
Legislative Fiscal Division

Revenue Estimate Profile

Common School Interest and Income

Revenue Description: The Common School trust is a fund set up for the support of schools using income generated from state land and the subsequent interest on the account.

Lands granted by the federal government to the state for the benefit of public schools generate income. The common school trust is actually part of the trust and legacy trust fund that includes nine other trusts. Prior to FY 1996, interest and income from the common school trust was deposited in the state equalization account. Beginning in FY 1996, this interest and income was deposited in the general fund, as mandated by SB 83, passed by the 1995 Legislature. Beginning FY 2003, House Bill 7 from the August 2002 special legislative session changed the deposit to the state special revenue guarantee account and statutorily appropriated the money for schools. The estimates show the amount of revenue deposited to the guarantee account and are net of amounts diverted for DNRC administration costs and those deposited directly to the school facility and technology account. With the enactment of Senate Bill 65 by the 2009 Legislature, diverted revenue can be derived from: 1) distributable revenue; 2) sale of easements; 3) timber, except from public school and Montana university system lands; 4) mineral royalties; and 5) fees from sales of state lands except lands granted by the Morrill Act. The amount of the permanent revenue (mineral royalties and easements) diverted from the common school trust reduces the growth of the trust fund balance and, hence, reduces the amount of future distributable interest earnings.

With the enactment of HB 152 by the 2009 Legislature, revenue from the value of timber over 18 million board feet and revenue from power site rents are no longer deposited to the guarantee account, but are deposited to the school facility and technology account. Mineral royalty revenue required to pay interest and principal on the SB 495 loan is not included since the loan was repaid in FY 2008. All net (excluding amounts for administration) mineral royalty revenue is deposited to the guarantee account for transfer to the school facility and technology account. These items are explained below.

Common school lands produce two kinds of revenue: 1) distributable income such as interest earnings, agricultural rents or crop shares, and timber sale revenue; and 2) permanent income that is returned to the trust such as income from the sale of minerals (see the effects of Senate Bill 495 from the 2003 legislative session below), land, and easements. Excluding the amount of revenue diverted for DNRC administration (Senate Bill 65 enacted by the 2009 Legislature) and to the school facility and technology account (House Bill 152 enacted by the 2009 Legislature), 95% of certain distributable revenue is available to fund public schools. Timber revenue is allocated: 1) 5% to the permanent school trust; 2) revenue received from production over 18 million board feet is deposited to the school facility and technology account; and 3) any remainder to the guarantee account for the support of public schools.

As of October 1, 1995, all fixed-income investments held by the state's major trust funds (which include the trust and legacy fund of which the common school trust is a part), were transferred to a newly-created Trust Funds Bond Pool (TFBP). The majority of common school trust funds are invested as part of the TFBP. Some funds, however, are invested on a short-term basis in the state's Short Term Investment Pool (STIP). The state Constitution prohibits the investment of common school trust funds in common stock. Interest income is distributed 95% to the guarantee account and 5% to the trust.

Senate Bill 495 (enacted by the 2001 Legislature) authorized DNRC to purchase the mineral production rights (with a loan from the coal severance trust) from the common school trust. The department subsequently purchased \$138.9 million of net future mineral royalties from the school trust for \$46.4 million. Since these royalties will no longer be deposited to the trust, interest earnings from the trust corpus are lessened. It is estimated that the trust balance will be at least \$92.5 million less after all the \$138.9 million has been distributed. The net mineral royalties are first used to pay the principal and interest of the \$46.4 million loan with the remainder deposited to the guarantee account to fund base aid. Since the loan was paid off in FY 2008, SB 2 (May 2007 special session) directs that all net mineral royalties (until the total amount of \$138.9 million that was purchased is received) are to be deposited to the guarantee account and then transferred to the school facility improvement account (changed to the facility and technology account in HB 152 enacted by the 2009 Legislature). The amount of \$138.9 million in net mineral royalties was achieved at the end of FY 2010. After FY 2010, all mineral royalties (except those diverted for administration costs under SB 65 enacted by the 2009 Legislature) will be deposited to the permanent school trust fund. For further information and analysis on Senate Bill 495 contact the Legislative Fiscal Division for a copy of the two-part report: "Senate Bill 495-Implementation, Impacts and Implications."

