

<p style="text-align: center;">State Land Trust Land Department & State Treasurer Program Summary</p>
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Program Overview

The Arizona State Land Trust supports K-12 schools, universities, and other public agencies in Arizona by generating revenues via the sale and use of lands and the investment of proceeds associated with acreage granted to the state. The trust currently includes approximately 9.2 million acres of land and \$6.0 billion of fund balances, as of September 2019.

Background

History and Origin of State Trust Lands

When Congress established the Territory of Arizona in the 1863 Arizona Organic Act, it reserved 2 sections of each township for the benefit of the Territory's common schools (a.k.a. K-12 schools). Congress later passed the Enabling Act in 1910 as a precursor to Arizona gaining statehood. Among its provisions, the Enabling Act required that 2 additional sections of each township be held in trust for common schools and granted 2.3 million acres for other public institutions (*see Trust Beneficiaries and Acreage section*).

An 1881 Act of Congress had already granted the Territory of Arizona 60,000 acres for the University of Arizona, and later a 1929 Act authorized an additional 50,000 acres for the Miners' Hospital Trust. In total, 11 million acres of land were designated as state trust lands. In situations where a designated land parcel was already sold, reserved, or otherwise appropriated (such as a designated parcel being part of tribal reservation land, mining land, or national forest land) the state selected *indemnity in lieu* lands of equivalent acreage in place of already claimed land parcels.

State Land Department

The State Land Department and the system by which trust lands are to be managed was established in 1915 by the State Land Code. In compliance with the Enabling Act and the State Constitution, the Code gave the department authority over all state trust lands and the natural products from these trust lands with the mission of managing trust lands, preserving the trust land's long-term value, and optimizing economic returns to the beneficiaries named in the Enabling Act.

Use and Disposition of Trust Lands

Although trust lands belong to the state, they are not considered public lands. Public lands such as parks or national forests are designated for the benefit of the public, whereas state trust lands are designed to generate revenue for a specific beneficiary (*see Trust Beneficiaries and Acreage section*). In situations where public use of state trust land is permitted, it is closely regulated to protect the value and resources of the land.

The Enabling Act and the Arizona Constitution (approved by Congress in 1911) set forth the following requirements for state trust lands:

- All lands granted shall be held in trust.
- All trust lands shall be appraised at fair market value.
- Trust lands cannot be sold for less than the land's fair market value.
- Land sales or leases in excess of 10 years require a public auction.
- Trust land auctions must be advertised for 10 weeks.
- Trust lands cannot be mortgaged or encumbered in any way.
- All natural products and monetary proceeds of the trust lands shall be subject to the same trust as the lands producing them.

Trust Beneficiaries and Acreage

The Enabling Act named 14 beneficiaries of state trust lands—of which 13 remain—with common schools receiving the largest amount of trust land acreage.^{1/} Of the original 11 million acres granted, 9.2 million are still part of the trust, as shown in *Table 1*.

Land Trust Acreage by Beneficiary			
Trust Land Grants	Beneficiary	Acreage Granted	Acreage as of FY 2019
Common Schools	K-12 Education	9,400,000	8,051,126
Normal Schools	Board of Regents (Distributed to Universities)	200,000	174,786
A & M Colleges		150,000	124,944
Military Institutes		100,000	80,168
School of Mines		150,000	123,256
University Land Code		200,000	137,778
University of Arizona		60,000	48,916
Schools for the Deaf & the Blind		Schools for the Deaf & the Blind	100,000
Subtotal - Education		10,360,000	8,823,532
State Hospital	State Hospital	100,000	71,248
Penitentiaries	Department of Corrections	100,000	76,111
Legislative, Executive & Judicial Buildings	Leg., Exec. & Judicial Buildings	100,000	64,229
Miners' Hospital	Pioneers' Home	100,000	95,231
State Charitable, Penal and Reformatory	50% Pioneers Home	200,000	77,079
	25% Dept. of Corrections		
	25% Dept. of Juvenile Corrections		
Total		10,960,000	9,207,430

As shown in *Table 2*, trust lands are located across all 15 counties within the state.

