to English tradition.¹ The new United States passed a General Land Ordinance in 1785, which allowed for the sale of western lands and provided for section 16 of each public land survey township to be set aside “for the maintenance of public schools, within the said township.”² With the formation of states from the western territories, these reserved lands would become state trust lands. This was first put into practice with the admission of Ohio to the Union in 1802. All states admitted to the Union since then have received some amount of school trust land,³ except those few cases where the federal government owned no land.

The federal Organic Act of 1849 created the Territory of Minnesota and reserved sections 16 and 36 of each public land survey township “for the purpose of being applied to the schools in said territory.”⁴ The federal Enabling Act of 1857 granted the Minnesota Territory these reserved lands, and the people accepted this grant with the adoption of a Constitution in October of the same year.⁵ Minnesota became the 32nd state on May 11, 1858.



Allowances were made if sections 16 and 36 had already been claimed before the land was surveyed, were reserved for an Indian reservation or were under water. These "in lieu" lands were known as school indemnity lands. The grant ultimately resulted in 2.9 million acres being given to the state for the support of public schools. Also included in school trust lands today are the consolidation of remaining lands from two other federal land grants: the Swampland grant of about 4.7 million acres in 1860 and the Internal Improvement grant of 500,000 acres in 1866.

¹ Orfield, Matthias. (1915). *Federal Land Grants to the States with Special Reference to Minnesota*. Minneapolis, MN: Bulletin of the University of Minnesota, pp. 7-13.

² Ibid, 37.

³ Minnesota. Office of the Legislative Auditor. (1998). *School Trust Land: A program Evaluation Report*. St. Paul, MN: State of Minnesota.

⁴ Act of Congress, March 3, 1849, 9 Stat. ch. 121, section 18

⁵ Act of Congress, February 26, 1857, 11 Stat. ch. 60, section 5, first paragraph

A State Land Office was established in 1863. This office managed the trust lands until 1931. In 1931, the Department of Conservation replaced the State Land Office as manager of state trust lands. The Department of Conservation was renamed the Department of Natural Resources in 1969. Minnesota, like many other states, sought to translate trust land into cash for the schools; the first sale of trust land took place in 1862. By 1900, much of the best agricultural, timber and mineral land – especially in the southern part of the state – had been sold to private interests, with mixed results for the schools.⁶

Over time, the trustees and others began to question whether this quick sale policy was in the best interests of the trust. Other options, including leasing the land for specific purposes, were considered. In the early 1900's, the Minnesota Legislature modified its school trust management policy to place a number of restrictions on how the remaining school trust lands would be managed. These limitations shifted Minnesota's policy from one of divesting school trust lands to one of retaining school trust lands for future economic potential in addition to reserving some land for public use and enjoyment.⁷ A non-exhaustive list of legislatively imposed limitations include the 1901 law requiring a reservation of mineral rights, the 1923 law restricting sale of land bordering public waters and a 1935 law removing commercial peat deposits from sale. From the turn of the 20th century, the school trust lands were managed with the idea of "selective retention" of lands the state could manage best.⁸

Table 1. School Trust Land by Grant Type

Federal Grant	Original Grant Acres	Grant Acres Today ⁹
School and Indemnity School (1857)	2,900,000	966,175
Swamp (1860)	4,706,503	1,540,069
Internal Improvement (1866)	500,000	6,510
Total	8,106,503	2,512,754

The federal land grants described above entrusted Minnesota with a total of 8.1 million acres. All of these federal grants are now considered school trust lands after constitutional amendments in 1914, 1938, 1974 and

⁶ Minnesota. Department of Natural Resources. (1983). *School Trust Land Management and Oversight*. St. Paul, MN: State of Minnesota, pp. 10-12.

⁷ Minnesota. Office of the Legislative Auditor. (1983). *Evaluation of State Land Acquisition and Disposal*. St. Paul, MN: State of Minnesota, p. 12.

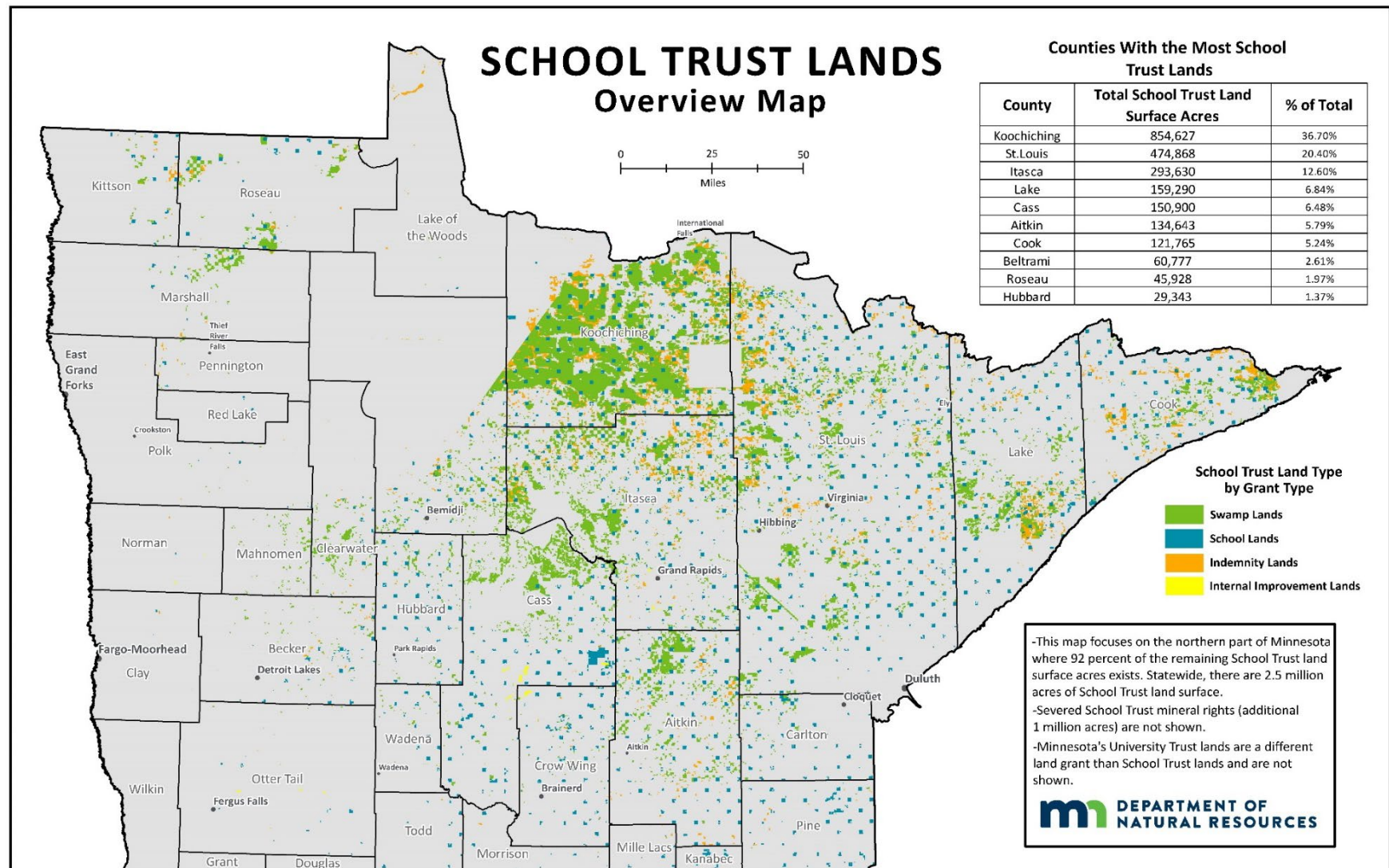
⁸ Ibid, 14-15.

⁹ Minnesota Department of Natural Resources, Land Records System, acres reported as of October 1, 2021.

1984. Approximately 2.3 million acres, roughly 92 percent, of Minnesota's school trust lands are located in ten northern Minnesota counties – Aitkin, Beltrami, Cass, Cook, Hubbard, Itasca, Koochiching, Lake, Roseau and St. Louis.

The DNR has continuously managed the school trust lands since 1931. The DNR actively manages school trust land, including surface and mineral resources for revenue generation through the following general activities: mineral evaluation, leasing and extraction, forest products sales, sale of real property, real property easements, leasing and licenses, evaluation and leasing of surface soil resources and leasing for recreational uses.

Figure 2. Overview Map of Minnesota's School Trust Lands

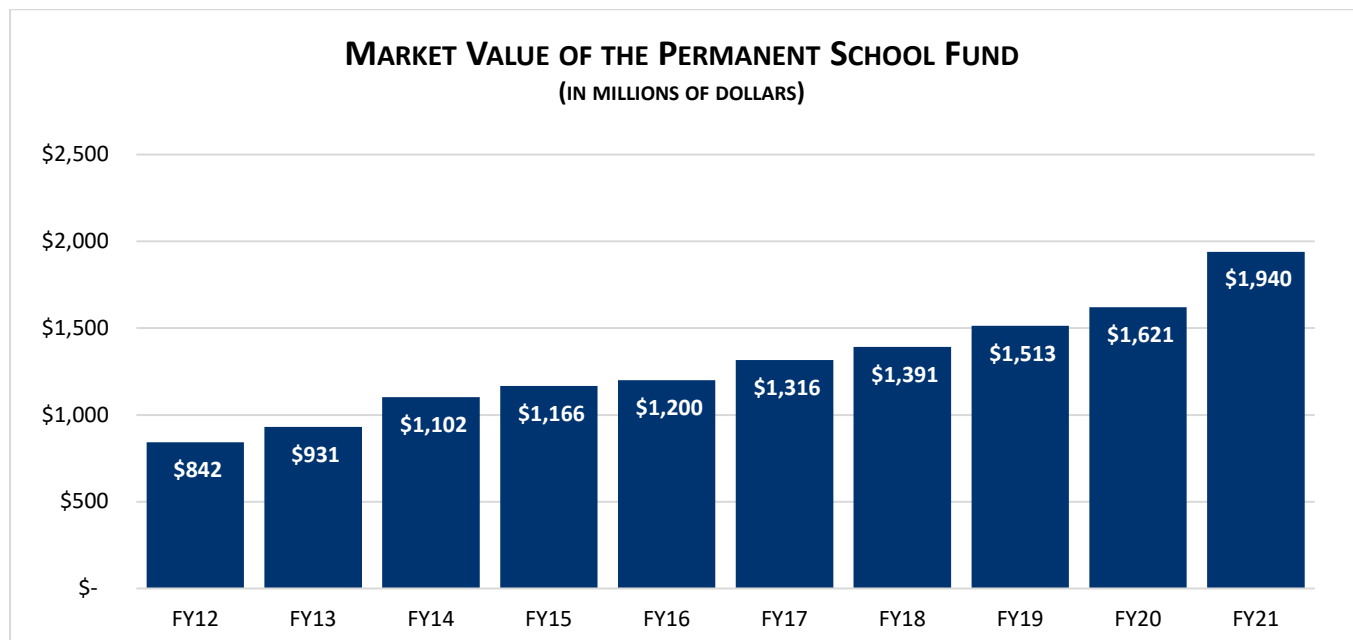


The Permanent School Fund

With the acceptance of the land grant, the Minnesota Constitution created the PSF under Art. XI, sec. 8. As previously stated, revenue for the fund is generated from many activities on school trust land, including sale of timber, gravel mining leases, peat leases, state forest campground fees, lakeshore leases, easements and utility licenses, the sale of school trust land and several other types of surface use. In addition, revenue is generated from rentals and royalties from leasing school trust mineral assets, including iron ore and taconite, non-ferrous metallic mineral leases, peat and industrial mineral leases.

