W E T L A N D S / S P E C I E S

Mitigation

The Ecosystem Marketplace's Daily Coverage of the 2007 Mitigation/Conservation Banking Conference

Thursday, April 12, 2007 **Volume 2, Issue No. 2**

Wildlands: A Capital Infusion

By Alice Kenny

Wildlands, Inc. recently announced that Parthenon Capital, a private equity firm with over $1.5 billion under management, has invested in the company. The Ecosystem Marketplace finds out how Wildlands, Inc. plans to put the new capital work

A rugged outdoorsman with an inventor's creativity, Wildlands, Inc. president Steve Morgan is a can-do kind of guy whose foray into mitigation banking was born of pragmatism. An avid duck-hunter, Morgan built a private 500-acre marsh to encourage duck migration in 1994. But as he sat on his porch admiring his accomplishment, state highway department officials waded through his land. Their mission, he learned, was to survey the marsh and then seize it to build a highway bypass. Instead of suing them, Morgan found a way to turn the situation to his advantage.

Under the Clean Water Act of 1972, private and public developers must compensate for any wetlands they destroy. When Morgan discovered that the U.S. Army Corps of Engineers approves wetland mitigation banks as a means for developers to meet this requirement, he crossed the street and bought 315 acres of land. He restored the wetlands on the parcel and then sold it to the state as mitigation for the highway they were building through his original property. Morgan thus founded the first wetlands mitigation bank in California and launched what was to become the business he now owns and runs: Wildlands, Inc.

Contra Costa goldfields, an endangered plant species, blooms at Wildlands' North Suisun Mitigation Bank

(photo courtesy of Wildlands)

Just over two decades later, Wildlands now runs 40 wetland mitigation and conservation banks in California and Washington State. The company has restored over 25,000 acres of habitat and has plans to expand dramatically. To fuel this growth, Wildlands recently announced that Parthenon Capital, a private equity firm with over $1.5 billion under management, has invested in the company.

The aggressive capital infusion could change the face of wetlands banking, enabling Wildlands to

New Money in the Air

In 1974, Congress passed the Employee Retirement Income Security Act (ERISA) encouraging institutional investors to diversify their portfolios. At the time, timber companies were carrying timberlands at book values well below their market values. Recognizing the chance to buy into a new asset class, Timber Investment Management Organizations (TIMOs) were born to manage partnerships among institutional investors interested in buying up timberlands. By 1989, TIMOs owned approximately $1 billion worth of timberlands throughout the world; by the end of 2006, the number had climbed to roughly $24 billion, with a concentration of holdings in the Southeastern United States.

What does any of this have to do with mitigation banking? At the very least, timberlands may provide some insight into how the injection of new capital can quickly transform a real-estate based industry into an asset class recognized by Wall Street investors – a topic germane to mitigation bankers as their companies mature and seek new ways to finance expansion in the coming years. Recent trends in the area of timberland investment might also send some institutional investors hunting for opportunities in the mitigation banking sector. Speakers at a World Forestry Center Conference in 2006 flagged two trends for TIMOs. First, they noted that timber deals in the United States were becoming increasingly innovative about their use of tax credits. And second, they predicted that the availability of timberlands in the United States was likely to dry up over the 2007-2010 period, pushing timberland investors into higher risk areas overseas.

As timberland investors in the United States look for new places to put their money (almost all global timber plantations yielded IRR returns of less than 7% in 2003), it is reasonable to think that some of them might stumble across the growing mitigation banking industry right on their doorstep. The Ecosystem Marketplace plans to watch this potential development closely. What is already clear is that private equity has taken an interest in wetland mitigation and conservation banking. On December 26, 2006, Parthenon Capital, a private equity firm with over $1.5 billion in management, inked a deal with Wildlands, Inc. that will inject millions of dollars into the mitigation banking company's expansion beyond California and the Pacific Northwest. We spotlight the deal in this issue as a potential harbinger of things to come in the next decade of this industry's development.

And, rumor has it, many other similar deals are in the works. Is mitigation banking ready for speculative investment? We'll leave that discussion to you in the days ahead.