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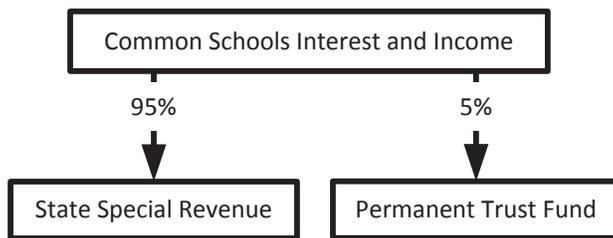
Statutory Reference:

Tax Rate – NA
 Distribution (MCA) – Montana Constitution Article X, Section 5; 20-9-342 (school technology); 20-9-622 (guarantee account)
 Enabling Act, Section 10
 Other (MCA) – DNRC trust land administration diversion (77-1-108 & 77-1-109)
 DNRC land bank administration diversion (77-2-362)
 Date Due - the last business day of February following the calendar year in which the money was received (20-9-342).

Applicable Tax Rate(s): N/A

Distribution: As described above, 95% of interest and income from the common school permanent trust fund (excluding a portion of timber sale revenue and after amounts diverted for DNRC administration) is distributed to the state special revenue guarantee account and is statutorily appropriated for schools. The remaining 5% is deposited to the permanent trust fund. The amount of timber sale revenue over 18 million board feet is deposited to the school facility and technology account. Up until the total of \$138.9 million of purchased royalties was reached, the portion of mineral royalties not used administration was deposited to the guarantee account and, with the enactment of SB 2 (May 2007 special session), transferred to the school facility and technology account (renamed in HB 152 enacted by the 2009 Legislature). Since the \$138.9 million was reached late in FY 2010, mineral royalties will again be deposited to the common school permanent trust fund and will generate additional distributable income. The amounts deposited to the guarantee account are shown in this revenue source.

Distribution Chart:



Summary of Legislative Action:

Senate Bill 369 – The legislation requires the Board of Land Commissioners to sell the cabin and home sites on school trust lands by July 2035. Distributable revenue from common school trust lands is deposited to the guarantee account and used to fund schools.

Common School Interest and Income – Legislation Passed by 63rd Legislature			
State Special Revenue Impact (\$ Millions)			
Bill Number and Short Title	FY 2013	FY 2014	FY 2015
SB0369 Revise state cabin site leasing laws	\$0.000	(\$0.089)	(\$0.137)
Total State Special Revenue Impact	\$0.000	(\$0.089)	(\$0.137)

Collection Frequency: Revenue is received monthly. However, distribution to the state special revenue fund takes place three times per year.

% of Total General Fund Revenue: N/A

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Revenue Estimate Methodology:

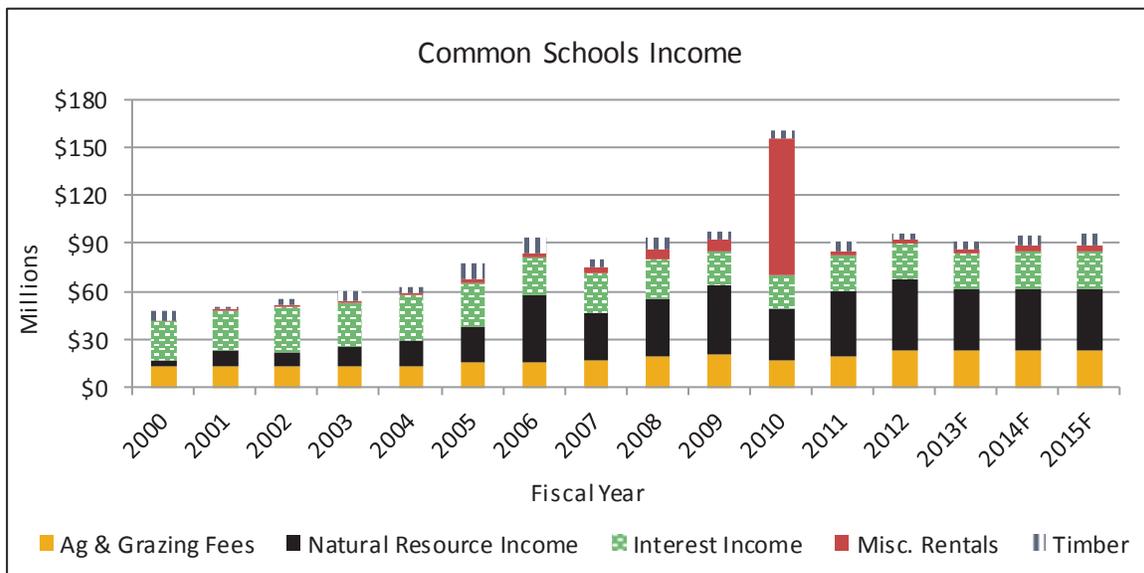
The estimate for interest and income from the common school trust determines the net amount of revenue that will be deposited to the guarantee account. This means that in addition to estimating the various revenues from the common school trust, estimates of the diversions for DNRC administration costs that reduce the amount of revenue deposited to the guarantee account must also be estimated. Therefore, the estimated amounts shown for this revenue source are not total revenues, but are net of diversions.

Data

Data from the state accounting system (SABHRS) provide a history of each individual interest and income revenue component from which estimates can be made. Department of Natural Resources and Conservation (DNRC) annual reports and other data provide additional information such as mineral prices and production. DNRC provided data for easement sales and timber harvest volumes. IHS provides future estimates of West Texas Intermediate oil and national well head natural gas prices.

Analysis

The estimate is derived by first estimating the revenue components and then estimating the amounts of the diversions.



Revenue Components

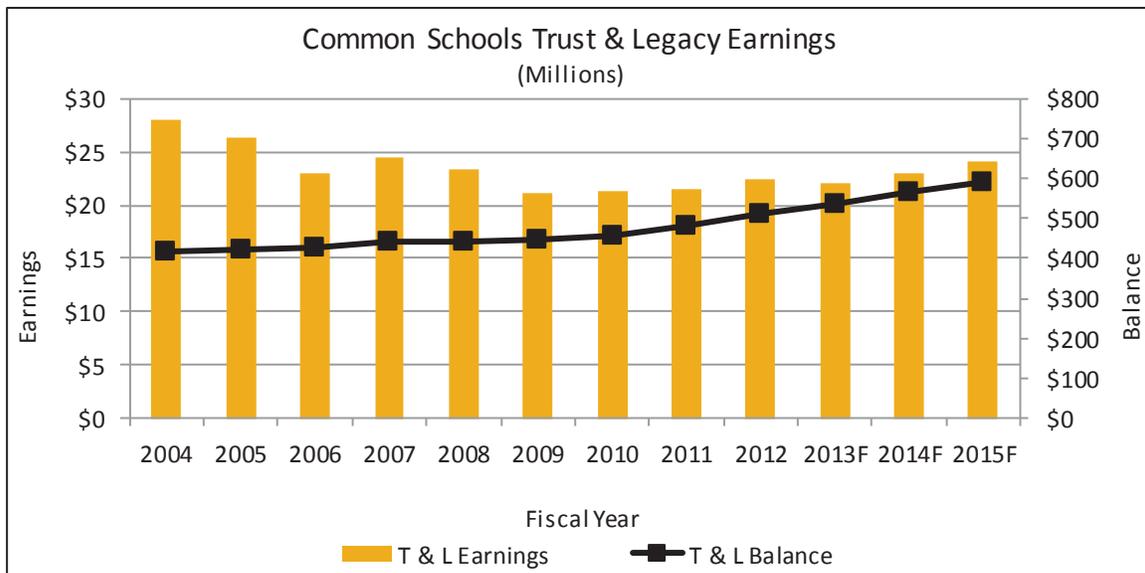
1. Agricultural Fees – Fees are based on a crop share basis. The estimates assume that fees will be the same as the most recent fiscal year for all forecast years.
2. Timber – Estimates of timber harvest revenue from common school trust lands are taken directly from DNRC estimates.
3. Oil & Gas Bonuses – With record highs in energy prices in the past and increased competition to obtain mineral leases, bonus payments have varied substantially. This can cause problems in estimating, which is dealt with primarily by taking a six year average of past bonus payments.
4. Grazing Fees – Rates are tied to the price of cattle, which is expected to be similar to the base year. The amount of fees received in the most recent fiscal year is used in all forecast years.
5. Oil & Gas Leases – For each fiscal year estimated, an average annual growth rate over the previous eight year period was applied.
6. Oil & Gas Penalties – For each fiscal year estimated, the ratio of the previous year’s penalties to the previous year’s oil and gas lease revenue was multiplied by that year’s estimate for oil and gas lease revenue.
7. Miscellaneous Rentals – Due to historical anomalies (FY 2008-2010 due to the Avista river bed lease and the agreement of Arch Coal to pay for the mineral rights to Otter Creek Coal), the amount collected in most recent fiscal year is used for all forecast years.
8. Short-term Investment Pool (STIP) – Because revenue initially deposited in the common school trust is invested on a short-term basis (about one month) before being invested in the T & L fund, a short-term rate is used to calculate the earnings. The short-term rate is a composite of IHS forecasts for the 3-month commercial paper, 3-month treasury bill, and 6-month treasury bill rates.