The State Board of Investment (SBI) manage funds for trusts and programs created by the Minnesota State Constitution and Legislature. The SBI completes quarterly and annual performance reporting and these reports describes the PSF as a trust established for the benefit of Minnesota’s public schools. According to SBI, as of June 30, 2020 (FY 20) the market value of the PSF was approximately \$1.62 billion and the fund had grown to over \$1.94 billion as of June 30, 2021 (FY 21).

Figure 3. Market Value of the Permanent School Fund



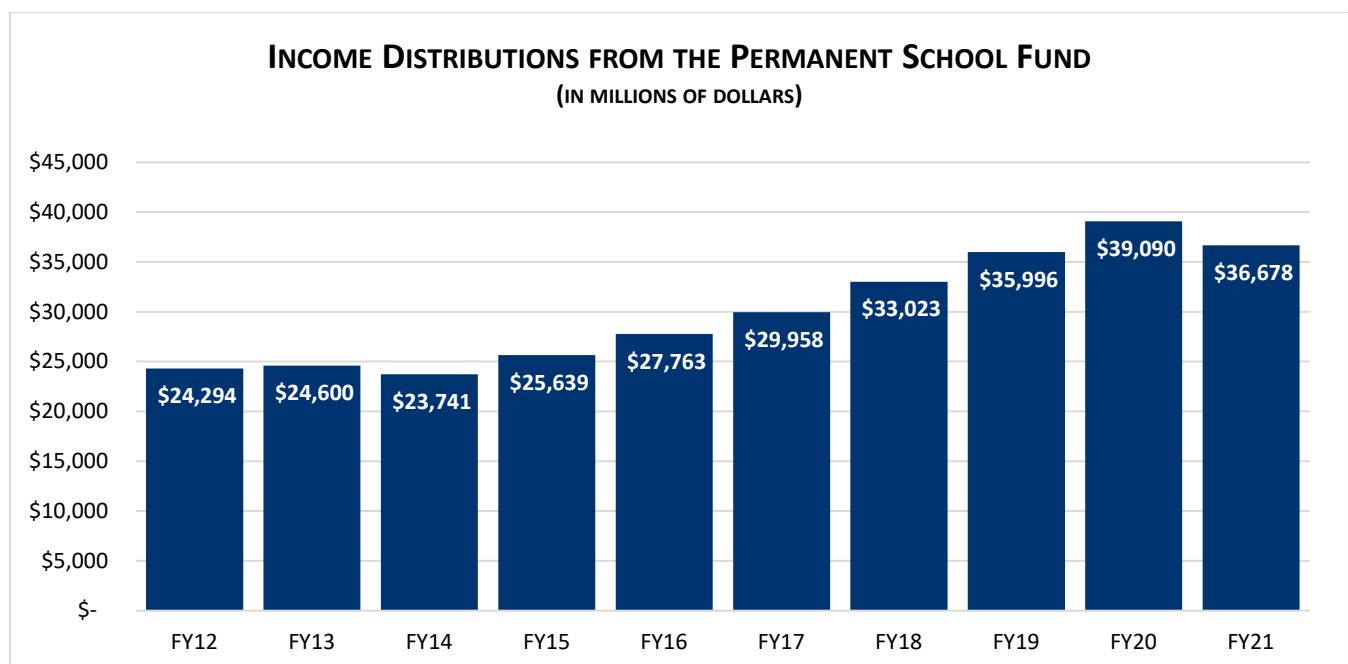
The PSF is invested in a balanced portfolio of common stocks and bonds. Common stocks provide the potential for significant capital appreciation, while bonds provide portfolio diversification and a more stable stream of current income.¹⁰ All PSF financial assets are invested and managed by SBI staff or externally by investment

¹⁰ Minnesota. State Board of Investment. (2021). *Minnesota State Board of Investment Quarterly Comprehensive Performance Report June 30, 2021*. St. Paul, MN: State of Minnesota, p. 102.

management firms retained by the SBI. The PSF uses various investments funds as a diversification strategy. The Equity Fund is managed by Mellon Investments Corporation¹¹; the Bond Fund is managed by Prudential Global Investment Management¹²; and the Money Market Fund is managed by State Street Global Advisors.¹³

PSF assets created roughly \$39.09 million of investment and dividend income as of June 30, 2020 (FY 20) and approximately \$36.68 million as of June 30, 2021 (FY 21). The investment and dividend income is transferred to the School Endowment Fund and distributed annually to Minnesota’s 326 public school districts and 178 academies and charter schools. The Department of Education distributes dollars to each district based on the number of students in average daily attendance during the preceding school year, with an estimated 850,000 students throughout the state’s public education system.

Figure 4. Annual Investment and Dividend Income Distributions



There are a few investment constraints and legal provisions for the PSF. As reported in the SBI 2020 Annual Report, any net realized capital gains from stock or bond investments must be added to the principal and the principal must remain intact. In other words, it cannot be spent or allocated from the fund for any purpose at any time. If the PSF realizes net losses in any given year, the losses must be offset against interest and dividend

¹¹ Minnesota. State Board of Investment. (2020). *Minnesota State Board of Investment 2020 Annual Report*. St. Paul, MN: State of Minnesota, p. B105.

¹² Ibid, B106.

¹³ Ibid, B107.

income before that income can be distributed to the public schools. Finally, all interest and dividend income must be distributed in the year in which it is earned.¹⁴

This information is presented in annual and quarterly SBI publications and is available on the SBI website: www.msbi.us

Office of the Legislative Auditor Special Review

In 2018, several legislators asked the Office of the Legislative Auditor (OLA) to review how effectively the state oversees the management of Minnesota’s school trust lands, as it relates to changes made by the 2012 Legislature. During FY 20, the OLA concluded a special review and developed a report titled *School Trust Land Management and Oversight*¹⁵ that focused on school trust related activities and initiatives, since the 2012 legislative changes of the DNR, the Office of School Trust Lands (OSTL), and the Legislative Permanent School Fund Commission.

There were a number of OLA recommendations and both the DNR and the OSTL provided responses to the report. Below you will find the OLA recommendations and a summary of the department’s response for recommendations under the authority of DNR.

Table 2. OLA Recommendations and DNR's Summary Response

OLA Recommendations	DNR Summary Response
The Department of Natural Resources—with input from the Office of School Trust Lands—should develop a comprehensive set of measures to help assess the management of school trust lands and the revenue they generate.	The DNR agrees with this recommendation to the extent that the DNR does not currently have a comprehensive set of goals specific to school trust lands. The DNR does maintain goals and measures that span across all types of state lands, including some limited specific goals for school trust lands (e.g., a “cords offered” target for school trust lands within the department’s sustainable timber harvest goals). The DNR is working with OSTL to develop a school trust land Asset Management Plan that will establish performance metrics, or recommendations for performance metrics, and will aid in the assessment of school trust lands management.

¹⁴ Ibid, B109.

¹⁵ Minnesota. Office of the Legislative Auditor. (2020). *School Trust Land Management and Oversight Special Review May 2020*. St. Paul, MN: State of Minnesota.

OLA Recommendations	DNR Summary Response
Consistent with state law, the Legislature should compensate the Permanent School Fund for instances in which state policies or legislative actions have prohibited school trust lands from generating revenue.	DNR did not respond to this recommendation as this consideration is under the authority of the Legislature.
The Legislature should consider clarifying in law: 1. Whether OSTL's authority to act as a temporary trustee of school trust lands is mandatory in cases involving school trust land condemnations. 2. Procedures by which land valuations or appraisals for school trust land condemnation must be obtained, and whether those appraisals or valuations must be by parties other than DNR. 3. How disagreements between OSTL and DNR in the school trust land condemnation process should be resolved.	1. This consideration is under the authority of the Legislature. DNR did not respond directly though supports clarifying roles in Minnesota statutes. 2. The DNR agrees with this recommendation. DNR and OSTL have been collaborating on a new standard operating procedure for condemnation transactions (see Policy section for more information). This procedure intends to clarify when land valuations or appraisals must be obtained and how the OSTL engages with DNR on school trust land condemnations. 3. This consideration is under the authority of the Legislature. DNR did not respond directly though supports clarifying roles in Minnesota statutes.
The Legislature should amend statutes to require the Office of School Trust Lands to obtain approval from the Department of Natural Resources before initiating real estate projects on school trust lands.	The DNR did respond to this consideration under the authority of the Legislature, only to say that DNR agrees with this recommendation and supports further clarifying DNR and OSTL roles regarding evaluating and initiating real estate projects on trust lands.
The Legislature should authorize the Legislative Permanent School Fund Commission to have at least one staff person knowledgeable in school trust land issues, preferably with legal expertise.	DNR did not respond to this recommendation as this consideration is under the authority of the Legislature.

OLA Recommendations	DNR Summary Response
The Department of Natural Resources should expeditiously use the proceeds of its legislatively required land sales to condemn and sell certain school trust lands that cannot generate revenue, thereby generating revenue for the Permanent School Fund.	The DNR agrees with this recommendation. The department plans to reprioritize work to first use the \$687,000 in proceeds from land sales completed under the legislative directive to buy out (i.e. condemn) the trust interest in prioritized Public Water Access (PWA) sites, instead of first completing additional PWA site land exchanges, as previously planned.
The Department of Natural Resources should report in its biennial reports about its progress in (1) maximizing the long-term economic return on trust lands unable to generate revenue due to policy or statutory designation and (2) obtaining funds from the Legislature or elsewhere to compensate the Permanent School Fund for these lands.	The DNR agrees with this recommendation. However, we also want to note that, while these updates have been limited within the biennial school trust land reports, efforts to maximize long-term economic returns and compensate the trust where statute or policy inhibit returns were covered extensively in two separate “compensation reports” that were provided to meet the intent of the statutory requirements. We have since restructured the biennial report to integrate compensation status reporting directly into the biennial report.
The Legislature should amend state law to require the Department of Natural Resources to prepare a biennial rather than a biannual report.	The DNR agrees with this recommendation. As mentioned in your report, Section 14 of the DNR’s 2020 policy bill (HF 3657 / SF 3842) includes this change to the reporting requirement (see Policy section for more information).

For more information or to view a copy of the report, please visit the OLA website at the following link:
www.auditor.leg.state.mn.us

School Trust Policy

During the reporting period, the DNR made improvements to school trust land policy and procedure through interdisciplinary department teams, as well as through the legislative process. The most significant efforts are described in this section.

Summary of New Law

The DNR and the OSTL put forth policy items in FY 2020 and FY 2021 as part of the legislative process. Those policy items, as well as the 2020 and 2021 DNR Lands Bills, passed in the 1st Special Session of 2021 as part of

the Omnibus Environment and Natural Resources Bill¹⁶. The table below contains the school trust land related provisions, as well as the provisions from the DNR Lands Bills.