State Trust Land Acreage by County ^{1/}					
(Acres as of FY 2019)					
County	Acres	County	Acres	County	Acres
Apache	652,643	Greenlee	171,824	Pima	844,272
Cochise	1,370,628	La Paz	254,388	Pinal	1,198,117
Coconino	1,119,868	Maricopa	619,198	Santa Cruz	61,154
Gila	31,231	Mohave	565,128	Yavapai	1,263,398
Graham	496,321	Navajo	369,900	Yuma	186,837
Total Acreage: 9,207,430					
^{1/} Historic and geographic changes in the course of the Colorado River have resulted in approximately 2,530 acres of Arizona State Trust Land being located in California.					

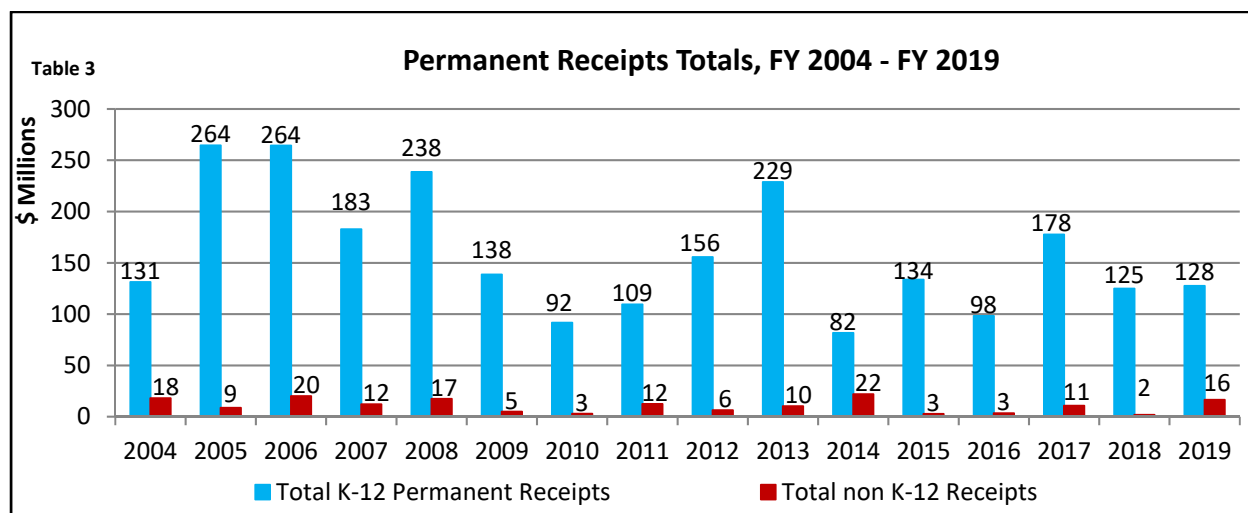
^{1/} County Bonds was a beneficiary of trust land revenues until the bonds were eventually paid. Revenues derived from County Bond lands are now added to the Common Schools grant.

Revenue from State Trust Lands

The State Land Department and State Treasurer both generate revenues from state trust lands. There are 2 forms of revenue generated from state trust lands: "permanent" and "expendable" receipts.

Permanent Receipts

Permanent receipts come from the one-time sale of state trust lands or royalty payments for the extraction of natural resources such as minerals, oil, and natural gas from those trust lands. This one-time revenue, which totaled \$143.9 million for all beneficiaries in FY 2019 is deposited into the appropriate beneficiary's Permanent Fund ^{2/}, which is administered by the State Treasurer. *Table 3* displays the permanent receipts for both K-12 and non K-12 beneficiaries from FY 2004 to FY 2019. K-12 permanent receipts were \$127.5 million in FY 2019 and have ranged from \$81.6 million to \$264.4 million since FY 2004. Comparatively, non K-12 permanent receipts were \$16.4 million in FY 2019 and have ranged from \$1.8 million to \$21.8 million since FY 2004.



Expendable Receipts

Expendable receipts are typically generated as recurring revenue by the Land Department through leases and permits (agricultural, grazing, commercial, etc.), interest from sales contracts, and other revenue from the non-permanent disposition of Trust assets ^{3/}. This revenue, which totaled \$64.1 million in FY 2019 is distributed directly to the beneficiaries for expenditure and use.

The Treasurer also generates expendable receipts by managing the monies in the permanent funds and investing them in stocks, bonds, and interest-bearing securities.