The Ecosystem Marketplace Team

A Capital Infusion

(continued from page 1)

take this typically regional industry to a national level. Many say the partnership, coupled with Wildlands' steps to open a dozen new mitigation and conservation banks, offers a peak at the future of environmental banking. "This," says Morgan," is a major jump in a very young industry."

By the Numbers

Acquiring land at a rate of 4-5,000 acres each year, Wildlands has added seven new mitigation banks to its portfolio in the past four months and has five more banks pending approval. According to Morgan, the banks offer sanctuary to a variety of threatened animals, including Chinook salmon and California tiger salamander. "Our success barometer is not the money we make but the sum of the acres we preserve," says Morgan. "It takes a business model to do that."

Wildlands typically pays between $12,000 and $20,000 per acre for properties it plans to restore. Once the habitat has been restored, wetlands mitigation credits sell for between $30,000 and $300,000; endangered species credits run between $3,000 and $50,000. Thanks to California's rapid-fire development, mitigation bank credits have, to date, been swooped up quickly despite their hefty price tags. Unlike many mitigation banks, Wildlands holds on to its land in perpetuity.

"Steve has done an unbelievable job bootstrapping the company," says Parthenon vice president Andrew Dodson. "To take the company to the next level, it needs a financial investor to help it grow and increase the magnitude of acres conserved."

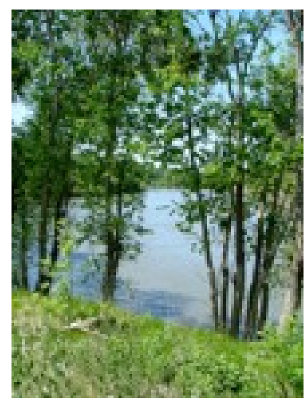
Sealing the Deal

Once a diehard bachelor, Morgan, 57, marvels at how much his life has changed. Now married, he says he spends most of his free time with his wife and seven-year-old identical twin girls. His daughters sat on their first horses when they were one year old, he brags, caught their first fish at age 2, went hunting with their dad by age four and "continue to roam the land with me." Coincidentally, a cold call from a fellow father of identical twin girls transformed his business model as well.

Parthenon's Dodson – the father of four-month-old twins – says that his company has tracked Wildlands' growth for the past three years. Parthenon typically invests in financial services, health care and high-tech manufacturing companies to make money for pension-fund investors. Their investment in Wildlands – signed December 26, 2006 – marks Parthenon's first play in environmental markets. It also marks the first purely profit-driven private equity investment in mitigation banking in the United States.

But from an investment perspective, Dodson says the jump into environmental markets is a fairly conservative step for his firm. Parthenon's six-month due-diligence investigation revealed that Wildlands scored investment returns spanning between 20 and 30 percent. And last year, Wildlands achieved returns of 35 percent.

Of course, Dodson says, "every deal is a risk. What we get paid for is finding the highest return with the lowest risk. We feel the wetlands market is here to stay because it answers a fundamental environmental need."



With the European Union already embracing carbon markets to reduce carbon emissions, the United States is bound to rely increasingly on environmental markets to solve environmental problems, says Dodson. Already, mitigation banks have grown in popularity in the United States by offering economically sound solutions to environmental challenges. They provide hundred-to-thousand-acre thriving wetland landscapes that replace otherwise ad hoc, often half-acre sights that are prone to failure. And they have bipartisan banking, with the former Democratic Clinton administration as well as the Republican administrations of George Bush Jr. and Sr. embracing them.

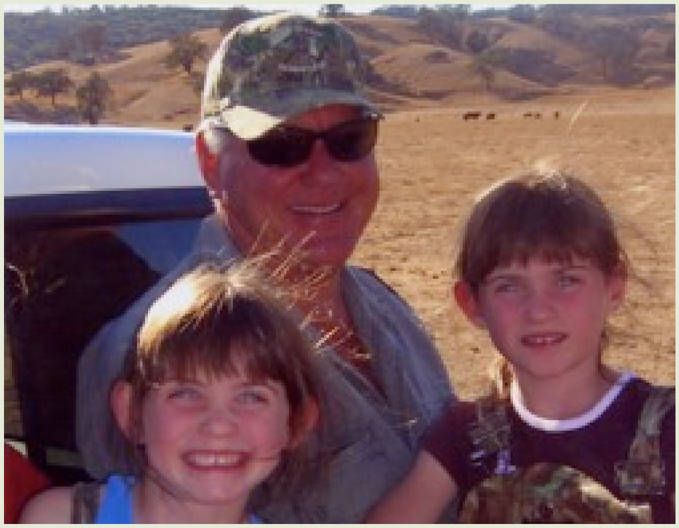
Don Ewoldt, the newly elected president of the National Mitigation Banking Association explained its bipartisan appeal. "The Republicans are pro business and the Democrats are pro environment," he says. "We're a business enterprise that is definitely positive for the environment."

The Next Phase of Growth

Successful banks can charge top dollar because the industry has, so far, been unable to keep up with market demand. Mitigation banking is capital intensive, meaning it requires upfront funding to create wetlands before it can begin to recoup investments. So Wildlands, similar to other mitigation banking companies, uses banks as seed money, rolling profits back into land acquisition.

Now Wildlands can instead invest Parthenon dollars. Although Dodson and Morgan declined to disclose Parthenon's exact investment, records reveal that Parthenon normally invests between $20 and $100 million per company. Dodson says that Parthenon typically expects to turn a profit within five to seven years after investment, a time frame that works well with mitigation banking whose wetlands are restored and ready for sale as wetlands within a few years of purchase.

Dodson sees his company's investment as making Wildlands "uniquely positioned to excel on a national level, leading the industry into the next phase of growth." As a first step, Morgan says Wildlands plans to expand to the east coast, opening offices in Charlotte, North Carolina and moving north and south from there.



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Bypass to the Future

Despite its rapid growth, mitigation banking still faces major hurdles. The regulatory environment is continually changing, and mitigation bankers compete for land with developers who are flush with cash.

As a result, private equity investment in mitigation banking will likely play a significant role in this environmental industry's future, Ewoldt says. Although Parthenon and Wildlands were the first to announce their partnership in the mitigation banking business, Ewoldt revealed that several mitigation bankers and private equity firms are in the midst of negotiations, although he declined to name them until the deals are signed.

Meanwhile, 23 years after surveyors waded through Morgan's duck club, the California highway department bureaucracy still has not built a bypass. But the mitigation banking business the department inspired is thriving.

Alice Kenny is a regular contributor to the Ecosystem Marketplace. She may be reached at alkenny@aim.com.

NMBA Meets, Appoints Board

"To the members we haven't seen in a year, welcome back," said Craig Denisoff in opening the last meeting of his three-year tenure as the President of the National Mitigation Banking Association (NMBA). "I am a little giddy this year because I know I get to turn over the reins."

While he may be happy to have served his time, others are sorry to see Denisoff go. During his term as NMBA President, the organization has doubled its membership from 25 to over 50 and has increased its annual revenues substantially. Some of this money has been put to work convincing legislators on both sides of the aisle that mitigation banks deserve the support of federal agencies in developing an innovative approach to conservation on private lands. The effort, according to Peggy Strand of Venable LLP, has begun to pay off. "We used to go to Congressional offices and they had no idea what wetland mitigation banking was," Strand said. "There's not an office we go to now where they don't know what natural resource trading is…they are looking to you in your knowledge and experience in this industry to lead a new era of natural resource policy in this country."

In particular, Strand celebrated a new Water Resources Development Act (WRDA) in process in the House that says federally funded water resource projects, "must first consider mitigation banks." She noted, however, that the Senate has not yet incorporated similar language and that bankers must continue to fight for the final release of the Department of Defense rules regulating wetland mitigation before the end of 2007. Strand also spoke of a recent lawsuit brought by the NMBA against the city of Chicago and its use of in-lieu fees to provide wetland mitigation for the expansion of its airport. The association, she said, lost that suit, but did manage to get favorable language in the court's wording. This loss, she said, just highlights why the industry needs to push harder for the final Dept. of Defense regulations on mitigation banking."We need regulations that we can enforce," concluded Strand. Denisoff echoed this thought in his self-dubbed "Outrageous Outgoing Remarks" and encouraged the Association to look both outward at the general public and inward at self-certification in the years ahead.