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9. Mineral Royalties – Mineral royalties are received from the mining of oil, natural gas, coal, sand and gravel, and other smaller sources. Since the effects of SB 495 (enacted by the 2001 Legislature effective FY 2002) ended late in FY 2010, mineral royalties are again deposited to the common school trust and become part of the trust corpus. The additional corpus will generate additional earnings. The estimate for mineral royalties is obtained by multiplying together estimates for production, price, and the applicable royalty rate.
- Production – Oil and natural gas production is estimated by increasing the previous fiscal year’s production by the growth rate obtained from a two-year average of the estimates for statewide oil and natural gas production (see the Oil and Natural Gas Production Tax profile). Coal production on state lands comes primarily from a single coal company with minor amounts from another company. Calendar year information on projected production and percentage of production on state lands was obtained by surveying coal companies, including the companies producing on state lands, from which the amount of production on state lands is derived. Fiscal year production is obtained by averaging production for the current and previous calendar years. All other mineral production was held constant at the amount of gravel royalty collection in the base year.
 - Price – Oil prices are calculated by increasing the previous year’s Montana price by the growth between the average West Texas Intermediate price estimates obtained from IHS for the four quarters of the same fiscal years. The same methodology is used for natural gas with the driving factor being the IHS estimated national well head price. Coal price is determined by increasing the previous fiscal year’s price by a growth rate obtained from a two-year average of the calendar year estimates for Montana coal prices (see the Coal Severance Tax profile).
10. Trust and Legacy Earnings – The monetary assets of the common school trust are pooled with monetary assets of other land trusts (termed “Trust and Legacy”) and invested by the Board of Investment in the trust funds bond pool. Based on the number of shares each trust owns, a share of the earnings is deposited in each trust. For the common school trust, the previous fiscal year share used. The pool balance grows when permanent revenue is deposited from the various land trust, including the common school trust. However, due to the ending of SB 495 in FY 2010, mineral royalties (permanent revenue) once again are added to the balance. The estimation of the total pool earnings is a three stage process:
- Earnings from new deposits – This additional money initially earns interest at the short-term rate before it is invested in a longer term investment. Also included in these calculations are short-term earnings from the average balance in the common school Land Bank Trust Fund.
 - Earnings from existing balance – The majority of these funds have been invested in bonds purchased over the past several years.
 - Non-portfolio earnings – Money not invested in the trust funds bond pool earns interest at the short-term rate.
- Once the total amount of the pool earnings has been estimated by summing the above three items, the common school is applied.