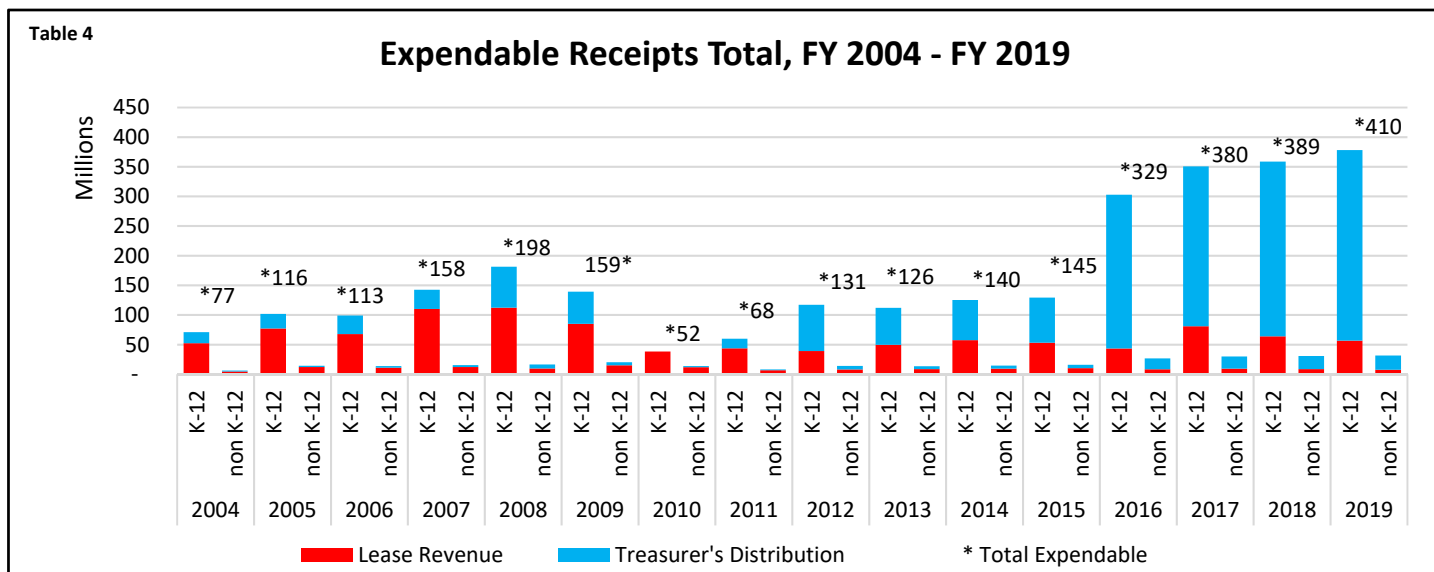
The 13 beneficiaries receive monthly distributions of investment earnings from the Treasurer according to the distribution formula defined in the Arizona Constitution (*see State Treasurer's Distribution Formula and Fund Balances section*). These monies, for which the aggregate amount for all beneficiaries in FY 2019 totaled \$345.4 million, are also distributed directly to the beneficiaries for use.

Table 4 summarizes the expendable receipts for both K-12 and non K-12 beneficiaries from the Land Department and Treasurer combined, which were \$409.5 million in FY 2019 (\$377.9 million for K-12 and \$31.6 million for non K-12) and have increased from \$70.9 million for K-12 and \$6.1 million for non K-12 since 2004.

^{2/} Each beneficiary has its own Permanent Fund. Revenues are deposited into a particular beneficiary's fund based on which beneficiary the relevant parcel of land was assigned to.

^{3/} Leases (expendable receipts) grant access to trust land; royalties (permanent receipts) must be paid for the actual extraction of minerals or resources.

As shown in *Table 4*, total expendable receipts for K-12 only increased substantially in FY 2016 due to Proposition 123 and reached a historical high of \$377.9 million in FY 2019. As shown in *Table 5*, the total expendable receipts, including both the Treasurers' distribution and the Land Department lease revenues, totaled \$409.6 million for all beneficiaries combined in FY 2019.



State Treasurer's Distribution Formula and Fund Balances

The Treasurer's distributions from the Permanent Funds to the beneficiaries are based on the formula outlined in Article X, Section 7 of the Arizona Constitution.

Prior to 2012, the distribution formula was based on a 5-year average inflation-adjusted investment return, which was multiplied by the 5-year average of a beneficiary's Permanent Fund balance. In 2012, Proposition 118 set a fixed distribution rate of 2.5% of the 5-year average value of a beneficiaries' permanent fund to reduce the year-to-year volatility of distribution payouts.