Rich Mogensen, outgoing Past President, then moved the meeting onto a lighter plane with his top ten reasons to come to the National Mitigation & Conservation Banking Conference. Our favorites after two years of covering the conference: "You can have fun bashing in-lieu fees" and "You can be confused by all the Georges." After coaxing laughter from the crowd, Mogensen introduced the incoming board and then yielded the stage to the incoming President, Don Ewoldt.

Stepping up to the podium, Ewoldt introduced himself as a farm-boy from Iowa and had a simple, strong message to his fellow bankers: "Our future," he said, "is in our hands."

2007 Board Officers:

- Don Ewoldt, President
- Sheri Ford-Lewin, Vice President
- George Kelly, Treasurer
- Dave Urban, Secretary
- Craig Denisoff, Past President

2007 Board Members:

- George Howard
- Rich Mogensen
- Stephen Collins
- Cynthia Robinson
- Open Slot

Guest Editorial: Ten Years for a Banking Company and an Industry

by George Kelly

George Kelly, a Partner and Founder of Environmental Banc and Exchange (EBX), reflects on the fact that his company and the National Mitigation and Conservation Banking Conference share the same anniversary.

In 1997, Environmental Banc & Exchange (EBX) was formed, the same year that the first National Mitigation Banking Conference was held. The Conference was in Washington, DC, where there were over 100 attendees with a heavy focus on wetlands. EBX was a fledgling, fresh-faced company that was formed to, among other things, embrace market-based approaches promised by the recently issued Federal Guidance on Wetland Mitigation in 1995. The Environmental Law Institute (ELI) reported that, at that time, there were over 50 mitigation banks active in 18 states in the United States.

Ten years later, the Conference thrives with up to 350 people in attendance, and EBX is flourishing as a national mitigation company focusing on the Southeast. ELI reports that the number of mitigation banks is now approaching 500 in over 34 states. And the Conference now includes focused discussion on stream mitigation and conservation banking as well as wetlands.

Although it is hard to believe that so much time has passed, ten years is a good benchmark for recollection on the lessons learned. As a so-called veteran, I thought it would be helpful to impart some of my insights:

Recognize the Important Role of the Conference and Associations

The Conferences have served as a place where participants can share the good and bad technical, regulatory and business issues. Resource agencies are afforded the opportunity to intermingle with bankers in an informal context and share best practices from around the country. Bankers, in turn, get to impart economic insights associated with banking.

Through this robust interchange, bankers began to understand the value of addressing shared issues in a cooperative fashion. Associations were formed, including the Florida Bankers Association in 1997, the National Mitigation Banking Association in 1998 and other regional associations, such as the North Carolina Environmental Restoration Association in 2002. The results have been staggering, witness the advent of a newly crafted federal mitigation policy that was informed, in large part, by the Associations. State associations, such as the North Carolina Environmental Restoration Association, have been instrumental in the formation and operation of the North Carolina Environmental Enhancement Program. The role of these Conferences and Associations cannot be overstated.

Criteria that Support the Market

Market-based approaches to environmental restoration require that there be a demand driver for mitigation products. Without clear rules and strict enforcement of the rules protecting resources, there is no market. This industry supports high standards for both environmental enforcement and restoration and is reliant on such standards to survive. We are particularly pleased that we now have web-based platforms, such as the Ecosystem Marketplace, to facilitate and support this industry.

The "Forces of Evil" Still Exist

Notwithstanding the existence of markets, the mitigation banking community is constantly fighting to eradicate mitigation standards that favor off-site mitigation and in-lieu-fee programs. These differential standards undermine the willingness of private enterprise to invest in mitigation banks, knowing that their projects could be undercut by alternative mitigation options that are not held to the same high standards. Doing away with differential standards is the essence of the recently enacted law in 2003 mandating that the Corps promulgate regulations creating equivalent standards for mitigation. Nevertheless, the mitigation rules have not yet been finalized and forces continue to promote different, more favorable treatment, for off-site and in-lieu mitigation. We need not go far to see the results of differential treatment. For example, in the O'Hare Airport expansion, $26 million was paid into an in-lieu fee program for mitigation with impunity, despite being contrary to federal guidance and the existence of approved mitigation banks that could service the mitigation.

There also have been a number of hiccups, such as Supreme Court decision in SWANCC, whereby the Corps ceded jurisdiction over certain isolated wetlands. Now, once again, the industry is faced with the uncertainty posed by the recent decisions in Rapanos and Carabell. These decisions have a direct impact on the marketplace.

"We also dream that it would take less time to get approval to restore a wetland than to destroy one."

Markets are Evolving

When the first conference was held, the focus was on wetland mitigation. Since then, markets have been evolving to include stream mitigation, habitat/conservation banking, water quality trading and carbon sequestration. The Department of the Interior issued "Conservation Banking Guidance" in 2003, the EPA issued guidance on Water Quality Trading in 2004 and the Corps/EPA issued a regulatory guidance letter in 2002 that promoted stream mitigation. States, such as North Carolina, have taken the lead in serving as a laboratory for stream mitigation rules and polices. EBX has been at the forefront of producing such stream mitigation. Some of these markets however still need additional flesh on the bones, while others are evolving at a rapid pace.

"Coming full circle, those of us at EBX dream of a time when eco-assets are freely bought and sold in a marketplace that values them even without a regulatory driver."

Capital is Here

Climate change, green technology and alternative energy have shown the spotlight on green industries and investments. The green investment sector is hot and mitigation banking is a prime candidate for such investment. Indeed, as of this writing, there are at least five capital providers registered to attend the conference in St. Louis and the keynote speaker will be from Al Gore's Investment Fund, Generation Investment Management.

Dreams

Coming full circle, those of us at EBX dream of a time when eco-assets are freely bought and sold in a marketplace that values them even without a regulatory driver. We dream of a robust industry with multiple restoration product lines. We also dream that it would take less time to get approval to restore a wetland than to destroy one. For now…we will keep dreaming and look forward to seeing you at mitigation conferences for many years to come!

Stay informed, sign up for "Mitigation Mail", a monthly e-mail newsletter on conservation/mitigation banking: www.ecosystemmarketplace.com

Darrell Westmoreland and Chip Johnson of North State Environmental man their booth

Ryan Bourriaque of Louisiana State University and Kate Carpenter of the Louisiana Department of Natural Resources do bit of networking

Sheri Ford Lewin of Mitigation Marketing and Cynthia Robinson of Robinsong raise a toast to the industry (or is it to being away from teenagers?)

John Hutton of Acer Environmental and Tara Allden of Restoration Systems. One wonders which one of them gets the third drink?

Judith Taggart of JT&A, our fearless conference organizer, has a word with Charles Bruton of Mulkey Engineers and Consultants

Craig Bailey of Westervelt finds out from Louisa Mamouney, of the New South Wales Dept. of Environment & Conservation in Australia how "Bio-banking" is taking root "down-under"

Craig "not my job any-more" Denisoff receives his parting gift as out-going NMBA President and claims to be "speechless", some-thing, he adds, that "doesn't happen very often".

Ken Sanchez of US Fish and Wildlife, Wayne White of W-Squared consulting, and Dixon Harvey of Environmental Banc and Exchange

John Ryan of Land and Water Re-sources and Don Ewoldt, NMBA's new President, prepare to present outgoing Presi-dent, Craig Deni-soff, with his part-ing gift

George Kelly (L) of EBX bends a regulator's ear (in this case, Mark Sudol of the US Army Corps of Engineers)

Agenda for Today (Thursday, April 12, 2007)

8:00 AM - 9:30 AM
Plenary *(Grand Ballroom)*
Welcome. Judith F. Taggart, & Col. Lewis Setliff III

Keynote Addresses:

Where We've Been & Where We're Headed: George Platt, The Wetlandsbank Group

An Environmental Review & Perspective on the Future: Lawrence A. Selzer, The Conservation Fund

Green Investing - What are the Opportunities for Banking: Jason Scott, Generation Investment Management

9:30 AM - 10:00 AM: BREAK

10:00 AM - 11:30 AM
SESSION 1: The Business of Banking, Primer 102 *(Miss. Ballroom)*
Moderator:George Platt, The Wetlandsbank Group

Sales policies, procedures, & identifying key targets for the established banker: Sheri Ford Lewin, Mitigation Marketing LLC
The Use of Conservation Easement Tax Write-offs: Jeff Kauttu,Kauttu Valuations
Investing in Mitigation and Conservaiton Banking: Dixon Harvey, EBX

SESSION 2: Outside the Box Banking - New Approaches *(Meramec Ballroom)*
Moderator: Peter Beesley, PG&E

Ecosystem Enhancement Program Update: William D. Gilmore, North Carolina EEP
Emerging Tools for Conservation Banking at a Landscape Scale: Doug Bruggeman, Michigan State U.
Australia's Biobanking Program: Louisa P. Mamouney, New South Wales Dept. of Environment & Conservation

11:30 AM– 1:45 PM
LUNCHEON -- PLENARY

Where We Are Today *(Grand Ballroom)*
Moderator: Don Ewoldt, Incoming President, NMBA

Regulatory Outlook: Chip Smith, Office of Asst. Secretary of the Army
Mitigation Banking in the Courts: Peggy Strand, Venable LLC
Environmental Outlook: Patricia White, Defenders of Wildlife

2:00 PM - 3:30 PM
SESSION 3: Conservation Banking *(Miss. Ballroom)*
Moderator: Ken Sanchez, US Fish and Wildlife Service

Build it and They will Come: Matthew Gause, Wildlands Inc.
Hickory Pass Ranch Conservation Bank: Kevin Ramberg, ACI Consulting
HD Ryals Florida Scrub Jay Conservation Bank: Quest Ecology, Inc.

SESSION 4: Tracking Progress *(Meramec Ballroom)*
Moderator: Daniel J. Hayes, US Army Corps of Engineers

The Status of RIBITS Nationwide: Mark Sudol, US Army Corps of Engineers
An Ecological Assessment of Ohio Mitigation Banks: John J. Mack, Ohio EPA
Mitigation Bank Status and Evaluation of Ecological Success: Vicki Tauxe, Florida Department of Env. Protection

3:30 PM - 4:00 PM BREAK

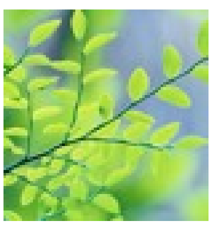
4:00 PM - 5:30 PM
SESSION 5: Stream Mitigation Banking *(Miss. Ballroom)*
Moderator: Lawrence J. Urban, Montana DOT

Large Scale Dam Removal as Mitigation: J. Adam Riggsbee, Restoration Systems LLC
Bannister Creek Mitigation Bank: John Hutton, Acer Environmental Inc.
Determination of Stream Credits: Shawn Sullivan, US Army Corps of Engineers

SESSION 6: Improving the IRT (MBRT) Process *(Meramec Ballroom)*
Chair:Palmer Hough, US EPA

Virginia as a Microcosm of the National Mitigation Banking Effort: Steve Martin, US Army Corps of Engineers
MBRT: What Works and Doesn't Work from a Banker's Perspective: Craig Denisoff, Westervelt Ecological Services
Training Program for Interagency Review Teams: Kris Hoellen, The Conservation Fund

5:30 PM - 7:00 PM
Reception in Exhibit Area
Hosted by Loafer Creek, LLC and JT&A Inc.



About the Ecosystem Marketplace

The Ecosystem Marketplace is the world's leading source of information on markets and payment schemes for ecosystem services; services such as water quality, carbon sequestration and biodiversity. We believe that by providing solid and trust-worthy information on prices, regulation, science, and other market-relevant issues, markets for ecosystem services will one day become a fundamental part of our economic and environmental system, helping give value to environmental services and thereby helping conserve them.

The Ecosystem Marketplace is a project of:

FOREST TRENDS

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This Publication made possible in part through the sponsorship of:

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