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Diversions

Diversions fund operational costs in DNRC, but reduce the amount of permanent and distributable revenue that would have been deposited to the common school trust or distributed to the trust beneficiaries. To determine future diversion amounts, estimates provided by DNRC were used. These estimates relied entirely on distributable revenue to fund the costs (See the trust land administration account below).

- Trust Land Administration Account – The total expenditures requested to be made from this account can be funded from distributable revenue, permanent revenue, or a combination of the two. It is up to the DNRC to decide. If permanent revenue is chosen, the corpus of the trust will not grow as rapidly as it would have and interest earnings from the trust will be less. If distributable revenue is chosen, the amount deposited to the guarantee account to fund public schools will be less, thus requiring more funding from the general fund.

Adjustments and Distribution

Once total revenue and total diversions have been estimated, the amounts are distributed:

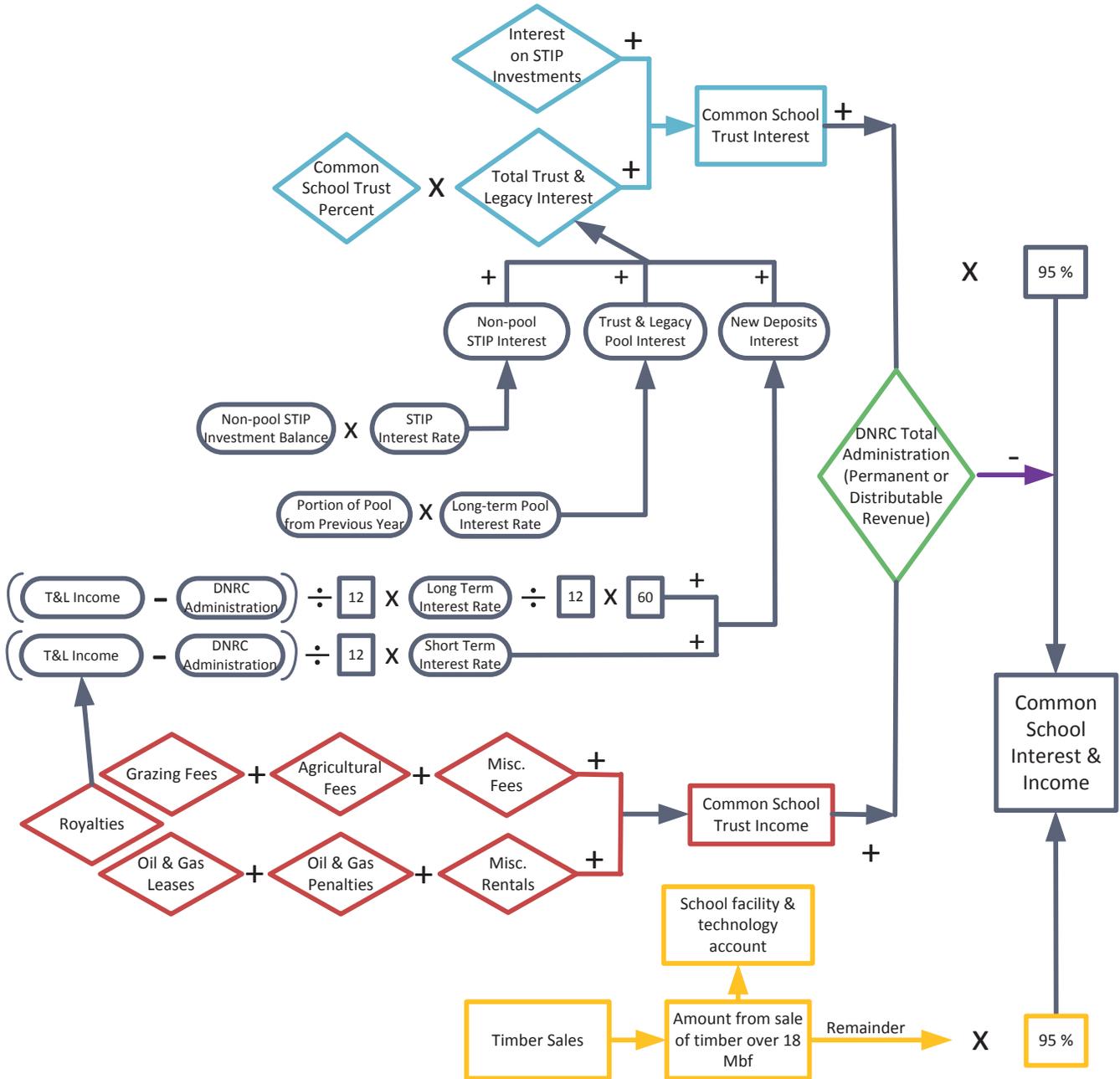
- 95% of the distributable interest and income (excluding a portion of timber revenue) net of diversions is deposited to the guarantee account and the remaining 5% is returned to the permanent trust fund. The money deposited to the guarantee account is used to fund public schools.
- The value received from timber sales over 18 million board feet is distributed to the school facility and technology account. The amount of money distributed to the account in one year is spent in the next year.