Proposition 123 (approved by voters at the May 2016 special election) increased the annual distribution rate from the State Land Trust Permanent Fund from 2.5% to 6.9% from FY 2016 through FY 2025. ^{4/}

While the Treasurer's distribution transfers monies out of the beneficiaries' Permanent Funds to the beneficiaries themselves, the Permanent Fund balances have continued to grow due to offsetting increases from new land sales (which are deposited into the Permanent Funds) and investment returns. As shown in *Table 6*, for example, the K-12 Permanent Fund balance has increased from \$2.2 billion in 2009 to \$5.6 billion as of September 2019.

The Treasurer's Office reports a 1-year investment return on the land trust endowment funds of 6.38% in FY 2019, a 3-year return of 8.8%, a 5-year return of 7.1%, and a 10-year return of 9.9%. ^{5/}

Permanent receipts from land sales and royalties generated by the State Land Department also added \$143.9 million to the Permanent Fund balances in FY 2019. Over the past 5 years, land sales and royalties have averaged \$139.3 million per year. ^{6/}

^{4/} Proposition 123 set the FY 2016 K-12 distribution at a fixed dollar amount, \$259,266,200, rather than 6.9%. The Proposition also allows the Legislature to reduce the distribution rate to as low as 2.5% if the 5-year average trust fund balance declines relative to the previous 5 years. The Proposition also allows for the suspension of required K-12 inflation funding increases if certain economic performance triggers are met. The Proposition does not alter beneficiaries' other expendable receipts (i.e. lease revenues) nor permanent receipts (i.e. land sales). (See the Classroom Site Fund section for additional information on the distribution requirements of K-12 land trust funds under Proposition 123.)

^{5/} <https://aztreasury.gov/investments/endowment-details/> referenced September 24, 2019.

^{6/} As shown in the monthly land receipts provided by the Arizona State Land Department.

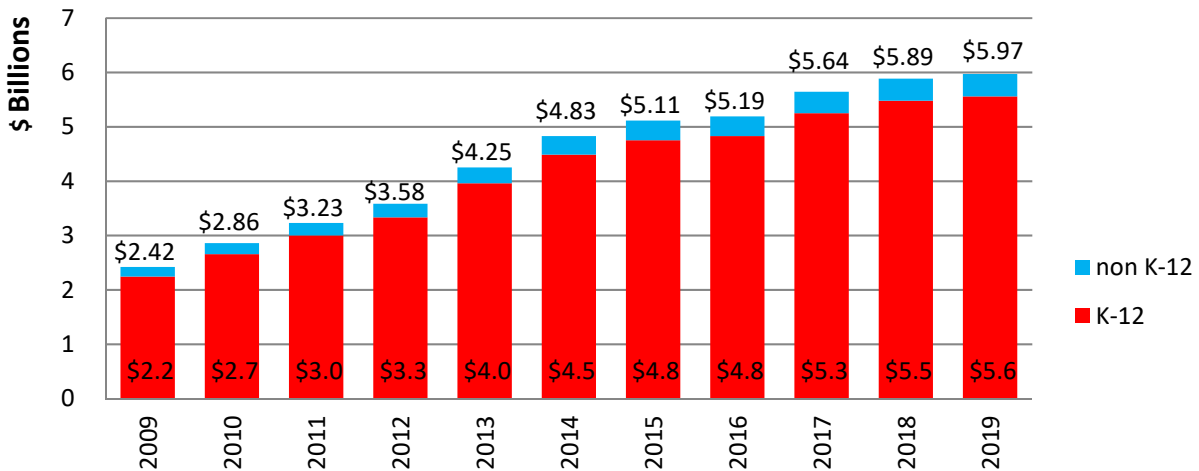
Table 5

FY 2019 State Trust Land Revenue

<u>Trust Land Grants</u>	<u>Beneficiary</u>	<u>Land Dept. Expendable Receipts</u>	<u>Treasurer's Distribution</u>	<u>Total Expendable Receipts</u>	<u>Permanent Receipts</u>	<u>Total Receipts</u>
Common Schools	K-12 Education	\$56,752,100	\$321,245,600	\$377,997,700	\$127,524,900	\$505,522,500
Normal Schools	Board of Regents (Distributed to Universities)	190,500	346,300	536,800	142,700	679,500
A & M Colleges		314,400	844,900	1,159,300	4,700	1,164,000
Military Institutes		68,100	46,400	114,500	800	115,300
School of Mines		173,700	958,400	1,132,100	41,200	1,173,300
University Land Code		679,200	1,720,600	2,399,800	6,574,300	8,974,100
University of Arizona		496,600	5,904,400	6,401,000	457,400	6,858,400
Schools for the Deaf and the Blind	Schools for the Deaf and the Blind	<u>183,800</u>	<u>463,300</u>	<u>647,100</u>	<u>120,000</u>	<u>767,100</u>
Subtotal - Education		\$58,858,400	\$331,529,900	\$390,388,300	\$134,866,000	\$525,254,300
State Hospital	State Hospital	\$ 340,800	\$ 565,000	\$ 905,800	\$ 46,700	\$952,500
Penitentiaries	Dept. of Corrections	1,196,300	1,273,000	2,469,300	6,500	2,475,800
Legislative, Executive & Judicial Buildings	Legislative, Executive and Judicial Buildings	129,700	699,900	829,600	50,700	880,300
Miners' Hospital	Pioneers' Home	1,833,600	1,897,400	3,731,000	1,236,300	4,967,300
State Charitable, Penal and Reformatory	50% Pioneers Home	892,800	4,729,400	5,622,200	3,874,600	9,496,800
	25% Dept. of Corrections	446,400	2,364,700	2,811,100	1,937,300	4,748,400
	25% Dept. of Juvenile Corrections	<u>446,400</u>	<u>2,364,700</u>	<u>2,811,100</u>	<u>1,937,300</u>	<u>4,748,400</u>
TOTAL		\$64,144,400	\$345,424,000	\$409,568,400	\$143,955,400	\$553,523,800

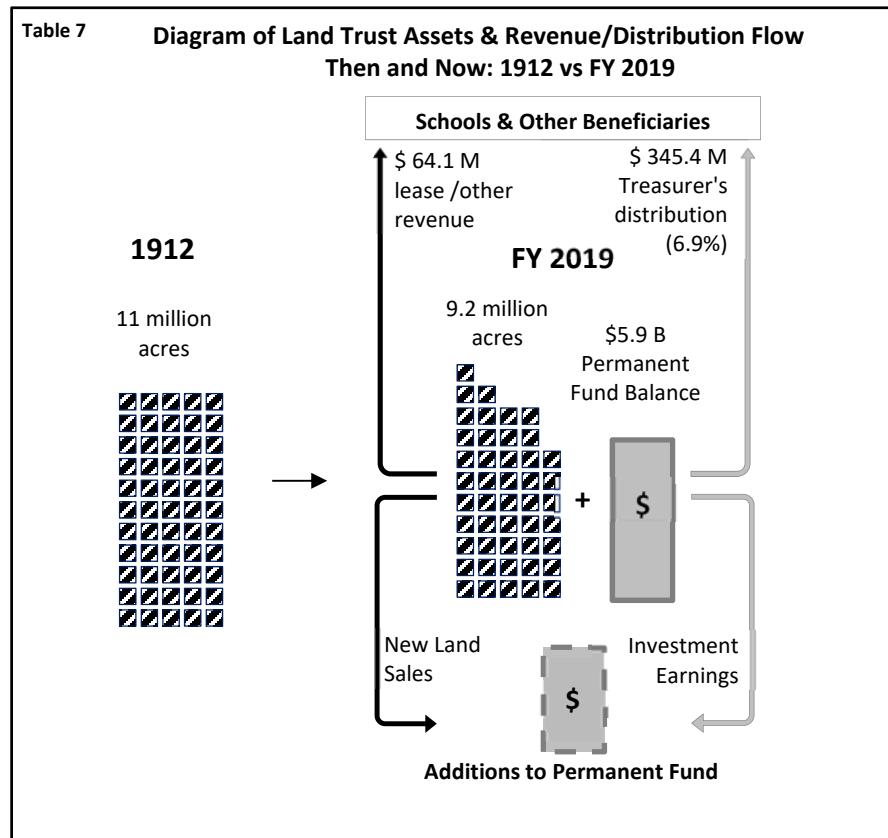
Table 6

Permanent Fund Balances, FY 2004 - FY 2019



1/ Figures for total Permanent Balances shown above charts bars. Figures for K-12 total balances shown at base of chart bars. Figures for non K-12 balance are not displayed.

