TIMOs and REITs

Situation in Brief:

Since the mid 1980’s, many vertically integrated forest products companies (VIFPCs) in the US, for reasons discussed below, chose to either: 1) sell-off all, or a large part, of their forestland holdings, or 2) restructure themselves so as to legally separate ownership and control of their forestland and timber from ownership and control of their manufacturing facilities. Where sales occurred, much of the land is now held by “Timber Investment Management Organizations” (TIMOs). TIMOs buy, manage, and sell forestland and timber on behalf of various institutional investors – e.g., insurance companies, pension funds, endowments, and foundations. Where restructuring occurred, the land and timber is now held by “Real Estate Investment Trusts” (REITs). REITs are entities that buy, manage, and sell real estate or real estate related assets – e.g., mortgages – on behalf of various private investors. The magnitude of the ownership shift has been substantial. As shown in figure (1), as recently as 1985 the total investment in forestland and timber by TIMOs and REITs was less than $1 billion, but by 2005 it had grown to exceed $25 billion – with approximately $15.0 billion having been invested by TIMOs, and $10.2 billion by publicly traded REITs. As shown in figure (2), in acreage terms, while the VIFPCs held 58 million acres of forestland in the US in 1980, by 2005 their holdings had dropped to 21 million acres – a roughly 60% reduction. In contrast, over this same period of time the holdings of the TIMOs and

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1 Paper prepared by Cliff Hickman, Forester, R&D, Policy Analysis Staff.
2 Other buyers have included government agencies, privately held (i.e., family owned) forest products companies, and various conservation organizations like the Nature Conservancy and the Conservation Fund. Of the roughly 27 million acres of forestland that was sold-off in the US by the VIFPCs; an estimated 15 million acres was acquired by TIMOs, 2 million acres by privately held forest products companies, and the remaining 10 million acres by different conservation groups, other private owners, and government agencies.
3 Various distinctions between TIMOs and REITs will be brought to light during the course of this paper, but one difference worth noting at the outset is that TIMOs don’t actually own forestland whereas REITs do. In the case of TIMOs, the forestland is actually owned by the individual investors the TIMOs represent.
4 It is perhaps worth noting that despite the recent shifts in forestland ownership that have occurred within the US, in the overall scheme of things the TIMOs and REITs are still not all that significant. The most recent national statistics published by the Forest Service’s FIA program show that in 2002 the US had 504 million acres of “timberland” – i.e., land capable of growing over 20 ft.³/acre/year and not legally withdrawn from timber harvesting. Figures compiled from different sources used to prepare this report suggest that in 2006 the TIMOs and REITs jointly held about 27.3 million acres of timberland, which would represent about 5% of the total. This figure generally agrees with similar figures reported within the financial community that show timberland ownership in value as opposed to acreage terms. To illustrate, one website set the value of all timberland in the US at $450 billion, and indicated that “institutional investors” held 4%. Another website put the value of privately held timberlands in the US at $230 billion, and indicated that “institutional investors” owned 5%. The main point is that at present TIMOs and REITs hold only a fairly small fraction of all the timberland in the US.
REITs grew from nothing to over 25 million acres – with the proportion of land being held by each being roughly equivalent to their relative investment levels.\(^5\) (03, 10) The holdings of the TIMOs and REITs are spread across all commercial forest regions of the US, but the biggest concentrations occur as pine plantations in the Southeast, conifer plantations in the Pacific Northwest (west of the Cascades), and mixed softwood and hardwood stands in the Northeast. (01)

Figure (1):

![Trend in US Forestland Investments by TIMOs and REITs](image1)

Figure (2):

![Trend in US Forestland Ownership by TIMOs/REITs vs. VIFPCs](image2)

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\(^5\) In 2006 both Potlatch and Longview Fibre, with combined forestland holdings of just over 2.0 million acres, converted to the REIT structure.
For various reasons these ownership shifts have been of concern to many within the forestry, conservation, and environmental communities. Questions being asked include the following: (04, 14)

- How will the new owners manage their forestlands, and what will be the implications for the flow of goods and services that can be expected in the future?
- Will the new owners hold forestland and timber for a long time, or will they contribute to increased fragmentation and development across forested landscapes?
- What roles will the new owners play in the broad community of interests concerned with forestry issues – e.g., will they actively support forestry research and public policies conducive to the forestry sector?