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Forecast Methodology:



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Revenue Estimate Assumptions:

This section contains the assumptions used to generate the revenue estimates contained in Senate Joint Resolution 2. It does not reflect changes, if any, enacted by the 2013 Legislature that may affect future estimates of this revenue source.

	<u>t</u>	<u>Total Rev.</u>	<u>GF Rev.</u>	<u>TFBP</u>	<u>STIP</u>	<u>Common</u>	<u>SB495</u>	<u>Trust Land</u>
	<u>Fiscal</u>	<u>Millions</u>	<u>Millions</u>	<u>Interest</u>	<u>Interest</u>	<u>School Share</u>	<u>Loan Pay.</u>	<u>Expense</u>
				<u>Millions</u>	<u>Millions</u>	<u>T&L</u>	<u>Millions</u>	<u>Millions</u>
Actual	2002	50.875	48.938	29.627	0.103	0.933		
Actual	2003	48.977	0.000	29.147	0.068	0.931	0.000	-3.551
Actual	2004	55.663	0.000	30.087	0.054	0.929	-1.821	-3.312
Actual	2005	68.036	0.000	28.106	0.270	0.927	-2.650	-3.680
Actual	2006	82.606	0.000	24.428	0.408	0.928	-10.849	-3.905
Actual	2007	70.429	0.000	26.207	0.268	0.927	-19.473	-3.130
Actual	2008	83.026	0.000	25.160	0.129	0.926	-11.574	-3.809
Actual	2009	61.821	0.000	22.711	0.066	0.926	0.000	-9.943
Actual	2010	133.315	0.000	22.916	0.018	0.932	0.000	-8.674
Actual	2011	60.144	0.000	23.194	0.033	0.929	0.000	-8.837
Actual	2012	102.391	0.000	24.175	0.028	0.930	0.000	-8.717
Forecast	2013	68.129	0.000	23.209	0.029	0.930	0.000	-9.107
Forecast	2014	65.698	0.000	24.129	0.030	0.930	0.000	-9.085
Forecast	2015	61.956	0.000	25.164	0.044	0.930	0.000	-9.073