Table 3. Summary of School Trust Related Policy Provisions

Article	Section	Summary	Origin
2	19	Amends Minn. Stat. sec. 84.027, subd. 18, to require a “biennial” instead of a “biannual” report to the Legislative Permanent School Fund Commission	DNR Proposal
2	21	Enacts Minn. Stat. sec. 84.625, authorizing the conveyance of conservation easements on state-owned, DNR-administered land	OSTL Proposal
2	48	Enacts Minn. Stat. sec. 92.503 to authorize the DNR to issue conservation planning leases for a term of up to 21 years	OSTL Proposal
2	106	Amends Laws 2016, chapter 154, section 16, to require wild rice lessees to pay all costs of a land exchange	DNR Proposal
2	107	Amends Laws 2016, chapter 154, section 48 (Coe College land exchange) to authorize the Land Exchange Board to consider a donation of land by the exchange partner, in addition to the land proposed for exchange, in determining whether the exchange is in the best interests of the school trust	DNR Amendment Request

For more information, please visit the Office of the Revisor of Statutes website at the following link:

www.revisor.mn.gov

Internal Policy and Procedure

Operational Order 121: Management of School Trust Lands

In April 2019, Commissioner Strommen signed Operational Order 121: Management of School Trust Lands. The DNR uses an internal policy framework and operational orders within this framework define policies and

¹⁶ Laws of Minnesota 2021, 1st Special Session, chapter 6, article 2

procedures concerning internal management. Operational Order 121 is specifically used to clarify and direct staff-level management activities on school trust lands. The school trust operational order does the following:

- It lays out the legal direction that guides our school trust land management;
- It describes what it means to act as a trustee on behalf of beneficiaries;
- It identifies how the department operationalizes “sound natural resource conservation and management principles”;
- It defines standard school trust land management practices;
- It clarifies department-level decision-making processes related to school trust lands including a dispute resolution process; and,
- It identifies how the department compensates the PSF when the DNR makes management decisions that reduce or prohibit revenue to the trust.

Department Training

After the reissuance of the operational order and during the reporting period, there was significant effort to educate and train DNR staff on this new set of policies and procedures used to guide management of school trust lands. Considerable time was spent at statewide trainings reviewing in more detail the items bulleted above, as well as discussing what it means to implement “sound natural resource conservation and management principles...” using the department’s three-pronged approach to: 1) implement state and federal law, 2) use widely vetted best management practices, and 3) develop guidelines to take ecological benefits into consideration that are in the best interests of the trust.

School Trust Land Forest Management Policy Guidelines Project

Under the policy framework outlined in Operational Order 121, the department defines standard school trust land management practices through the development of policy guidelines. School trust land policy guidelines:

1. clarify implementation of state and federal law,
2. define best management practices applied on school trust lands, and
3. implement specific strategies to manage for ecological benefits when doing so is in the best interest of the trust. The DNR may identify strategies to manage for ecological benefits in the following situations:
 - a. Endangered Species. When modifying management for species, that are at high-risk of being federally or state listed as threatened or endangered, to prevent an uplisting. An uplisting typically makes management more difficult and costly to the trust. Preventing an uplisting in the best interests of the trust.
 - b. Natural Resource Certification. When modifying management helps maintain relevant natural resource certifications, like forest certification. Maintaining the certifications helps make school trust products more marketable and is, therefore, in the best interest of the trust.
 - c. Commissioner's Office. When modifying management, on a limited basis and as determined by the Commissioner, when it is in the best interests of the trust.

During FY 20-21, the department identified a need to develop forest management guidelines on a small set of specific topics to identify and clarify DNR’s management approach. Through an interdisciplinary process, staff

identified the following topics for guideline development: vernal pools, ungulate conifer cover for deer, jackpine woodland, northern mesic hardwood, dry barrens oak savanna, northern goshawk, natural origin red pine and ungulate conifer cover for moose.

The process allows for each topic to initially be developed by an interdisciplinary team with recommendations for management. These recommendations are reviewed and revised as needed by the DNR School Trust Advisory Team and the Executive Forest Resources Issues Team. The OSTL is then consulted and provides advice as to the extent to which the guidelines meet the goals of the PSF and other policy outlined in law. The final step is for the DNR Commissioner's Office to review these guidelines, and for those that are approved, distribute them for department-wide implementation.

The department is evaluating management recommendations for five of the eight topics. Three of the eight topics are still in the development phase. Staff will continue to work on these topics and will report outcomes in the next biennium.

School Trust Land Condemnation Procedure Project

Operational Order 121 also identifies how the department compensates the PSF when the DNR makes management decisions that reduce or prohibit revenue to the trust. The statutory goal of maximizing the long-term economic return from school trust lands, while managing those lands according to sound natural resource conservation and management principles, will occasionally necessitate the permanent acquisition of school trust lands by the DNR.

During the biennium, the DNR and the OSTL collaboratively developed an administrative procedure for compensation to the PSF via condemnation. The DNR acquires school trust land through a condemnation action in which the department pays the value of the land, and applicable resources, to the PSF to permanently extinguish the school trust interest in school trust lands. The government's power of eminent domain to condemn property must be for public use and must provide just compensation for the taking. This procedure clarifies the process the DNR uses to acquire school trust lands and the statutory requirement of the OSTL School Trust Lands Director to "serve as temporary trustee of school trust land for school trust lands subject to proposed or active eminent domain proceedings..."¹⁷ The development of this procedure improves business functions between DNR and OSTL and allows DNR to facilitate these complex transactions in a more effective manner.

Gross Revenue

DNR management of school trust land generates revenue from three major categories – mineral lease rental and royalty payments, forest management and surface activities, and real estate transactions. Various factors affect the amount of revenue generated from school trust lands year to year and revenues ebb and flow. Economic

¹⁷ *Minnesota Statutes*, section 127A.353, subdivision 4, paragraph (b), clause (6)

returns can vary significantly based on global and regional market-driven price fluctuations for minerals and timber, as well as the cost of these operations.

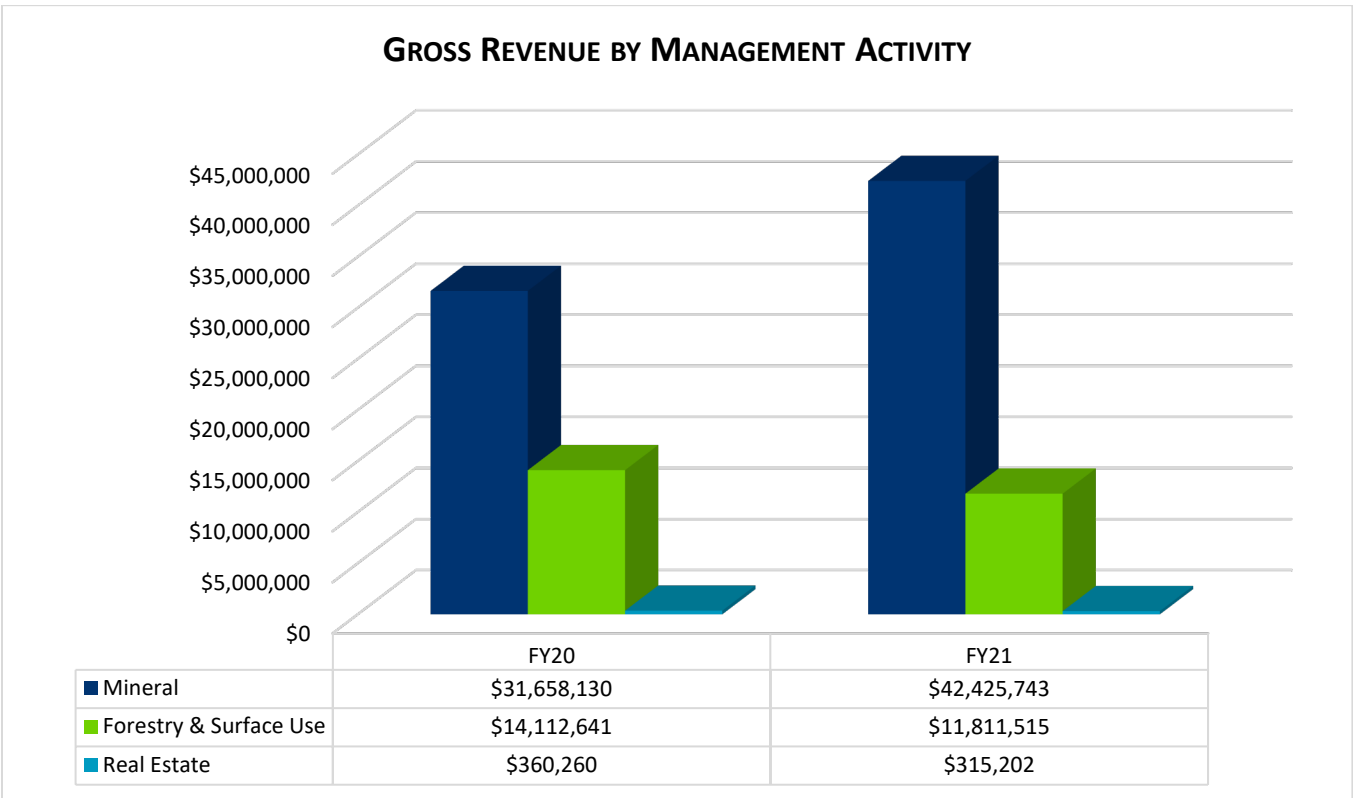
School Trust Gross Revenue

During the reporting period, school trust management activities generated gross revenue of \$100.68 million from school trust lands and resources. This is the most revenue ever reported in a single biennium and represents a 53% increase over the previous reporting period’s (FY 18-19 biennium) gross revenue of \$65.73 million. The majority of this increase is due to additional tons of crude ore mined and an increase in mineral royalties (see [Mineral Management](#) section for more information).

In FY 20 (7/1/19 – 6/30/20), school trust management activities generated gross revenue of \$46.13 million from resources such as minerals, forest products, and land. Mineral lease fees and royalty payments accounted for \$31.66 million. Forest products and surface leasing contributed \$14.11 million and real estate transactions, such as water crossing licenses and school trust land sales, supplied an additional \$360,260.

In FY 21 (7/1/20 – 6/30/21), school trust management activities generated gross revenue of \$54.55 million from resources such as minerals, forest products, and land. Mineral lease fees and royalty payments accounted for roughly \$42.43 million. Forest products and surface leasing contributed \$11.812 million and real estate transactions, such as water crossing licenses and school trust land sales, supplied an additional \$315,202.

Figure 5. Gross Revenue by Management Activity



Expense and Cost

DNR generates revenue from three primary revenue-generating asset classes (i.e., resources) and transfers revenues and receipts, less expenses and costs allowed under state law, from these activities into the PSF. The management costs allowed under state law are described in this section for minerals and forest management. Real estate management costs are not allowed to be certified against school trust proceeds under state law.