Table 7 provides a summary diagram of the flow of funds related to the Land Trust: Over time, 1.8 million of the original 11 million acres have been sold, leaving 9.2 million acres and resulting in a \$5.9 billion fund balance as of September 2019, including investment returns. Each year, the investment earnings on the fund balance (6.38% in FY 2019) and the proceeds from additional land sales (\$143.9 million in FY 2019) increase the value of the beneficiaries' permanent funds. At the same time, the Treasurer distributes 6.9% of the fund balance to the beneficiaries (\$345.4 million in FY 2019) while the Land Trust generates lease revenues (\$64.1 million in FY 2019) that also go directly to the beneficiaries.



Classroom Site Fund

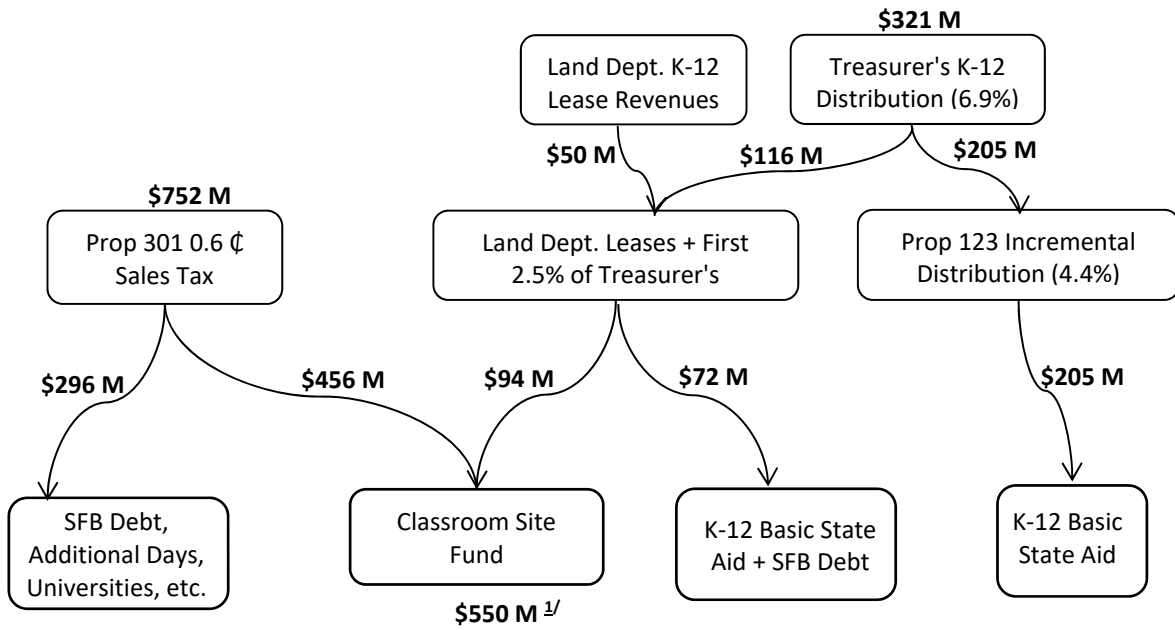
Passed by voters in 2000, Proposition 301 established the Classroom Site Fund (CSF) to dedicate new resources for teacher salaries, classroom size reduction, and dropout prevention programs. The CSF is funded by both the land trust as well as a 0.6¢ educational sales tax that Proposition 301 put into effect through FY 2021.

As shown in Table 8, after funding other obligations (e.g. School Facilities Board debt, additional school days, universities, etc.) all revenue from the sales tax goes to the CSF (\$456.4 million in FY 2019).

Of the 6.9% Treasurer's distribution, the incremental 4.4% (\$204.8 million in FY 2019) authorized under Proposition 123 all goes toward Basic State Aid. The other 2.5% of the distribution (\$116.4 million in FY 2019) is combined with expendable lease revenues generated by the Land Department (\$49.9 million in FY 2019). A.R.S. § 37-521 requires that of these combined funds (lease revenues + 2.5% distribution), any expendable receipts above \$72.3 million must be deposited into the CSF. As a result, the CSF received \$93.8 million in FY 2019 from the Land Department and Treasurer combined, in addition to the \$456.4 million from the sales tax.

Table 8

FY 2019 Land Trust K-12 & Prop 301 Classroom Site Fund Revenues



^{1/} Excludes prior year carry forward.