	<u>t</u>	<u>Trust Income</u>	<u>New Deposit</u>	<u>Non Pool</u>	<u>Non Pool</u>	<u>SB495</u>	<u>Oil&Gas</u>
	<u>Fiscal</u>	<u>New Deposit</u>	<u>Long Term</u>	<u>STIP</u>	<u>STIP Bal</u>	<u>Interest</u>	<u>From Schools</u>
		<u>Millions</u>	<u>Rate</u>	<u>Rate</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>
Actual	2002	2.348	6.2%	2.6%	7.334		
Actual	2003	2.363	5.7%	1.4%	6.242		
Actual	2004	2.972	5.4%	1.3%	7.050		
Actual	2005	1.458	5.2%	2.4%	12.107	-3.006	
Actual	2006	1.425	5.2%	4.1%	3.863	-2.256	
Actual	2007	7.174	5.4%	4.7%	14.954	-1.505	
Actual	2008	3.102	5.3%	3.1%	2.461	-0.283	
Actual	2009	4.126	5.1%	1.0%	4.161	0.000	
Actual	2010	10.710	4.8%	0.2%	11.340	0.000	
Actual	2011	22.233	4.4%	0.1%	15.565	0.000	
Actual	2012	31.517	3.8%	0.1%	11.492	0.000	12.336
Forecast	2013	26.766	3.4%	0.1%	11.492	0.000	8.917
Forecast	2014	27.198	3.8%	0.1%	11.492	0.000	8.203
Forecast	2015	30.366	4.2%	0.2%	11.492	0.000	7.306

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	<u>t</u>	<u>Grazing</u>	<u>Agriculture</u>	<u>Misc.</u>	<u>O&G Lease</u>	<u>O&G Bonus</u>	<u>O&G Penalty</u>	<u>Misc.</u>
	<u>Fiscal</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>
Actual	2002	5.467	6.999	0.000	1.540	0.478	0.335	1.244
Actual	2003	5.243	7.975	0.000	1.575	0.301	0.399	1.349
Actual	2004	4.971	8.051	0.000	1.649	0.871	0.534	2.156
Actual	2005	5.918	8.816	0.000	1.893	3.827	0.641	2.057
Actual	2006	6.277	9.453	0.000	2.331	13.005	0.864	2.193
Actual	2007	7.057	9.408	0.000	2.506	2.102	1.067	2.510
Actual	2008	6.408	12.282	0.000	2.701	2.154	0.812	6.418
Actual	2009	6.470	14.081	0.000	2.760	11.828	0.541	6.795
Actual	2010	5.861	10.985	0.000	2.873	7.243	0.615	85.247
Actual	2011	5.984	13.464	0.000	2.937	13.234	1.008	2.840
Actual	2012	7.471	15.009	0.000	3.672	15.104	1.411	3.162
Forecast	2013	7.471	15.009	0.000	4.037	11.205	1.551	3.162
Forecast	2014	7.471	15.009	0.000	4.366	7.627	1.677	3.162
Forecast	2015	7.471	15.009	0.000	4.726	7.627	1.816	3.162

	<u>t</u>	<u>Int. Land</u>	<u>Int. STIP</u>	<u>Int. Trust</u>	<u>Timber</u>	<u>Res. Dev.</u>	<u>Commercial</u>	<u>Avista</u>
	<u>Fiscal</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Millions</u>	<u>Lease</u>	<u>Millions</u>
							<u>Millions</u>	
Actual	2002	0.000	0.305	27.775	3.625	-0.504		
Actual	2003	0.020	0.189	27.202	3.606	-0.499		
Actual	2004	0.003	0.200	27.991	0.667	-0.518		
Actual	2005	0.026	0.408	26.306	3.652	-0.686	-0.067	
Actual	2006	0.000	0.642	23.048	2.879	-1.003	-0.068	
Actual	2007	0.000	0.733	24.541	1.929	-0.722	-0.057	
Actual	2008	0.000	0.606	23.428	2.251	-0.786	-0.057	
Actual	2009	0.000	0.293	21.094	1.855	-1.129	-0.096	
Actual	2010	0.000	0.063	21.370	2.990	0.000	0.000	
Actual	2011	0.000	0.042	21.570	2.713	0.000	0.000	
Actual	2012	0.000	0.053	22.515	1.886	0.000	0.000	
Forecast	2013	0.000	0.031	21.977	2.438	0.000	0.000	4.327
Forecast	2014	0.000	0.030	22.879	2.753	0.000	0.000	4.401
Forecast	2015	0.000	0.043	23.952	2.793	0.000	0.000	0.000