Objectives of Paper:

The objectives of this paper are to look briefly at: 1) the primary reasons for the shift in forestland ownership patterns – including the impact of tax and other public policies; 2) how the management objectives, practices, and behaviors of the new owners compare to those of the prior owners; 3) the outlook for further ownership changes; and 4) the actions the Forest Service should take in response to this situation.

Reasons for Changing Ownership Pattern:

The reasons for the changes in private forestland ownership that have occurred in the US may be viewed from at least three different perspectives: 1) that of the former VIFPCs that elected to sell-off all or part of their forestland holdings,6 2) that of the TIMOs and the institutional investors they represent, and 3) that of the former VIFPCs that elected to restructure and create timber REITs.

Key motives and factors influencing the VIFPCs that elected to sell-off some or all of their forestlands included the following:7

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6 Before looking at the reasons why some VIFPCs elected to sell forestland, it may be worthwhile to briefly reflect on why they originally acquired such land. Unquestionably the key rationale was their desire to gain control over the conditions of availability – e.g., timing, delivered cost, species, volumes, and log sizes – of an input required by their manufacturing facilities. Other rationales included: 1) the investment returns realizable through timber management and appreciation in land values, and 2) the ability to enhance their corporate images by demonstrating that they were responsible land stewards. (05)

7 While the factors listed here are felt to have been the most important, other factors no doubt also played a role. One additional factor was the increased availability of relatively attractive forestland investment opportunities overseas where biological productivity rates were often higher and environmental restrictions less stringent. (01) Another factor was the apparent decline in the domestic demand for stumpage needed to produce some forest products such as paper and paperboard, where the use of recycled fiber has grown over time and is expected to exceed 40% in a few years. (01) Finally, yet another factor was the emergence of tax strategies – e.g., installment sales – that made it possible to better manage the capital gains tax implications of making timberland divestitures.
• **Relatively weak financial performance and the need to improve returns to stockholders.** – Stockholder returns over the 10-year period 1995 to 2005 averaged +6.2% for the “Forestry and Paper Group” as compared to +12.1% for the S&P 500, and +13.1% for the Dow Jones Industrial. (04) To ensure continued flow of investment capital into the industry, it was essential that stockholder returns be increased – and the sale of timber holdings was seen as a way to achieve this end.

• **Generally Accepted Accounting Principles (GAAP):** – Related to the preceding factor, GAAP for “Sub-Chapter C Corporations” precludes such entities, when it comes to computing their return on investment, from recognizing any appreciation in the value of the timberland assets they hold – only profit realized from the harvesting and processing of trees may be considered. This treatment contrasts with the conventions that apply to “Sub-Chapter S” and “Limited Liability” corporations, to TIMOs, and to REITs. (01, 12)

• **Rising Forestland Values:** - Related to both of the preceding factors, throughout much of the US forestland values have been rising in response to what has been characterized as “the grand tidal wave of sprawl now sweeping over the nation.” (09) As forestland values rose, so did the value of what was arguably the primary asset held by the VIFPCs. Although GAAP prevented these companies from recognizing this appreciation in value in their formal accounting, it didn’t stop them from “cashing in” through the sale of some of their lands – especially tracts with good access, proximity to urban areas, water frontage, scenic value, or outdoor recreation potential.

• **Consolidations made to enhance international competitiveness also increased debt burdens.** – Over the last 10 to 15 years, the VIFPCs in the US have faced increasing competitive pressure from low cost timber suppliers and forest products manufacturers in other parts of the world. In response, the domestic industry went through a period of substantial consolidation. Oftentimes significant debt was incurred to finance these consolidations. The sale of timber holdings was seen as a way to get this debt off corporate balance sheets. (01)

• **Rethinking of the long held belief that ownership of timberlands was essential to ensure future availability of an essential raw material at reasonable cost.** – Historically, as previously noted, a major rationale for the acquisition of timberlands by the VIFPCs was to gain some degree of control over the conditions of availability of an essential raw material. During the last 10 to 15 years, however, many firms came to believe they could confidently rely on open market sources of timber – both domestic and international.\(^8\) (01, 04)

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\(^8\) It is perhaps worth noting that where forestlands that were previously owned by a VIFPC are now under the control of a TIMO, it’s not uncommon for the TIMO to be operating under a “supply agreement” that obligates it to provide a certain amount of timber to the company that previously owned the land. Similarly, where a VIFPC has restructured to form a timber REIT – typically some of the firm’s manufacturing facilities have been retained and placed into a fully taxable REIT subsidiary that the timber REIT is obligated to supply.
• **Federal income tax policies.** – While no doubt unintentional, federal income tax policies also appear to have encouraged many US forest products companies to divest themselves of their timber holdings. Of greatest importance is the fact that the traditional VIFPCs are classified as “Sub-Chapter C Corporations” for income tax purposes. For this type of entity, any profits obtained from the sale of timber are taxed twice – once at the corporate level (35%), and once at the stockholder level when dividends are disbursed (15%). The practical effect of this tax policy is that investors who own both manufacturing plants and forestland often recoup as little as 50 cents out of every dollar of profit made from cutting trees whereas investors who own just forestland can normally pocket at least 85 cents out of every dollar.9 (01, 04, 07, 14)

Key motives and factors influencing the TIMOs and their institutional supporters to increase their forestland investments included the following:10

• **Passage of the Employee Retirement Income Security Act (ERISA) of 1974.** – This federal law, and similar pieces of state legislation, encouraged institutional investors – e.g., pension fund managers – to seek increased returns by diversifying their investment portfolios to include more than just fixed-income securities like government and corporate bonds. Collectively these statutes opened-the-door for institutional investment in timberlands. (01)

• **Increased recognition within the financial community of the advantages of timberland investments.** – Experience suggests that investments in timberland offer the following advantages for the patient investor – i.e., for the investor not interested in quick returns:

  o **Favorable returns** – Overtime, investments in timberland – considering both income generated and appreciation in value – have compared favorably to other investment options. To illustrate, over the period 1987 to 1999 when much of the shift in timberland ownership was occurring, total returns to timberland investments averaged +20.1% per year - +7.8% of this total was due to income generated, and +12.3% was due to appreciation in value. (01, 12)

  o **Lower risks** – While foresters tend to think of timberland investments as being fairly risky because of hazards like wildfire, insects, and disease – to financial managers, who view them as one part of a diversified investment portfolio, they

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9 Prior to the Tax Reform Act of 1986 the effect of the double tax on Sub-Chapter C Corporations was greatly moderated by the fact that such entities paid a significantly lower tax rate on “capital gains” income – which ordinarily included any income received from the harvesting of timber. The elimination of this rate differential in combination with the double tax applicable to their income has created a heavy burden for the Sub-Chapter C Corporations to bear. To date, efforts to get a rate differential for capital gains income restored have proven unsuccessful.

10 Ownership of timberland by institutional investors can take many forms. It is usually not direct fee simple ownership, but rather an interest or share in a fund, limited liability partnership, master limited partnership, limited liability corporation, or insurance company group annuity contract.
are generally seen as a way to reduce risk because experience suggests that returns to timberland investments tend to run counter to the returns provided by many other types of investments. (01, 12)

- **Inflation protection** – Experience indicates that timberland investment returns are highly correlated with the rate of inflation, which makes such investments a good hedge against inflation. (12)

Key motives and factors influencing those forest products firms that restructured to form timber REITs included the following:

- **Passage of the Real Estate Investment Trust Simplification Act (REITSA) of 1997**: - This legislation removed a provision of prior law known as the “Thirty Percent Gross Income Test” that had effectively precluded the VIFPCs from forming timber REITs. Basically this test would have required the VIFPCs that desired to be recognized as a REIT to forgo any timber harvesting for 4 years. Another favorable provision in the REITSA was that it allowed large institutional investors such as pension funds to hold shares in a REIT. This statutory change had the effect of increasing the liquidity of timberland investments for those REITs that are open to public trading.11 (11)

- **More favorable tax treatment and enhanced after-tax investment returns.** – This factor was discussed above when looking at the reasons why many VIFPCs have chosen to restructure themselves to separate ownership and control of their timber holdings from ownership and control of their mills. REITs are single tax entities – i.e., the REITs themselves pay no income tax, only the shareholders – and this tax is normally computed at a rate of not more than 15% as compared to the 35% rate applicable to any income realized by Sub-Chapter C Corporations.12 (13, 20, 21)

- **Desire to ensure timberlands were fairly valued in financial markets – i.e., to “monetize” timberlands.** – When a VIFPC restructures to form a timber REIT, two changes occur that help to ensure its timberlands will henceforth be fairly valued in financial markets. First, GAAP no longer precludes recognizing appreciation in value as part of return on investment. Secondly, as noted above, if public trading is allowed

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11 There are presently four publicly traded timber REITS: Plum Creek Timber Company, Inc.; Rayonier Inc.; Longview Fibre Company; and Potlatch Corporation.

12 REITs didn’t always enjoy single tax status; this benefit was authorized with passage of the Real Estate Investment Trust Act of 1960. The goal was to encourage creation of special purpose companies that would make it possible for average Americans to invest in real estate, an option that had previously only been open to wealthy individuals and corporations. To qualify as a “pass-through” tax entity, REITs must satisfy a number of requirements. Some of the more important of these are:

- They must be jointly owned by 100 or more persons/entities for at least 335 days each year.
- They must derive at least 75% of their gross income from real property sources – e.g., rents, mortgage interest, and proceeds from the sale of real property including timber.
- They must pay annual dividends of at least 90% of their income.
- They must have no more than 50% of their shares held by 5 or fewer people during the last half of each taxable year.
- They must have no more than 20% of their assets consist of stocks in taxable REIT subsidiaries. (20)
liquidity is enhanced because a wide array of investors can now participate directly in “pure” timberland investments. (11, 12)

Management Objectives of Different Ownership Groups:

While the specific organizational entities that make up the three ownership groups of interest in this paper – i.e., VIFPCs, TIMOs, and timber REITs – are all different and have somewhat unique management objectives and reasons for holding forestland and timber – different authorities have nonetheless offered some generalizations that seem relevant to this discussion. These include the following:

- **VIFPCs own both forestland and related manufacturing facilities, and as a result have certain strategic supply objectives that influence their decisions about when to cut timber and how long to hold on to forestland. TIMOs, and to a lesser degree timber REITs, have no such strategic objectives – when market conditions are favorable timber is generally cut and sold to the highest bidder in open-market auctions. When market conditions are unfavorable, timber need not be harvested but can be left to appreciate in value.** (01)

- **TIMOs and timber REITs apply modern portfolio theory to their decisions about when and where to buy, hold, and sell forestland. They are interested in diversifying their holdings among regions, timber types, and age classes. In contrast, the VIFPCs frequently make such decisions based on the locations of their existing manufacturing facilities and forestland holdings.** (01)

- **Capital availability oftentimes constrains the management options open to the VIFPCs but is typically not a limiting factor for the TIMOs because the funding sources that they can potentially tap into are extremely large.** Capital availability can be more of a problem for the timber REITs, especially if they are not publicly traded.

- **TIMOs invest funds on behalf of their clients (e.g., pension funds, endowments, and foundations) for a specified period of time – quite commonly 10 to 15 years. Unless the specific investment vehicle provides an option to extend, the assets will be sold at the end of this time period. Additionally TIMOs, especially when they are engaged in investing pension funds, have an implicit fiduciary responsibility to manage the investment so as to yield the best possible return – i.e., to maximize profits.** (01)

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13 The reality is almost certainly more complex than this observation suggests. It’s not uncommon for TIMOs to have “supply agreements” with manufacturing facilities located in the vicinity of their timberland holdings, and these agreements can limit their flexibility to postpone harvest. Similarly, where VIFPCs have restructured to form timber REITs, in most cases at least some of the parent company’s manufacturing facilities were retained and placed in a “taxable” REIT subsidiary – and the need to keep these subsidiaries supplied can constrain their flexibility to delay harvest. Additionally, timber REITs are obligated to annually pay an agreed upon distribution per share which may be either a dollar amount or a percentage – and this requirement may also create pressure to harvest annually. (01)

14 To illustrate, even as long ago as March of 2000 – US pension fund assets were estimated to be on the order of $10 trillion. (01)
Taxes are a major decision-making factor for the VIFPCs. TIMOs and timber REITs are less concerned about taxes because they are only taxed once, they are taxed at a lower rate, or they are tax exempt. (01)

Management Practices and Behaviors of Different Ownership Groups:

As noted earlier, as TIMOs and REITs have gained control over more forestland in the US – many within the forestry, conservation, and environmental communities have grown concerned about the implications of the ownership shifts. These groups wonder what the changes will mean in terms of such things as: how forestlands will be managed, the flow of goods and services that forestlands will provide, the pace of forestland fragmentation and development, and levels of support for forestry research as well as other important forestry-related activities. After years of working with the VIFPCs these groups had learned what to expect from this class of forest owners – but the shift in historic ownership patterns has created much less predictability as concerns the future of US forests.

Because the changes in forestland ownership are for the most part relatively recent, very little empirical evidence exists that can be used to answer the questions being posed by the forestry community. Even in the few cases where relevant studies have been conducted, the results must be interpreted with caution. Some studies have elicited information on planned management activities, but plans aren’t always carried-out. Other studies have looked at the management practices actually being applied, but either the interval of years represented has been very narrow or the geographic coverage has been spotty. For the most part analysts have been forced to draw inferences based on the presumed management objectives of the various ownership classes. Recognizing these realities, the following impressions are offered:

- **Type of forest management practiced.** – At present there is little evidence to suggest that the management practices employed by a TIMO or REIT on a given piece of land should be expected to differ markedly from those that would have been applied by a VIFPC. The new owners, like the old, generally have an incentive to leave their land in as good or better shape than it was when they acquired it – and as noted earlier, they typically don’t suffer from the same limitations on capital availability as often plagued the VIFPCs. There is some evidence to indicate that TIMOs show a preference for silvicultural treatments that will produce a benefit in 10 to 15 years, and that they tend to concentrate their investments early in a given investment period; but when longer-term investments are needed to maintain or enhance property values – e.g., investments in site preparation and planting – it appears these investments will be made as long as they can be economically justified. As previously noted, some authorities have argued that because they don’t have mills to support, TIMOs and REITs are under less pressure to cut – especially when markets are weak; however, as has been pointed out elsewhere, the validity of this argument is questionable – especially as it applies to the timber REITs. In a somewhat different vein, it should be noted that the TIMOs and REITs are subject to the same forest practice regulations
and mandatory environmental restrictions as apply to other forest owners. Whether or not the new owners will be as willing to comply with voluntary BMPs as were the VIFPCs is unclear, however, especially when the BMPs will result in cost increases that are not inconsequential. The VIFPCs were often willing to accept such cost increases in order to enhance their corporate image and maintain their “social license” to practice forestry. Finally, yet another point worth noting is that some TIMOs and REITs have elected to participate in independent programs designed to “certify” the sustainability of their forestry practices. On this score, however, it should be pointed out that in most of these cases the lands were previously enrolled in a certification program and thus the decision was to continue, not initiate, certification.

- **Type of goods and services (including environmental amenities) produced.** – It seems clear that at present the forest product of greatest interest to TIMOs and REITs, as it was for the VIFPCs, is timber – and that other non-market goods and services that can be provided without significantly compromising the flow of timber products will continue to be “jointly produced” in the future as they were in the past – e.g., wildlife habitat and watershed protection. Where the different types of owners may take different stances is when it comes to producing those forest-related goods and services that potentially have a market value – e.g., different types of recreational pursuits such as hunting. While the VIFPCs sometimes sold hunting leases when this was an accepted practice in a given area, oftentimes they provided free public access to their lands for this pursuit as well as others – but it is presently unclear whether TIMOs and REITs will continue to honor this tradition. Additionally, it’s interesting to speculate about what would happen if a national cap were to be imposed on carbon emissions and an active market for carbon sequestration credits were to emerge. Given less of an obligation to supply dependent mills, TIMOs and REITs would be comparatively free to adjust their management strategies to take full advantage of the relative values of timber versus a unit of carbon sequestered.

- **Ownership tenure and fragmentation:** – This has been raised as an issue mainly as concerns ownership by TIMOs, which as previously noted – typically operate within a 10 to 15 year timeframe. This situation contrasts sharply with the VIFPCs, many of whom – at least until recently – held forestland for periods of 50 years or more. The main concern is that more frequent ownership turnovers will lead to increased fragmentation. The limited evidence that is available to date suggests these fears may have merit. In instances where TIMOs have sold timberlands, it appears they have frequently disposed of their holdings in smaller sizes than when they were acquired – and some observers suggest this is being deliberately done in order to capture the higher prices obtainable in the “retail” as opposed to “wholesale” land markets.

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15 An example would be the Anderson-Tully Company, a timber REIT whose hardwood management activities are certified by the Forest Stewardship Council (FSC).

16 Illustrative is the fact that on February 23, 2007 Potlatch Corporation – a publicly traded timber REIT – announced that starting April 1, 2007 it would be requiring users to purchase a permit to recreate on its forestlands in Idaho. Additional information can be obtained by going to [www.potlatchcorp.com](http://www.potlatchcorp.com).
While TIMOs occasionally sell to other TIMOs, sometimes sales are made to smaller regional buyers such as sawmills. This has led to a secondary concern that many of these purchases are being financed with borrowed capital – and that the purchasers may subsequently be required to cut their lands heavily to payoff the debt they’ve incurred. Overall it appears that although TIMOs may be long-term holders of forestland in the aggregate, they can be expected to periodically turnover specific areas – and this will likely contribute to increased fragmentation. (12, 18)

- **Willingness to convert forestland to other uses.** – There is some evidence to suggest that TIMOs and REITs, because they don’t have the same level of responsibility to supply dependent mills as did the VIFPCs, are more willing to convert forestlands to other uses. Indeed, it’s not uncommon for TIMOs and REITs to have a staff, or subsidiary, that is specifically tasked with handling the sale of lands that have been determined to have some “higher and better use” than continued timber production. That said, there is also some evidence which suggests that TIMOs and REITs, in selecting what forestlands to invest in, make a conscious effort to avoid lands that have development potential or are environmentally sensitive because purchasing such lands is inconsistent with their basic goal of realizing the returns obtainable from timberland investments.17 Additionally, some observers have noted that TIMOs, and to some degree REITs, seem relatively willing to enter into conservation easements with environmental organizations, land trusts, and/or governmental agencies.18 The easements that have been negotiated typically ensure that sensitive forestlands will be remain in their current use but also permit continued timber harvesting under stipulated conditions. (06, 07, 09, 18) For the TIMOs and REITs, the rationale for entering into such easements is multifaceted; they can be a way to: 1) reduce up-front land acquisition costs and maximize overall investment returns,19 and 2) side-step the potential controversy associated with trying to practice forestry on lands deemed “sensitive.”20 While the acreage of land protected by conservation easements has been increasing over time, a persistent problem for the conservation and environmental communities has been finding adequate funding to consummate desired easements.21

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17 Lands with recognizable development potential would be more expensive to acquire, and sensitive lands would be more costly to manage; in either case the returns realizable from practicing forestry would be compromised.

18 Conservation easements may be donated or sold, but when a TIMO or REIT is involved typically an easement will be sold. This situation is consistent with their emphasis on maximizing investment returns and the fact that taxes are generally less important to these owners.

19 A case can be made that the existence of an easement will influence a property’s eventual resale value. For some landowners this possibility may not be important, but for a TIMO or REIT it likely will be – and thus it seems reasonable to assume this possibility will be taken into account when negotiating a sales price.

20 There can also be important income, estate, and property tax benefits associated with entering into conservation easements – but typically these advantages are not as important to TIMOs and REITs as they are to other types of private landowners.

21 Within the US, the area of land protected by conservation easements grew from 1.4 to over 5.0 million acres between 1998 and 2003. (06) This figure includes all types of undeveloped rural land, not just forestland.
• **Support for forestry research.** – There is some evidence to suggest that TIMOs and REITs are less supportive of forestry research than were the VIFPCs – many of which had their own forestry research organizations. One indicator is that as timberland ownership by the VIFPCs has declined, so has participation in various university-affiliated forestry research cooperatives. In the case of the TIMOs, this phenomenon has been attributed to the fact that they operate under relatively short investment horizons (10 to 15 years) whereas the payoffs from most forestry research activities are realized over long periods of time; however, this logic only holds-up if you assume the TIMOs don’t expect to be in existence beyond the duration of their initial investment offerings – and this doesn’t seem rational. In the case of the REITs, the phenomenon has been attributed to the fact that they are required to annually distribute 90% of their income to their shareholders – and that consequently their capacity to support forestry research is diminished. Some observers have suggested that the problem may not be that TIMOs and REITs are unwilling to support forestry research, but that they simply haven’t been in existence long enough to find a suitable mechanism for allocating these costs to their investors. (01, 04)

• **Support for forestry in general.** – There is some evidence to suggest that TIMOs and REITs will be somewhat less active within the broad forestry community than were the VIFPCs – i.e., that they will not participate as extensively in different forestry organizations at the national and state levels, and not be as aggressive in supporting federal and state legislative initiatives of concern to the forestry sector. Indicative is the fact that membership in the American Forest & Paper Association (AF&PA) as well as many state forestry associations has been declining. In a somewhat different vein, in the South there is some evidence to suggest that the TIMOs are not as supportive of cooperative fire fighting efforts as were the VIFPCs. During the last 15 years private fire fighting capability in the South has been declining, at least in part because the TIMOs seem more willing to defer the responsibility for providing fire protection to the states. Again, it may be somewhat premature to form any final conclusions – perhaps the new owners simply need more time to assess the benefits of participating in such cooperative ventures. (01, 04)

**Conclusions and Possible Responses:**

Only one conclusion will be offered based on the results of this analysis, and this is that the movement of forestland ownership within the US from the VIFPCs to TIMOs and REITs is likely to continue in the future – although the pace of change may very well slow.\(^\text{22}\) The main reason why this shift in ownership classes is likely to continue is that

\(^{22}\) A case can be made that to the extent there is further growth in the amount of US timberland held by TIMOs and REITs, this growth will occur mainly within the REIT sector. There are still a few VIFPCs that hold significant amounts of timberland – e.g., Weyerhaeuser, Mead-Westvaco, and Temple-Inland. For these firms restructuring as a timber REIT would produce significant tax benefits while not requiring a complete severing of any connection to their manufacturing facilities since the latter could, within limits, be placed in a taxable REIT subsidiary. It may also be worth noting that timber REITs enjoy certain advantages over many other types of REITs, a key one being that most of their income will qualify to be recognized as a capital gain. Once timber REITs are better known within the financial community, these advantages could lead to an increase in the amount of investment capital available to such entities.
the pressure to move ownership of forestlands to a more tax-efficient structure is very strong – i.e., those VIFPCs that do not embrace more tax efficient structures will find themselves in a constant struggle to remain competitive.\textsuperscript{23} Reasons why the trend may slow include the following: a lot of industry land has already moved into other ownership classes, suitable timberland investment opportunities are becoming more difficult to find, and rates of return on US timberland investments have moderated somewhat – perhaps due to increased international competition and the fact that domestic markets have now adjusted to the decline in national forest timber sales in the Pacific Northwest.\textsuperscript{24}

The lack of hard data showing, beyond a reasonable doubt, that serious economic, environmental, or social problems are occurring as a result of the shift of substantial acreages of forestland from ownership by the VIFPCs to ownership by TIMOs and REITs suggests that the Forest Service should be cautious and prudent as regards the actions it takes, or advocates that others take, in response to this matter. At the same time, the evidence now at hand very definitely suggests that a number of potentially undesirable trends may be emerging – and that existing federal tax policy may well have contributed to the situation. Under these circumstances the Agency would be remiss to do nothing, and so the following possible responses are suggested:

- That the Agency commit to monitoring and periodically making available, perhaps through the FIA program, data on: 1) changes in forestland ownership, including ownership by TIMOs and REITs; 2) shifts in land use by ownership class; 3) the types of management practices being applied by different types of forest owners; and 4) changing resource conditions on the forestlands held by different types of forest owners.

- That the Agency, to the extent allowed by other priorities, commit to conducting or supporting additional research that will provide better information about the true economic, environmental, and social consequences of the shifts in forestland ownership that have occurred in the US.

- That the Agency, consistent with the spirit of its “Cooperating Across Boundaries” initiative, expand its outreach efforts to the TIMOs, REITs, land-trusts, and other key partners in order to find collaborative solutions that will help keep America’s forests and grasslands “healthy across the landscape” – perhaps through the more effective use of working forest conservation easements. (08)

\textsuperscript{23} Relevant to this point, at the time this paper was being written, the press and various industry newsletters were reporting that: 1) Weyerhaeuser had recently appointed a REIT expert to its corporate board, and 2) Temple-Inland had announced plans to sell-off its forestland holdings. If these companies divest themselves of their timberland holdings, while there will still be some family-owned forest products corporations that own significant acreages of forestland – Mead-Westvaco would become the last VIFPC to still own forestland.

\textsuperscript{24} It is perhaps worth noting that two institutional investors – i.e., the California Public Employees Retirement System (CalPers) and Harvard University – have recently terminated their North American timberland investments, purportedly because of declining returns.
• That Agency leaders, on appropriate occasions, use their “bully pulpit” to describe
how federal income tax policy appears to have influenced the ownership of private
forestlands in the US – and to discuss the apparent conservation implications of these
changes. 25

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25 Considerable care should be exercised in acting on this suggestion. The Agency must avoid putting itself
in the position where it could be perceived as advocating a “tax break” for wealthy corporations –
especially given current levels of public concern over the national debt and growing annual budget deficits.
Agency leaders should strive to be factual and stress that their dominant concern is to encourage adoption
of tax policies that are conducive to responsible forest management and conservation.


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