School trust land revenues, earnings, and expenditures flow through various state funds and the complexity of school trust land-related accounts and funds, as well as state law directing DNR activities, precludes the department from recouping all of its school trust land management expenses and costs. According to a report developed by Minnesota Management and Budget, the general fund, state bond funds and other available funds appropriated by the Legislature for a wide-variety of DNR management activities provide a significant funding subsidy that directly benefits the PSF.¹⁸

While working to develop the School Trust Lands Asset Management Plan (see [Strategic Projects](#) section for more information), the DNR and OSTL Project Core Team initiated an exercise to more clearly identify what a management expense is versus a management cost. The team documented management expenses as usually associated with performing an activity at the parcel level, whether done internally or by a third party. This includes, but is not limited to: maintenance, engineering, taxes and assessments, travel, fuel, advertising, marketing, signage, utilities, legal work, entitlements, research studies, third party fees, appraisals, feasibility studies, inspections and regulatory fees. Expenses may also refer to some one time portfolio-level items such as research studies, investigations, subscriptions or conference fees related to a sector such as minerals.

Management costs, however, generally refer to ongoing costs and overhead that benefit the entire portfolio and, for school trust land management, are more difficult to allocate by asset class or on a parcel basis. These may include, but are not limited to: costs of office facilities, technology, administration and salaries of people not directly involved in managing the assets on a day-to-day basis such as DNR's leadership personnel, Office of the General Counsel and the Commissioner's Office.

Expense and Cost for Minerals Management

In 2005, legislative changes permitted the DNR to receive a portion of gross mineral revenues to fund mineral management activities. Pursuant to Minnesota Statutes, section 93.22, twenty percent of mineral receipts are deposited into the Minerals Management Account (MMA) for the administration and management of the entire 12 million acre mineral estate owned by the State of Minnesota, including the 3.5 million acres of school trust

¹⁸ Minnesota. Minnesota Management and Budget, Management Analysis and Development. (2018). *Costs for School Trust Lands Management: Current Approaches, Issues, and Potential Alternatives October 30, 2018*. St. Paul, MN: State of Minnesota.

mineral rights. The remaining eighty percent of the school trust revenue from mineral leasing is distributed to the PSF, from which the net interest and dividends are distributed to the school districts throughout the state.

Minerals Management Account Background

The DNR manages the entire mineral estate retained by the State of Minnesota. Minnesota's mineral portfolio includes mineral rights where the state has control of the surface. It also includes mineral rights where another party controls the surface (i.e. severed mineral rights). The DNR manages the mineral estate of multiple land classes such as consolidated conservation lands, Volstead lands, county tax forfeit lands, school trust lands and university trust lands.

The MMA was designed to create a \$3 million principal that could be drawn upon in the event that future mineral income drops. At the end of each quarter, the amount exceeding \$3 million is distributed to the PSF, Permanent University Fund and local taxing districts in the same proportion as the total lease revenue received in the previous biennium from these land ownership classifications. Minnesota Statutes, section 93.2236 states that the legislature approves DNR's use of MMA funds for "mineral resource management and projects to enhance future mineral income and promote new mineral resource opportunities."

Each year, the legislature appropriates money to DNR from the MMA for the administration and management of the state's entire 12 million acre mineral estate. DNR does not certify its mineral management costs against the gross revenues. This is important to note, as the MMA funds minerals promotion and management activities on all state-owned land types as mentioned above and not exclusively school trust lands.

Minerals Management Account Appropriations

The FY 20 and FY 21 appropriations to the DNR from the MMA are in Laws of Minnesota 2019, 1st Special Session, Chapter 4, article 1, section 3, subdivision 2. The table below describes the appropriations for the biennium.

Table 4. Minerals Management Account Appropriations

FY 2020 MMA Appropriation	FY 2021 MMA Appropriation	Comments
\$200,000	\$200,000	For environmental research relating to mine permitting.
\$3,032,000	\$3,083,000	For use as provided in Minnesota Statutes, section 93.2236, for mineral resource management, projects to enhance future mineral income and projects to promote new mineral resource opportunities.

Expense and Cost for Timber and Surface Management

Forestry Certification Process

Minnesota Statutes, section 16A.125 provides for which surface management costs can be certified against school trust revenues and how the certified costs and net revenues from the school trust lands are distributed. The allowable expenses are categorized as improvement, administration, management of forestland and the construction and maintenance of forest roads. Only those charges that were paid from the state's general fund and forest management investment accounts, appropriated for the Division of Forestry, are included. Costs charged to other state and federal funds are excluded from the cost certification process.

The Minnesota Constitution, article XI (appropriations and finances), section 11 (timber lands set apart as state forests; disposition of revenue) reads:

“School and other public lands of the state better adapted for production of timber than for agriculture may be set apart as state school forests, or other state forests as the legislature may provide. The legislature may also provide for their management on forestry principles. The net revenue therefrom shall be used for the purposes for which the lands were granted to the state.”

The DNR identifies hours of paid staff time and dollars expended using a set of cost codes for forestry activities. These cost codes track charges based on the type of activity (e.g., forest improvements, forest inventory, timber sales, administration, etc.) and on the land type on which the activity took place.

More information is presented in the Division of Forestry's annual “Minn. Stat. 16A.125 Transfer Certification Report” and is available on the DNR website: <https://www.dnr.state.mn.us/aboutdnr/reports/index.html>

Expense and Cost for Real Estate Management

Forest Suspense Account Appropriations to the Lands and Minerals Division

For the FY 20-21 biennium, the legislature appropriated \$215,000 the first year and \$218,000 the second year from the Forest Suspense Account (FSA) in the PSF to “secure maximum long-term economic return from the school trust lands consistent with fiduciary responsibilities and sound natural resources conservation and management principles”.¹⁹ These dollars are used for real estate management activities such as land sales, land exchanges, resolution of trespass or encroachment, accelerating commercial leasing and enhancing aggregate leasing.

¹⁹ Laws of Minnesota 2019, 1st Special Session, Chapter 4, article 1, section 3, subdivision 2

Management Activity Highlights

Mineral Management

DNR administers the entire 12 million acre mineral estate owned by the State of Minnesota. This includes mineral rights for all state-owned lands including but not limited to: school trust, university trust, consolidated conservation, Volstead and tax forfeited lands. The DNR, acting in its trustee capacity, manages the school trust mineral estate for the benefit of the K-12 public education system and its students. The DNR manages mineral rights predominantly for iron ore and taconite, non-ferrous metallic minerals, dimension stone, industrial minerals and stockpiled ore.

Mineral Management Highlights

Iron Ore and Taconite Leasing

During FY 20, iron ore mining for Minnesota's six iron ore pellet producing facilities was impacted at the onset of the COVID-19 pandemic with mines temporarily closing and production was curtailed into FY 21. Demand for iron and steel products did soon recover and became very strong in the latter half of FY 21. The most significant source of school trust iron ore mined in the biennium was at US Steel's Minntac operation in Mountain Iron, Minnesota. Northshore Mining also mined school trust iron ore.

A summary of royalty payments for the two mines in operation on school trust lands can be found below in Table 4. The other mining company facilities found within the table did not mine school trust ore in the biennium, but the PSF did receive mineral lease fees from these operations.

Table 5. Summary of Mineral Lease Fees and Royalties

Mining Company Facilities	Iron Ore Lease Fees & Royalties FY 2020	Iron Ore Lease Fees & Royalties FY 2021	Total Biennium
Minntac	\$25,567,890	\$25,939,674	\$51,507,564
Northshore Mining	1,482,126	124,582	1,606,708
Hibbing/Ontario	219,353	219,353	438,706
Keewatin Taconite	39,600	39,600	79,200
Mesabi Metallics	21,600	1,593,638	1,525,238

Mining Company Facilities	Iron Ore Lease Fees & Royalties FY 2020	Iron Ore Lease Fees & Royalties FY 2021	Total Biennium
Other	(13,311)	1,700	(11,611)
Total	\$27,317,258	\$27,828,547	\$55,145,805

Total mineral receipts paid by these taconite iron ore pellet operations from school trust lands was \$55,145,805 for the FY 20-21 biennium. This is up \$17,638,264 or 47% from the previous FY 18-19 biennium receipts of \$37,507,541. In addition, 14.6% of the increased revenue is due to additional tons of crude ore mined from school trust lands compared to the previous biennium. The remaining 32.4% of the biennium over biennium increase is due to higher royalty rates. The higher royalty rates are attributable to favorable iron ore and steel pricing used to escalate the per ton payments.

In addition to the six taconite iron ore pellet producers in Minnesota, the state also received \$107,176 in payments attributable to school trust stockpiled material from legacy stockpiles that were reprocessed by Mining Resources, Hibbing Taconite and Prairie River Minerals.

Industrial Minerals

Under Minnesota law, high-quality dimension stone is classified as an industrial mineral on state lands. Dimension stone is bedrock cut into blocks and slabs that is used for various building construction applications, to make monuments and for decorative stone once polished. Over the past 30 years, DNR geologists spearheaded an inventory of classifying dimension stone potential on public lands. This inventory considers the suitability and durability of bedrock through a developed methodology consisting of geologic interpretation combined with on-site observations and sampling.

This effort led to the discovery and leasing of several dimension stone sites on state and federal lands in northern Minnesota, which are operated by Minnesota-based companies. On state trust land, Kasota Stone Fabricators Inc.'s ("Kasota Stone") L-231 Quarry, is considered world-class due to its extremely limited joint spacing and uniformity in both color and texture. These qualities allow for the removal of large, consistent blocks. DNR implements a guaranteed royalty rate that ensures income on leases even in nonproductive years. A guaranteed royalty rate benefits the trust by providing long-term revenue streams from royalty payments while incentivizing the company to expand operations over time.

As a critical function of school trust land management, DNR continues to capitalize the economic opportunities of dimension stone resources for the trust. In FY 20 and FY 21, DNR staff oversaw the administration of three industrial minerals leases on school trust land, two with Kasota Stone (Mankato, MN) and one with Cold Spring Granite (Cold Spring, MN). DNR staff monitor exploration activity, quarry activity and production year to year to ensure compliance with lease terms, operation and reclamation plan conditions. The PSF received over \$239,435 during the reporting period in royalties from dimension stone leases, with continual growth since 2016.

Non-Ferrous Metallic Minerals Leasing

Three processes are used to offer non-ferrous metallic mineral leases in Minnesota: public auction, negotiation and preference rights application.²⁰ Before the DNR can issue any non-ferrous metallic mineral lease, the proposed lease must be approved by the State Executive Council.²¹ During the past biennium, the DNR did not hold a public lease auction for non-ferrous metallic mineral leases.

During FY 20, the State Executive Council approved four negotiated non-ferrous metallic minerals leases to Vermillion Gold, Inc. covering 1,668.15 acres in Itasca County. Of the total acres, 631.05 are school trust lands.

During FY 21, the DNR initiated a public input process for a request by Vermillion Gold, Inc. for three additional negotiated non-ferrous metallic minerals leases in St. Louis County and a metallic minerals lease amendment request by Kennecott Exploration Company in Aitkin County. Of the areas requested for lease by Vermillion Gold, Inc., 80 acres are school trust lands.

Mineral Research

DNR has invested in developing a document management system aimed to organize and publicly distribute archived exploration data and reports. This effort includes scanning and potentially digitizing geospatial data to aid in the usability and search ability of the data, and to attract interest in nonferrous leasing of school trust lands. Results of this effort include release of AngloGold terminated lease data, oxide-bearing ultramafic intrusions data within the Duluth Complex that host occurrences of titanium and vanadium, as well as the state's archive of geophysical data.

DNR has also participated in a cooperative effort with the Minnesota Geological Survey, the Natural Resource Research Institute, the US Geological Survey, to better define the mineral potential in the state. As a result, over \$500,000 of data acquisition, that includes high-resolution geophysical data, has been acquired for a portion of the state as well as detailed geologic mapping. This effort is a part of the federal government initiative to identify domestic sources of critical minerals. With the some of the world's largest deposits of copper, nickel, cobalt, and manganese, Minnesota will likely continue to be a place of interest has funding for this initiative continues.

Forest and Surface Management

The Minnesota Constitution establishes that school trust lands, along with other state-owned lands, can be set aside as a special class of productive forest lands and managed on forestry principles.²² The Sustainable Forest Resources Act (Minnesota Statutes, Chapter 89A) provides primary statutory direction for DNR forest

²⁰ *Minnesota Rules*, part 6125.0500-.0610

²¹ *Minnesota Statutes*, section 93.25, subdivision 2

²² Minnesota Constitution, article XI, section 11

management. Accordingly, it is the state's policy to "pursue the sustainable management, use, and protection of the state's forest resources to achieve the state's economic, environmental, and social goals," with sustainability defined as "meeting the needs of the present without compromising the ability of future generations to meet their own needs."

Using the state's public land base, DNR comprehensively plans using a "multi-lands" approach. There are many different land types, within the state's public land base, that allow DNR to manage comprehensively yet differently, to adhere to various obligations for particular land types. To provide maximum benefit to all state lands, the DNR has implemented a forest management approach that manages the state's forestlands as one large group. This is beneficial to all land types as efficiencies continue to be realized. State-owned lands and resources are the foundation in which the DNR executes its mission for the benefit of all Minnesotans.

The overarching forest management strategy differs significantly from many private timber managers. DNR recognizes the symbiotic relationship between state-owned lands and Minnesota's economy. While private timber companies may elect to hold their timber off the market when prices are low, the DNR approach is to continue to offer timber resources for two main reasons. First, continuing to offer timber resources is the primary means by which DNR can manage the health of our forested lands. Second, maintaining harvest levels helps ensure that a viable forest products industry will remain in Minnesota, thereby protecting the long-term value of our timber assets. These strategies continue to make sense. If there is a change in the future economic condition, DNR's strategy may change as well.

Forest and Surface Management Highlights

Sustainable Timber Harvest Analysis and Implementation

Good forest management includes periodic review of timber harvest levels and their impact to the greater forest ecosystem and economy. Governor Dayton directed the DNR to analyze the sustainability of harvesting one million cords of timber per year from DNR-managed forestlands. If the analysis determined that an annual harvest of one million cords was not sustainable, the governor asked DNR to identify an alternative sustainable harvest target. Mason, Bruce & Girard (MB&G), an independent contractor, conducted the analysis and a stakeholder advisory group provided input.

The Sustainable Timber Harvest Analysis (STHA) was a transparent stakeholder process utilizing a 14-member stakeholder advisory panel. In addition, the OSTL was engaged as a direct advisor in the process. More than 140 individuals or groups provided comments that were shared with MB&G for consideration in their final report; the DNR also considered these comments in making the harvest level decision.

DNR strives to provide a stable, quality source of wood fiber to industry in a manner that is sustainable and conserves Minnesota's state forest resources into the future. A variety of environmental and economic factors were considered in the analysis. The final MB&G report provides an assessment of the long-term sustainability of potential harvest levels from DNR-managed lands given the results of models emphasizing various values.

After more than a year of rigorous scientific analysis, discussions with key partners, including conservation organizations and forest industry and public input, DNR set a new 10-year sustainable timber harvest at 870,000 cords offered for sale annually from DNR-managed forest lands. Under the sustainable timber harvest target of

870,000 cords annually, DNR-managed forest lands will continue to sustain Minnesota's rich biodiversity, provide healthy and thriving wildlife habitat, offer multiple recreation opportunities, support our state economy, contribute to clean air through carbon storage and help keep our water clean.

Beyond the 870,000 cords, DNR launched a five-year initiative to offer up to 30,000 additional cords of ash and tamarack annually in response to the threat posed by emerald ash borer and eastern larch beetle. Forest health professionals suspect that these two insects will decimate Minnesota's ash and tamarack forests. The DNR is accelerating its harvest to capture value before the trees are killed and plans to reforest the sites.

Management regimes (rotation ages, thinning intervals and reserve percentages) were developed and applied in a harvest scheduling model. Different regimes that prioritize wildlife habitat were applied to non-school trust lands within Wildlife Management Areas and other management opportunity areas identified during STHA. All other lands were modeled using management regimes consistent with the rotation ages, thinning intervals and reserve percentages from past DNR planning efforts. The standard DNR management regimes were also applied to all school trust lands included in STHA regardless of their location. All of the regimes are consistent with the multiple forest values, including wildlife habitat, rare species, water quality and recreation, and they balance these values somewhat differently.

To implement decisions associated with STHA and the 10-year sustainable timber harvest target of 870,000 cords, the department developed a 10-year stand exam list which is a forest resource management plan specifying which forest stands the DNR will visit and evaluate for potential harvest during FY 2021 – 2030. The actual harvest of each stand is contingent on results of a site visit, public auction, and the operational environment. The Forestry Division's Timber Program is responsible for timber sales and related management.

All of the information found above and pertaining to the STHA is available on the DNR website:

www.dnr.state.mn.us/forestry/harvest-analysis/index.html

Timber Management

Timber sale management is directed by statute (Chapter 90). Timber management activities generate revenue across a number of fiscal years. The initial revenue is a 15 percent down payment, based on the appraised value of the permit made at the time of sale at a public auction. The remaining value of the timber permit is a required payment in the form of cash or documentary credit before the high bidder begins the harvest. The actual value of timber harvested is then invoiced on a quarterly basis until the harvesting is completed. Timber permits have between a three-year and five-year lifespan with ability for a one-year extension, if requested.²³

In FY 20 (7/1/19 – 6/30/20), DNR offered 895,771 cord equivalents, sold 727,897 cord equivalents and scaled (volume or weight measurement of harvested wood) 706,403 cord equivalents of all species, products, and units of measure across all DNR managed lands. DNR offered 475,007 cord equivalents, sold 404,708 cord equivalents and scaled 368,805 cord equivalents of school trust timber resources in FY 20.

²³ *Minnesota Statutes*, section 90.193

In FY 21 (7/1/20 – 6/30/2), DNR offered 894,118 cord equivalents, sold 734,161 cord equivalents and scaled (volume or weight measurement of harvested wood) 661,671 cord equivalents of all species, products and units of measure across all DNR managed lands. During FY 21, DNR offered 514,833 cord equivalents, sold 406,084 cords equivalents and scaled 359,822 cord equivalents of school trust timber resources.

Of note, in June of 2020, Verso announced their decision to idle paper mills in Duluth, MN and Wisconsin Rapids, WI. This had an immediate effect on the amount of volume sold and scaled from school trust lands. The MN Legislature included “Timber Relief” as part of the 2021 MN Session Laws. This will allow qualifying permits to be extended two years interest free or turned back to DNR. Also, in July of 2021, Huber announced that they will build an oriented strand board or “OSB” mill in Cohasset, MN.

Table 6. Summary of Cords Offered, Sold and Scaled

Fiscal Year	Land Status	New Offered Volume ²⁴ (in cords)	Sold Volume (in cords)	Scaled Volume ²⁵ (in cords)
FY 2020	All DNR Admin	895,771	727,897	706,403
FY 2020	School Trust	475,007	404,708	368,805
FY 2021	All DNR Admin	894,118	734,161	661,671
FY 2021	School Trust	514,833	406,084	359,822

This information is presented in the Division of Forestry’s annual “Minn. Stat., sec. 16A.125 Transfer Certification Report” and is available on the DNR website: <https://www.dnr.state.mn.us/aboutdnr/reports/index.html>

Forest Investments

The 2020 & 2021 Minnesota Legislatures did not appropriate reforestation bonding resources. Reforestation funded with bonding appropriations is not currently charged to the PSF. It is important to understand that bonding investments lower the near term costs to the PSF. They do not appear as expenses on the school trust forest certification reports. The result is reduced expenses and increased net revenue in years where increased bonding for reforestation is applied. Without bonding resources, all reforestation efforts are funded by the

²⁴ Includes new offered volume of cords and thousand board foot units in cord equivalents. Timber offered under Good Neighbor Authority are not included.

²⁵ Scaled volume is volume or weight measurement of harvested wood.

Forest Management Investment Account which is a direct expense on the forest cost certification reports. There will be a subsequent increase in expenses charged and decrease in revenue to the PSF for this reason.

The 2021 Legislature continued the 2017 Legislature approval of an additional road appropriation. A portion of these costs are charged to the PSF in the cost certification process. Additional road maintenance has been required to keep many aging state forest roads operational. These investments to improve and maintain forest access increase future gross revenue that can eventually offset the short-term costs.

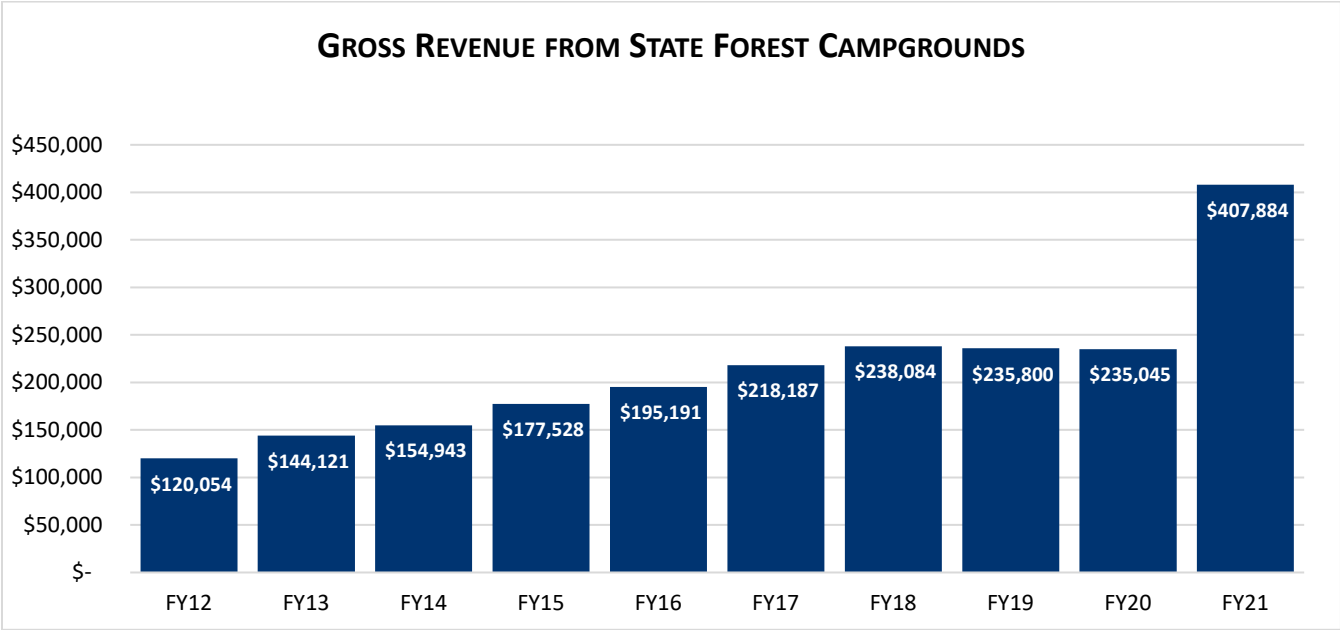
Forestry investments are by nature long-term investments. Money spent on reforestation and stand improvement will not begin to return revenue for many years. Investments in roads also increase the value of school trust timber by allowing summer access in the future. Summer accessible timber usually holds a premium over winter accessible timber.

Surface Leasing and Recreational Use

The DNR leases the surface of school trust land for various use including recreational purposes. Examples of destinations with recreational leases are Hill Annex State Park, Knife River Marina, North Country Hiking Trail and Superior Hiking Trail. The revenue from these leases are considered qualifying revenue and subject to the forest cost certification process. However, the Forestry Division does not certify direct expenses related to surface leasing for purposes not related to timber management. Therefore, the surface leasing revenues are deposited into the FSA, as a pass through account, then into the PSF.

The DNR also manages forest campgrounds located on school trust lands. The major difference between forest campgrounds and surface leasing is the forest campground revenues are not subject to forest cost certification and the Parks and Trails Division subsidizes all related maintenance expense and direct costs.

Figure 6. Gross Revenue from State Forest Campgrounds



In FY 20, the forest campground fees generated revenue of \$235,045. In FY 21, forest campground fees generated about \$407,884, an increase of approximately 73.5% from the previous year. This increase was due to the unprecedented visitation to Minnesota's public lands for recreational use, including camping in state forests during the pandemic.

The Parks and Trails Division, interested groups and stakeholders regularly communicate interest in making investments to certain forest campgrounds on school trust land to improve services and amenities. Though the DNR would like to be responsive to user groups and increase revenues to the school trust, the department does not have legislative authority to recover costs related to forest campground operations, improvements, or maintenance.

Real Estate Management

The DNR enters into various real estate transactions on school trust lands and generates contract revenue through leases,²⁶ easements²⁷ and licenses.²⁸ Additional revenue is generated through public auction land sales of school trust lands.²⁹ In addition, the DNR may enter into land exchanges³⁰ that reposition school trust lands to consolidate surface ownership, improve management, reduce costs and improve opportunities for future revenue potential.

Revenues deposited in the FSA from forest management, subject to forestry cost certification,³¹ are not limited to timber sales and related resource permits. Revenues are also generated from surface leasing transactions (aggregates, agriculture, hunting cabins, miscellaneous commercial and government and lakeshore), permits (resource management access and grant-in-aid), easements (primarily for right-of-way) and utility licenses (land and water crossings). Water crossing utility licenses, wild rice farming leases and state forest campground revenues are not subject to cost certification under statute and are deposited directly to the PSF or in the state FSA in the PSF.

²⁶ *Minnesota Statutes*, section 84.153 (residences); *Minnesota Statutes*, section 89.17 (forest use); and *Minnesota Statutes*, section 92.50 (miscellaneous use)

²⁷ *Minnesota Statutes*, section 84.63

²⁸ *Minnesota Statutes*, section 84.415

²⁹ *Minnesota Statutes*, section 92.12

³⁰ *Minnesota Statutes*, section 94.343

³¹ *Minnesota Statutes*, section 16A.125

Real Estate Management Highlights

Land Exchanges

During the FY 20-21 biennium (7/1/19 – 6/30/21), no school trust land exchanges were completed. DNR continues to work towards the completion of proposed land exchanges as part of the Boundary Waters project, as well as a land exchange project in southern St. Louis County. The project in St. Louis County involves almost 15,000 acres of public land. Title issues on the tax forfeited lands have delayed this project.

For information on the Boundary Waters project, please refer to the [Strategic Projects](#) section of this report.

Land Sales

State law requires the DNR to hold frequent sales of school trust lands³² and other state-owned lands. Revenue generated from the public auction³³ of school trust lands is not subject to forest cost certification. In order to comply with the constitutional and statutory requirements to offer school trust land at public auction, the DNR incurs costs for professional services related to survey, appraisal, legal, advertising and other fees on behalf of the trust prior to the land sale.³⁴

The minimum bid price for school trust lands offered at public auction includes the appraised value and most of the related sale expenses. The department is able to pass on some of the related costs to the high bidder if the land is purchased at auction. If no one purchases the land, the DNR must absorb those costs using other sources, usually general fund dollars. When a school trust parcel sells at public auction the DNR deposits the high bid amount won into the PSF, pursuant to state law. Given that school trust land can only be sold at public auction and not over the counter, DNR incurs the expenses for all unsold parcels and incurs additional costs if it reoffers unsold school trust land at subsequent public auctions.

During FY 20-21, six school trust land sales across two public land sale auctions generated \$524,789 to the PSF. A parcel with road access in Isanti County sold for nearly three times the minimum bid at the 2019 auction. Also sold was a remote, 320-acre parcel in the Kabetogama State Forest located in St. Louis County. The 2020 public auction was conducted as a sealed-bid auction to accommodate the COVID-19 pandemic and social distancing guidelines. The DNR provided an opportunity for public participation in the bid awards through webinar and phone-in options. Bids were accepted for five trust parcels, resulting in four completed sales after the default of one sale for non-payment. A small sale parcel resolved an encroachment on land adjacent to a state facility in Cook County. Three trust parcels in Wadena County were sold for a total of 202 acres. Additional trust acres were offered in Wadena County but did not sell. Those parcels will be re-offered for sale in 2021.

³² *Minnesota Statutes*, section 92.12

³³ Minnesota Constitution, article XI, section 8

³⁴ *Minnesota Statutes*, section 94.16

Condemnations

The DNR acquires school trust land through a condemnation action in which the department pays the value of the land, and applicable resources, to the PSF to permanently extinguish the school trust interest in school trust lands. The government's power of eminent domain to condemn property must be for public use and must provide just compensation for the taking.

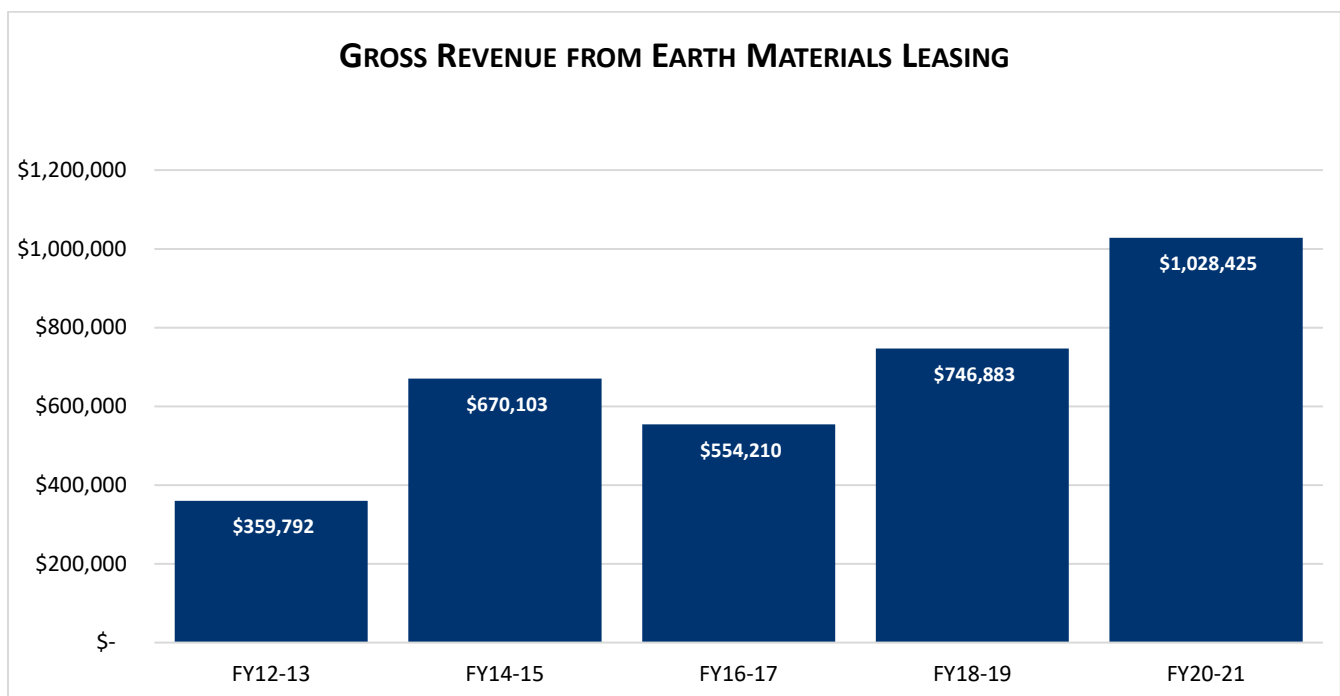
During FY 20-21, no condemnations were completed. There is one condemnation proceeding in process for the Watrous Island Scientific Natural Area (SNA). The condemnation action was filed in Koochiching County District Court on April 29, 2021. The DNR and OSTL have stipulated to the facts and value of \$9,500 based on an appraisal. The school trust land at issue is a 4.5 acre portion of an island adjacent to an existing SNA.

Construction Aggregate Leasing

Surface leasing of construction aggregate resources (sand, gravel, crushed stone and landscape rock) is a relatively profitable way to generate revenue from school trust lands for Minnesota's public schools. The DNR administers earth materials leases to private companies and local governments for the commercial production of aggregate resources and collects lease rental fees and royalty payments for every unit of material removed.

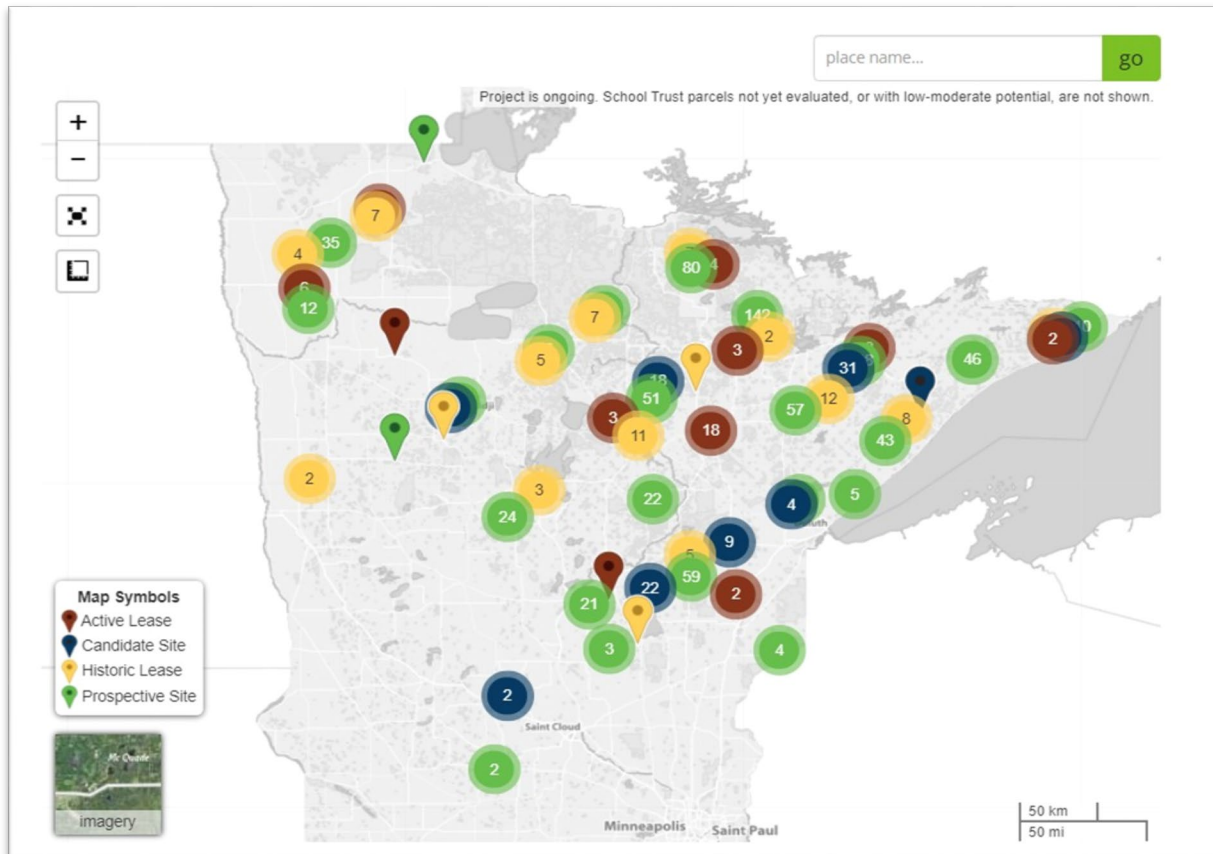
During the FY 20-21 biennium, earth materials leases on school trust lands generated \$1,028,425 in lease rental fees and royalties, an approximate 37.7% increase from last biennium. During the biennium the department initiated 9 new earth materials leases, compared to 6 in the previous biennium which equates to a 50% increase in the initiation of new leases. Gross aggregate revenue is deposited in the FSA and is subject to forest cost certification.

Figure 7. Gross Revenue from Earth Materials Lease Rentals and Royalties



The DNR advertises school trust parcels with the highest aggregate potential on the “School Trust Aggregate Finder” web map application on the department’s website. This tool connects public transportation administrators and private companies with aggregate prospect information and improves public recognition of school trust lease opportunities.

Figure 8. School Trust Aggregate Finder Web Map Application



In unison with lease site promotion, the DNR embarked on a proactive continuous improvement project during the previous reporting period targeting earth materials lease processes, customer satisfaction and lease compliance. The ongoing implementation of this continuous improvement project optimizes business functions and allows DNR to facilitate a growing number of active leases stemming from increased promotion efforts.

Information on school trust aggregate and the “School Trust Aggregate Finder” is available on DNR’s website: www.mndnr.gov

Strategic Projects

Boundary Waters Land Exchanges

Boundary Water and Canoe Area Wilderness History

Congress passed the Wilderness Act in 1964 including the Boundary Water and Canoe Area Wilderness (BWCAW) as part of the National Wilderness Preservation System. The Minnesota Legislature passed legislation that mirrored federal wilderness area restrictions related to resource management. In 1976, the Legislature enacted law that prohibited peat harvesting and mining of state minerals³⁵ within the BWCAW except when Congress declares as national emergency. In 1978, Congress passed the BWCAW Wilderness Act designating the Boundary Waters Canoe Area Wilderness. At that time, approximately 83,000 acres of school trust lands were placed under the wilderness designation and thus incapable of generating revenue. The effort within the State of Minnesota and the United States Forest Service (USFS) to resolve the set-aside of school trust lands have been on-going for many years. Though this project presents complex and challenging problems, both made significant progress since the 1978 Wilderness Act, as described below.

The Hybrid Model

In 2009, the DNR and USFS initiated a new effort to resolve the issue of school trust lands within the BWCAW. A group of interested stakeholders, legislators, USFS and DNR developed and agreed to a hybrid exchange and sale model. The hybrid model's goal is to extinguish school trust interests in the BWCAW. This is accomplished with an exchange of one-third of the school trust lands and sale of the remaining two-thirds to the USFS.

The Minnesota Legislature enacted two statutes in 2012 to expedite the hybrid model. The expedited land exchange statute authorizes DNR to modify its process for appraisal and land title review. It also identifies legislative priority areas. The expedited land sale statute instructs the state to condemn the school trust land interests in the BWCAW and sell directly to the USFS. It also provides the state with flexibility regarding appraisal and title standards.

Evolution of the Hybrid Model

Minnesota formally proposed the two-thirds land sale in 2012. In order to accomplish this project, Minnesota must first extinguish the school trust lands interests prior to a direct sale of the land to the USFS. This entails the state bringing condemnation actions on approximately 52,000 acres situated in three counties within the BWCAW. The Minnesota Legislature appropriated funds to initiate these transactions.

³⁵ *Minnesota Statute*, section 84.523

The USFS required funding, appropriated through the federal budget process, to purchase the 52,000 acres of school trust lands. The USFS continued to be unsuccessful in receiving appropriations after requesting funding for the purchase for many years. To provide assistance with funding requests and maintain momentum on the project, the State of Minnesota and the USFS developed a partnership with The Conservation Fund (TCF). The partners worked together to create a unique solution to this ongoing effort called the “Plan B: Private Forestland Alternative” (Plan B). This alternative includes pivoting on the plan for the sale of the remaining two-thirds school trust lands in the BWCAW. Instead of a sale to the USFS, there will be a new land exchange proposed between TCF and DNR; exchanging school trust lands in the BWCAW for private productive forestlands outside the wilderness. This new land exchange proposal would be implemented in phases.

According to The Conservation Fund, Plan B is embraced by local governments, environmentalists, school districts, timber companies and communities as it plans to secure more than 40,000 acres of productive timberlands for the school trust, while protecting more than 50,000 acres within the BWCAW for enhanced hiking, canoeing, camping and fishing opportunities.

Project #1: The Federal Land Exchange

The hybrid model’s one-third land exchange approach was proposed in 2012. Since that time, the DNR and USFS Superior National Forest actively engage in a land exchange project that would replace up to 31,000 acres of school trust lands in the BWCAW with equivalent land currently in federal ownership that could produce future revenue for the trust. Both parties worked collaboratively to advance the project.

The partners involved in the Federal Land Exchange include: US Forest Service, DNR, OSTL and the Legislative Permanent School Fund Commission.

Project #2: The “Plan B” Private Forestlands Land Exchange Alternative

The hybrid model’s two-thirds sale approach, implemented via the Plan B option, will ensure that revenue generation is achieved in the near-term. The proposal lays out that the State of Minnesota will exchange, in phases, the school trust lands within the BWCAW for equally valued productive timberlands acquired by TCF. The plan is for TCF to acquire the private timberlands and enter into phased land exchanges with the DNR. To close out the project, TCF will complete phased land sales of the former school trust lands to USFS for incorporation into the BWCAW.

The partners involved in Plan B include: US Forest Service, TCF, DNR, OSTL and the Legislative Permanent School Fund Commission.

Status of the Hybrid Model

Through collaborative partnerships and the appropriation of congressional funding, the federal government is much closer to fulfilling its obligation to the State of Minnesota, the PSF and its beneficiaries. During the reporting period, the partners of the project have:

- completed the Environmental Impact Statement assessment,
- purchased high value private forestlands as part of Plan B,

- completed the appraisal process,
- received federal appropriations to facilitate the hybrid approach.

DNR and the project partners – USDA Forest Service and The Conservation Fund – remain committed to addressing the school trust land inholdings within the BWCAW. The project partners are focused on the same outcome that will ensure Minnesota maintains healthy working forests. Additional discussions and work by all project partners is necessary to complete the project in the coming years.

School Trust Land Asset Management Plan

Minnesota’s population, demands on natural resources, and school funding needs have increased significantly since the federal government granted school trust lands to the state in 1857, to provide income for Minnesota’s public schools. What remains unchanged is the intent of the language in the Minnesota Constitution that directs that the management of school trust lands provide a steady stream of income to support Minnesota’s public schools.

To help address these changing conditions, the DNR is working in conjunction with the OSTL in the Office’s effort to create the state’s first School Trust Land Asset Management Plan. The OSTL contracted with an institutional investment consultant, Callan LLC, to develop the plan. The purpose of the project is to create a robust asset management plan that identifies the best and most efficient mix of revenue-generating opportunities to increase the value of school trust assets and related cash flows, while enhancing the compatibility of revenue generation with sound natural resource conservation and management principles.

The OSTL and DNR Project Core Team anticipates seeking input from school trust beneficiary groups, tribal government representatives, conservation organizations and local units of government during its development. A final plan is expected in early 2022.

For more information, please visit the OSTL website at the following link: www.mn.gov/school-trust-lands/

Office of School Trust Lands Strategic Plan Update

During FY 21, the OSTL set out to update its 2018-2028 Strategic Plan,³⁶ developed in 2018. In doing so, the Strategic Plan Project Team, made up of staff from OSTL and DNR, collaborated with school trust beneficiaries, Tribal governments, members of the Legislative Permanent School Fund Commission, county and local governments, conservation organizations, and industry representatives.

³⁶ Minnesota. Office of School Trust Lands. (2021). *Minnesota Office of School Trust Lands 2018-2028 Strategic Plan 2021 Update*. St. Paul, MN: State of Minnesota.

The OSTL thought it was important to update the plan as a number of key events had occurred since 2018. A few of these events include:

- the election of Governor Walz,
- appointment of a new DNR Commissioner,
- reappointment of the School Trust Lands Director,
- emerging opportunities for revenue enhancement and resource stewardship, and
- the COVID-19 pandemic.

The update will guide OSTL in its work and is organized around three main goals and strategies. The first is advancing the school trust lands portfolio, while the second focuses on OSTL's collaboration, and the third and final emphasis is on outreach and engagement.

Status of Compensation

This section is intended to meet the legal requirement for reporting pursuant to Minnesota Statutes, section 84.027, subdivision 18(c), which states that PSF reports issued after the 2013 inventory report must include a status report of the commissioner's progress in maximizing the long-term economic return on lands identified in that report. The lands identified in the 2013 inventory report and their statuses are listed and summarized in this section of the report. The summaries are in three categories: natural resource (Table 7), recreational (Table 8) and statutory (Table 9).

Table 7. Summary of Natural Resource Policy or Designation Impacts and Status

Natural Resource Policy or Designation	Acres	2013 Status	2021 Status
Candidate Research Natural Areas	10,220 acres	Recommendation to modify management.	Management has been modified. Through the STHA, these sites were evaluated and included in the productive timber pool, and if identified by the STHA model, will be evaluated for harvest or for potential stand swapping of like stands.
Natural Area Registry Sites	769 acres (7 sites)	Recommendation to purchase or exchange with a note that the current agreements are	Management has been modified. Most registry sites are not located on productive timberlands. Through the STHA, these sites were evaluated and included in the productive timber pool, and if identified by the STHA

Natural Resource Policy or Designation	Acres	2013 Status	2021 Status
		voluntary and non-binding.	model, will be evaluated for harvest or for potential stand swapping of like stands.
Native Prairie Conservation Sites	7,000 acres	It is unknown whether the Minnesota Prairie Conservation Plan will prohibit revenue generation.	There is no formal designation or informal management of native prairie sites on school trust lands. To date, the Minnesota Prairie Conservation Plan does not prohibit or restrict revenue generation. Any future activity will follow the DNR's internal policy for management of school trust lands (Operational Order 121).
Old Growth Stands	17,800 acres	The objective of the designation is natural resource protection. This designation prohibits revenue generation via policy.	DNR plans to compensate via exchange or condemnation under 2016 Session Laws, Chap. 189, Art. 3, sec. 43. There have been multiple efforts to compensate the PSF for old growth stand designation, which the school trust maintains to meet forest certification requirements. The OLA has instructed DNR to prioritize condemnation of PWA's on school trust lands with dollars from the sale of lands under the 2016 Session Law.

Table 8. Summary of Recreational Policy or Designation Impacts and Status

Recreational Policy or Designation	Acres or Sites	2013 Status	2021 Status
Day-use Areas	36 acres	Day use areas are open for public recreation and provide boating access, swimming and other forms of outdoor recreation. No specific recommendation is provided.	Status as a day-use area does not limit the potential for future revenue generating activities. As a result, it does not restrict or prohibit revenue generation.

Recreational Policy or Designation	Acres or Sites	2013 Status	2021 Status
State Parks	640 acres	School trust lands within the state park system have largely been exchanged out of state park boundaries. Where they are located within state park boundaries, they operate under agreements that permit future revenue generation, or provide compensation to the trust via lease payment. No further action is needed.	DNR continues to manage as described in 2013.
State Recreation Areas	40 acres	Where school trust lands are located within state recreation areas (Cuyuna Country State Recreation Area), the establishing legislation permits future revenue generation. No further action is needed.	DNR continues to manage as described in 2013.
Public Water Access (PWA) Sites	1,100 acres or 177 sites	The objective of the designation is to provide for public recreation. This designation prohibits other forms of revenue generation. The designation would need to be vacated to allow for multiple use. In addition, revenues are not collected on behalf of the PSF.	DNR plans to compensate via condemnation under 2016 Session Laws, Chap. 189, Art. 3, sec. 43. The OLA has instructed DNR to prioritize condemnation of PWA's on school trust lands with sale proceeds under the 2016 Session Law. See pages 39 and 40 for a more detailed description of progress.

Table 9. Summary of Statutory Prohibitions or Limitation Impacts and Status

Statutory Prohibitions or Limitations	Acres	2013 Status	2021 Status
Boundary Waters Canoe Area Wilderness	83,000	The DNR and U.S. Forest Service Superior National Forest are actively engaged in a land exchange project that would replace up to 31,000 acres school trust lands in the BWCAW with equivalently valued land currently in federal ownership that could produce future revenue for the trust. The DNR and USFS are also looking at sales and additional exchanges to address the approximately 53,000 trust acres remaining in the BWCAW.	See pages 32 – 34 for a detailed project status report.
Peatland Protection Act	51,000	The Peatland Protection Act restricts management of the surface and mineral estates for revenue generating purposes. Minnesota Statutes, section 84.035, subdivision 9 directs that the commissioner shall acquire the surface interests, including the peat resources, in these school trust lands by exchange or eminent domain. To-date, funding has not been provided for such acquisition.	Funding has not yet been provided for such acquisition.

Remaining Uncompensated Designation or Policy Provision Restrictions

Minnesota Statute, section 84.027, subdivision 18, paragraph (b) requires that, “any uncompensated designation or policy provision restrictions on the long-term economic return on school trust lands remaining after July 1, 2018, must be compiled and submitted to the Legislative Permanent School Fund Commission for review.”

A list of these uncompensated designation or policy provision restrictions on the long-term economic return on school trust lands that remain after July 1, 2018 is included in Table 10.

Table 10. Summary of Remaining Uncompensated Designation or Policy Restrictions

Policy or Designation	Acres	Remaining Compensation Balance
Public Water Access Sites	1,100	\$13,500,000 Note: See pages 39 and 40 for a more detailed description of progress.
Old Growth Stands	17,800	\$19,900,000
Peatland Protection Act	51,000	\$25,500,000
Total	69,400	\$58,900,000

Progress on Compensation: Public Water Access Sites

In 2015 Session Law, amended in 2016³⁷, the Legislature required DNR to sell or exchange at least \$3 million worth of state-owned, non-trust lands by June 30, 2017. The DNR has conducted land sales under the 2015 Session Law and the amendment in 2016. Table 11 provides a summary of non-trust land sales that have been sold in response to this legislative directive.

To date, no sale proceeds have been used to extinguish the school trust interest on school trust lands where PWA sites are located. The proceeds from land sales are approximately \$687,000 and remain available to extinguish school trust interests. The department is currently evaluating the PWA sites on school trust land proposed for condemnation and will begin to process the transactions in the next biennium.

Table 11. Summary of Non-trust Land Sales Required Under 2015 and 2016 Session Laws

Fiscal Year	Sale Price	Estimated Proceeds (less allowed costs)	Description	County	Acres
FY 2016	\$1,049	\$1,000	Todd County Oxbow	Todd	0.36

³⁷ Laws of Minnesota 2016, chapter 189, article 3, section 43 that requires the DNR to sell or exchange at least \$3 million worth of state-owned, non-trust parcels located outside units of the Outdoor Recreation System and use the proceeds to compensate the PSF.

Fiscal Year	Sale Price	Estimated Proceeds (less allowed costs)	Description	County	Acres
FY 2016	\$19,540	\$18,700	Former Hudson Pit	Douglas	5.00
FY 2016	\$61,360	\$39,700	Lake Alice Township	Hubbard	30.30
FY 2017	\$542,150	\$522,800	Hastings North Forty	Dakota	40.23
FY 2018	\$13,000	\$10,500	Ortonville Fish Hatchery	Big Stone	5.25
FY 2018	\$16,000	\$14,800	Read's Landing	Wabasha	4.30
FY 2018	\$40,000	\$27,000	Koochiching Parcel	Koochiching	30.00
FY 2019	\$19,300	\$16,200	Weissel Parcel	Pine	11.60
FY 2020	\$33,400	\$28,800	Itasca Hwy 48	Itasca	36.83
FY 2020	\$10,500	\$7,300	Tamarac Forestry	Becker	5.00
Est. Total		\$686,800			168.87

Progress on Compensation: Old Growth Stands

Under the session law, no sale proceeds have been used to extinguish the school trust interest on school trust lands with designated old growth stands. The OLA has directed DNR to focus first on condemning PWA sites located on school trust land. It is important to note, the school trust currently maintains designated old growth stands to meet forest certification requirements and maintain dual certification. The legislative requirement to compensate (via condemnation or land exchange) may need to be revisited given the requirement by certification bodies to maintain and protect Type 1 and Type 2 old growth stands.

Progress on Compensation: The Peatland Protection Act

The Peatland Protection Act restricts management of the surface and mineral estates for revenue generating purposes on approximately 51,000 acres. State law directs the commissioner to acquire the surface interests,

including the peat resources, in these school trust lands by exchange or eminent domain.³⁸ To-date, no dollars have been appropriated to fund such acquisition.

Proposals for Compensation

DNR Proposals

Since 2011, the DNR has continued to seek appropriations from a variety of sources to compensate the PSF consistent with Minnesota law. The Department's primary means of seeking those appropriations is through the executive branch operating and capital budget processes. The department included general fund budget and bonding proposals to compensate the trust as part of its larger budget request submitted through the executive branch budget process. In addition, the DNR sought appropriations from the Environment and Natural Resource Trust Fund (ENRTF).

During FY 20 and FY 21, DNR did not seek compensation funding due to other priorities related to the COVID-19 pandemic. Table 12 provides a summary of proposals in previous reporting periods for school trust compensation from general funds, non-general funds and state bond funds.

Table 12. Summary of Funding Proposals for Compensation

Session	Amount Requested	Amount Provided	Funding Source	Notes
2018	\$80M	\$0	Bonding	To start the compensation plan and buyout of certain school trust lands
2017	\$13M	\$0	General Fund	To start the buyout of Peatland Scientific and Natural Areas
2016	\$20M	\$0	Bonding	To start the compensation plan and buyout of certain school trust lands
2015	\$84M	\$0	General Fund	To start the compensation plan and buyout all school trust lands with policies or designations that prohibit long-term economic return

³⁸ *Minnesota Statute*, section 84.035, subdivision 9

Session	Amount Requested	Amount Provided	Funding Source	Notes
2015	\$2M	\$0	ENRTF	To start the buyout of old growth forest complexes
2014	\$20M	\$0	Bonding	To start the compensation plan and buyout of certain school trust lands
2014	\$2.1M	\$0	ENRTF	Buyout of old growth forest complexes
2013	\$5M	\$0	ENRTF	Buyout of Peatland Scientific and Natural Areas
2012	\$5M	\$0	Bonding	To start the compensation plan and buyout of certain school trust lands

Legislative Proposals

Budget proposals are also introduced in the Legislature by individual House and Senate members. Since 2013, a variety of House and Senate bills have been introduced to compensate the PSF. However, these proposals have not been enacted into law.

The 2020 and 2021 Minnesota Legislatures did not seek compensation funding due to other priorities related to the COVID-19 pandemic. The table below provides a summary of legislative proposals in previous reporting periods introduced to address school trust compensation.

Table 13. Summary of Legislative Proposals for Compensation

Session	Amount Requested	Amount Provided	Funding Source	Notes
2019	\$100M	\$0	General Fund: Forecast of Budget Surplus	HF 152 / SF 617 Permanent school fund compensation for land based on general fund forecast funding provided and money appropriated

Session	Amount Requested	Amount Provided	Funding Source	Notes
2017	Funds sufficient to meet requirements outlined in the bill	\$0	General Fund: Forecast of Budget Surplus	HF 2499 / SF 2258 Money appropriated based on general fund forecast to compensate permanent school fund for land
2015	Funds sufficient to meet the requirements outlined in the bill	\$0	General Fund: Unclaimed Lottery	HF 887 / SF 1034 Unclaimed lottery prize money dedicated for acquisition of school trust lands and money appropriated
2014	Funds sufficient to meet the requirements outlined in the bill	\$0	General Fund: Unclaimed Lottery	HF 2439 / SF 2017 Unclaimed lottery prize money dedicated for acquisition of school trust lands, condemnation of school trust lands to be acquired provided and money appropriated

Acknowledgements

Information presented in this report was provided using an interdisciplinary approach. We thank our colleagues who provided insight and expertise that greatly assisted in the production of this report and the information provided within. The department's Land Asset and School Trust Administrator, Trina Zieman, in the Operation Services Division, leads the interdisciplinary development of the report content, ensures compliance with reporting requirements outlined in law, constructs report design, coordinates review and implements edits.

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