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	<u>t</u>	<u>Total</u> <u>Timber</u> <u>Millions</u>	<u>Timber</u> <u>Sales Pgm.</u> <u>Millions</u>	<u>School</u> <u>Technology</u> <u>Millions</u>	<u>Oil</u> <u>Royalties</u> <u>Millions</u>	<u>Gas</u> <u>Royalties</u> <u>Millions</u>	<u>Coal</u> <u>Royalties</u> <u>Millions</u>	<u>Other</u> <u>Royalties</u> <u>Millions</u>
Actual	2002	3.625	0.000	1.822	2.390	1.523	2.837	0.144
Actual	2003	5.508	-1.829	0.000	3.682	1.995	3.877	0.148
Actual	2004	2.968	-1.941	3.179	4.852	2.718	4.677	0.170
Actual	2005	10.602	-2.536	4.414	7.966	4.330	4.240	0.194
Actual	2006	10.227	-2.707	4.641	14.759	6.317	4.180	0.356
Actual	2007	5.398	-2.573	0.896	15.133	5.083	3.729	0.148
Actual	2008	7.317	-3.117	1.949	19.367	5.660	5.865	0.156
Actual	2009	5.457	-2.901	0.701	14.809	4.738	7.841	0.485
Actual	2010	5.381	0.000	2.391	12.478	2.841	4.984	0.488
Actual	2011	6.412	0.000	3.699	12.621	2.329	8.497	0.285
Actual	2012	3.583	0.000	1.697	14.371	1.468	7.400	0.894
Forecast	2013	4.568	0.000	2.130	14.120	0.743	7.554	0.137
Forecast	2014	6.790	0.000	4.037	14.195	0.929	8.280	0.137
Forecast	2015	7.699	0.000	4.906	13.725	0.945	12.155	0.137

	<u>t</u>	<u>Oil</u> <u>Barrels</u> <u>Millions</u>	<u>Gas</u> <u>MCF's</u> <u>Millions</u>	<u>Coal</u> <u>Tons</u> <u>Millions</u>	<u>Oil</u> <u>Price</u> <u>\$/Barrel</u>	<u>Gas</u> <u>Price</u> <u>\$/MCF</u>	<u>Coal</u> <u>Price</u> <u>\$/Ton</u>	<u>Excess</u> <u>Royalties</u> <u>To Trust</u>
Actual	2002	0.911	5.892	2.758	20.32	1.91	11.80	
Actual	2003	1.017	5.381	3.689	28.14	3.20	9.59	
Actual	2004	1.123	5.720	4.183	31.02	3.95	8.60	
Actual	2005	1.400	7.240	3.914	44.69	5.09	9.12	
Actual	2006	2.024	7.878	4.213	57.24	6.64	8.63	
Actual	2007	2.012	7.708	3.006	55.85	5.13	9.55	
Actual	2008	1.809	7.752	4.720	88.87	6.12	10.87	
Actual	2009	1.662	6.710	5.604	60.16	4.66	11.97	-5.542
Actual	2010	1.571	5.306	2.680	60.74	3.36	12.09	-1.398
Actual	2011	1.242	4.527	4.813	80.30	3.25	13.13	19.733
Actual	2012	1.292	3.989	4.175	84.38	2.57	13.94	20.134
Forecast	2013	1.337	1.881	4.093	80.12	2.76	14.52	18.554
Forecast	2014	1.372	1.697	4.312	78.48	3.82	15.10	19.541
Forecast	2015	1.403	1.523	6.100	74.23	4.33	15.67	22.962

Total Rev. = (Grazing + Agriculture + O&G Lease + O&G Bonus + O&G Penalty + Misc. + Int. Land + Int. Stip + Int. Trust + Timber + Res. Dev. + Commercial Lease) × .95 + Oil Roy. + Gas Roy + Coal Roy. + Other Roy. + School Technology + Trust Land Admin. - Excess Royalties To Trust

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Revenue Projection:

