Financial Evaluation of the Right-of-Way Acquisition Loan Fund (RALF)

Program

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Introduction

Purpose

The purpose of this study is to review and assess the Metropolitan Council's Right-of-Way Acquisition Loan Fund (RALF) program to evaluate its financial efficiency over the past 30 years, to determine its future viability and to make recommendations for continued management of the program.

Background

The Metropolitan Council is responsible for transportation planning and transit operations including aviation, highway and transit systems in the seven-county Twin Cities metropolitan area. Since 1982 Mn. State law 473.166 (establishing the Right-of-Way Acquisition loan fund, or "RALF") has allowed the Council to levy a regional property tax for advance acquisition of officially mapped highway rights of way threatened by imminent development. The law was subsequently amended to acquire any officially mapped right-of-way that becomes available on the open market. The levy currently generates approximately $3.6 million per year. The funds are used by the Council to make interest-free loans to counties, cities and towns, which in turn buy the property within the officially mapped right-of-way for state trunk highways or metropolitan highways. The city retains title to the property until the Minnesota Department of Transportation (MnDOT) purchases it immediately prior to construction and the loans are repaid to the revolving RALF fund.

The cost of highway right-of-way can represent a significant share of the overall cost of the project and at times may represent more than half the total project cost. Acquiring right-of-way well in advance of highway construction can be financially beneficial if it pre-empts development or averts the longer term appreciation of property value. Advanced acquisition can also have non-financial benefits such as purchasing homesteaded properties facing hardship.

RALF Program

The revolving RALF loan program provides a funding source to enable early acquisition of these highway rights-of-way. The Metropolitan Council lends money to the cities to purchase right-of-way from willing sellers in certain in certain officially mapped highway corridors. Cities are responsible for having the property appraised and negotiating the price with the owners (which MnDOT reviews and certifies). The total loan amount also includes city-incurred expenses for acquiring the property including appraisal fees, review appraisal fees, title research, field title reports, pro-rated property taxes, relocation costs and closing costs. Net income derived from the properties while under city ownership is returned to the RALF fund.

Study Methodology and Land Cost Analysis

The Metropolitan Council contracted with ProSource Technologies, LLC (ProSource) to collect and analyze data from the RALF loan records. Key elements required for this analysis include:

- Purchase price of property used for right-of-way;
- Acquisition cost(s) involved in property purchase;
- Relocation benefits (if any);
- Projected value at the time of project construction based on available resources

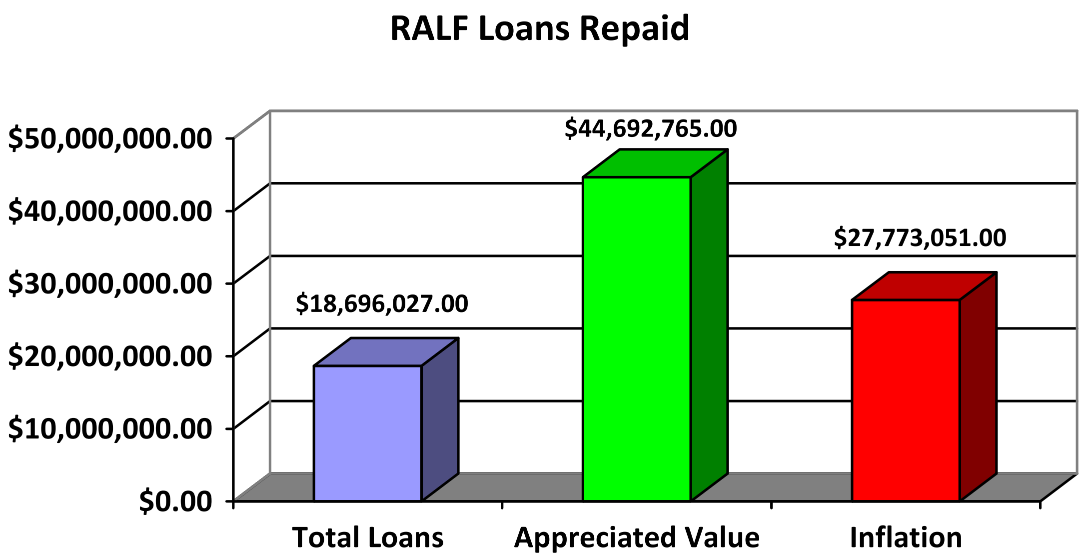
Since the fundamental benefit of the RALF program is the avoidance, through advance purchase, of higher property costs due to real estate development or appreciation, the study reviews initial property purchase prices under the program versus the expected property purchase prices. The analysis calculated costs using the Net Future Value (NFV) methodology, which compares present day monetary value to future monetary value. The analysis covers all loans since RALF's inception in 1982, including 55 completed (repaid) projects as well as 57 outstanding loans.

The analysis covers parcels that were purchased by certain participating cities for later purchase by MnDOT. Corresponding values were generated on 1) the purchase value of the land at the time of the purchase by the city and 2) the projected value at the time MnDOT purchased the right-of-way. For loans that have not yet been repaid the second value calculated was the estimated current land value. The RALF loan amount includes the purchase price of each parcel and the acquisition delivery costs (acquisition labor, relocation costs and any administrative costs). Relocation costs are included in hardship loans.

The price of land was adjusted by the annual average increase or decrease in land value in the Twin Cities' metro area for each of the years between the time of purchase of the land under the RALF program and the estimated purchase date of the land by MnDOT. The price of the acquisition delivery costs were adjusted annually for the rate of inflation.

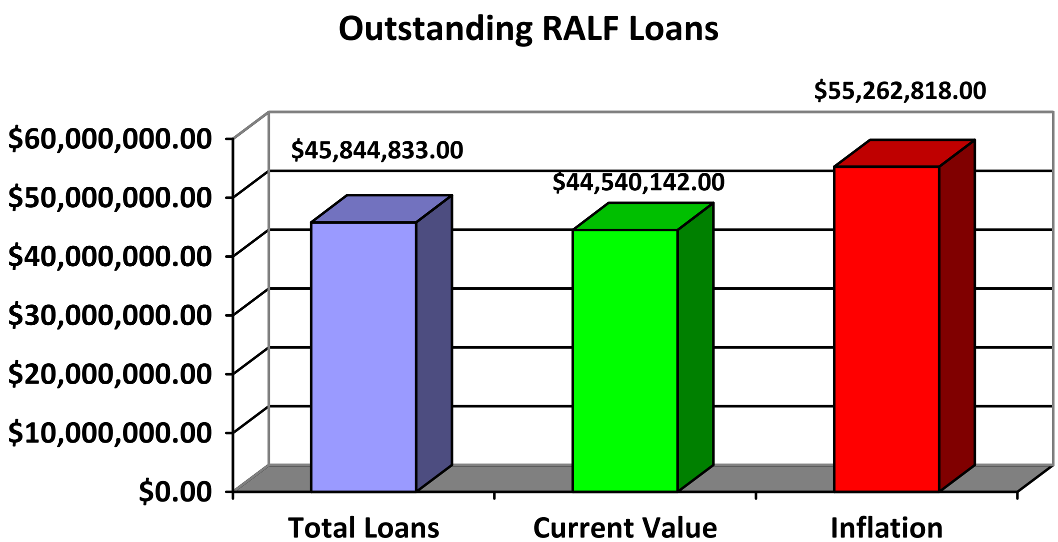
Once we determined the estimated land value at loan payoff, the purchase amount was compounded for inflation. This was calculated by multiplying the purchase price by the corresponding inflation rate for each applicable year. This step equates the time value of the actual and estimated purchase values as of the payoff moment. The difference in these values, then, represents the "real" gain or loss, expressed as the Net Future Value.

A major purpose of this evaluation is to determine the financial performance of the RALF program since inception. Analyses of loans that have been repaid show a net gain of $16.9 million. Loans currently outstanding show a current value of $10.7 million decline in value. The total net shows a savings of $6.2 million dollars. The charts below show summarize the total value of loans that have been repaid to date, and those that are still outstanding.



Total Loans	Appreciated Value	Inflation	Net Gain
$18,696,027	$44,692,765	$27,773,051	**$ 16,919,715**

Most of the loans represented above were repaid prior to 2006, i.e., during the extended real estate boom. In such an environment, RALF's ability to fund advance property acquisitions realized significant value.



Total Loans	Current Value	Inflation	Net Difference
$45,844,833	$44,450,142	$55,262,818.	**($10,722,676)**

More recent outstanding loans, by contrast, reflect the reality of the declining real estate market, and show an estimated aggregate current value of $10.7 million less than the purchase price. Because the properties are still subject to real estate prices, the numbers could be significantly different in five years. The real estate market could stay flat and appreciation would be minimal. Conversely, the market could rebound and we could see appreciation rates of the late nineties through 2005. There are many variables that affect real estate some of which are the economy, interest rates, politics and buyer demand. Many of the outstanding loans, thirty of the loans totaling $27.4 million, were issued in 2006 or later. Since then, real estate values have dropped significantly in both the Metro and nationwide.

While it is difficult to predict the future of the real estate market over the next ten years, it should be noted that real estate prices have had an upward trend and have outpaced inflation over the past thirty years, as shown in the graphs below compiled by Dr. Robert Schiller of Yale University, a leading real estate economist.

In the long term, holding real estate outpaces inflation and thus increases in value. In the case of the loans that have yet to be repaid it is impossible to determine if savings will be realized. Below is a summary of RALF loans extended, savings achieved and loans outstanding. For loans that were made from the program's inception and since repaid, the indication is that the RALF program has been successful in advancing the public interest. It is less clear with regard to the outstanding loans at this time, while the overall real estate market is depressed. A clear determination of the value of these loans cannot be made until the loans are repaid.

The total land cost analysis is summarized below; individual statistics on all the repaid RALF loans are included by city at the end of this report.

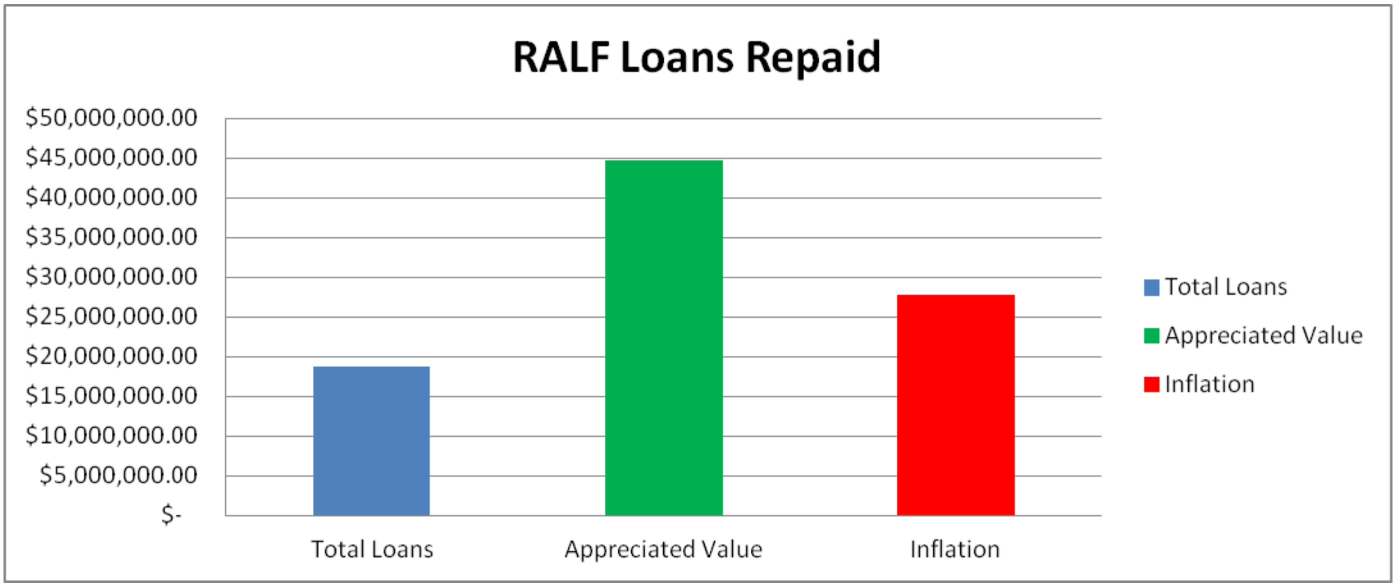
	Amount	Appreciated Value	Inflation	Net Gain / Loss
RALF Loans Repaid	$18,696,027	$44,692,765	$27,773,051	$16,919,715

RALF Loans Outstanding	$45,844,833	$44,450,142	$55,262,818	**($10,722,676)**
Total	**$64,540,860**	**$89,142,907**	**$83,035,868**	**$6,197,039**

Below are the rollups by cities for loans that have been repaid.

RALF Loans Repaid

City	Total Loans		Appreciated Value		Inflation		Net Gain	
Brooklyn Park	$	796,738.00	$	2,409,879.00	$	1,421,832.00	$	988,047.00
Chanhassen	$	2,303,889.00	$	4,937,173.00	$	2,897,554.00	$	2,039,619.00
Chaska	$	5,580,200.00	$	13,923,273.00	$	8,269,417.00	$	5,653,856.00
Eden Prairie	$	2,929,519.00	$	6,487,876.00	$	4,082,287.00	$	2,405,590.00
Inver Grove Heights	$	730,776.00	$	2,409,788.00	$	1,421,831.00	$	987,957.00
Maple Grove	$	4,304,728.00	$	9,705,611.00	$	6,417,382.00	$	3,288,229.00
Richfield	$	636,125.00	$	793,180.00	$	764,011.00	$	29,170.00
Shakopee	$	1,166,438.00	$	3,365,382.00	$	2,128,767.00	$	1,236,615.00
Woodbury	$	247,613.00	$	660,603.00	$	369,970.00	$	290,633.00
	$	**18,696,026.00**	**$**	**44,692,765.00**	**$**	**27,773,051.00**	**$**	**16,919,716.00**

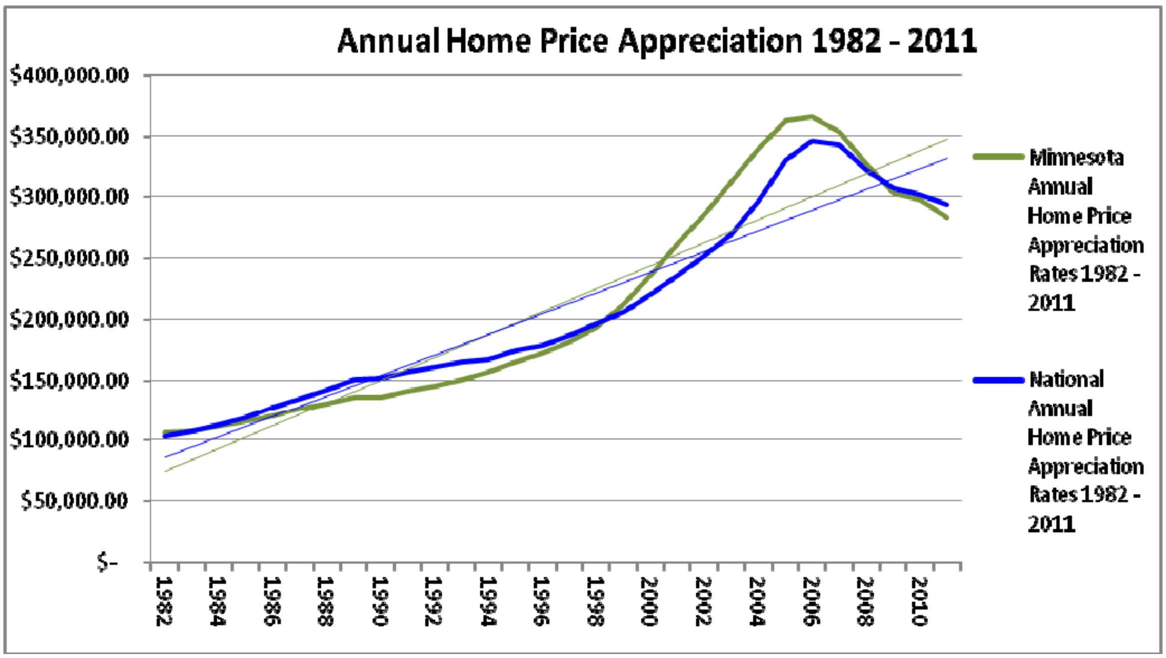


Other Financial Considerations in Evaluating RALF

In addition to the land cost analysis ProSource researched three other financial issues for consideration in the analyzing of the RALF program. Housing cost trends, transition zone land values and lost property tax revenue are described below.

Housing Cost Trends

Below is a chart showing annual home value appreciation / depreciation between 1982 and 2011 in the Twin Cities as well as nationwide. The numbers were obtained from Forecast-Chart, which is a service of Signal Trend, Inc.



The period between 1998 and 2006 saw double-digit appreciation in the housing market, fueled by economic activity, population growth and interest rates. Since 2007, there has been dramatic depreciation in the housing market that only recently has shown signs of recovery. Despite these extremes in performance, and annual volatility, the average from 1982 to 2011 shows a positive upward slope in appreciation.

The average value of homes in the Twin Cities' housing market fluctuated more than the national average home price between 1982 and 2011. The trend line indicates that the Twin Cities' housing values have been slightly higher than the national average over the past thirty years.

Transition Zone Land vs. Fully Developed Land

In addition to the Land Cost Analysis above, ProSource also considered the economic advantage of acquiring undeveloped right-of-way before it transitions to a higher and better use. An appraiser uses both “market” and “income” approach for each property to best determine its optimum current market value. As part of the appraisal, consideration is given to the “highest and best” use of the property, which might not be its current use. For example if the property is currently zoned agricultural it would be valued as farmland. However, if the property were adjacent to fully developed land (the transition zone) and the necessary public infrastructure to develop it were available, then the value of the land could be significantly higher than farmland.

As part of the study, ProSource interviewed its own and other appraisers who have valued transitional land for anticipated road projects. These appraisers all agree that valuing land in the “transition zone” is extremely difficult due to factors such as zoning change approvals, development and platting approvals, the timing and availability of public infrastructure and the cost of building gas and electric lines to a new development. They also agree that converting land from transition zone property to fully-developed property dramatically increase its value. It would reasonable to assume its square foot value could increase by 10 to 20 times when fully developed. In addition to the costs of the land itself, associated expenses such as acquisition, relocation and administrative costs may increase significantly due to the number of landowners that would be impacted.

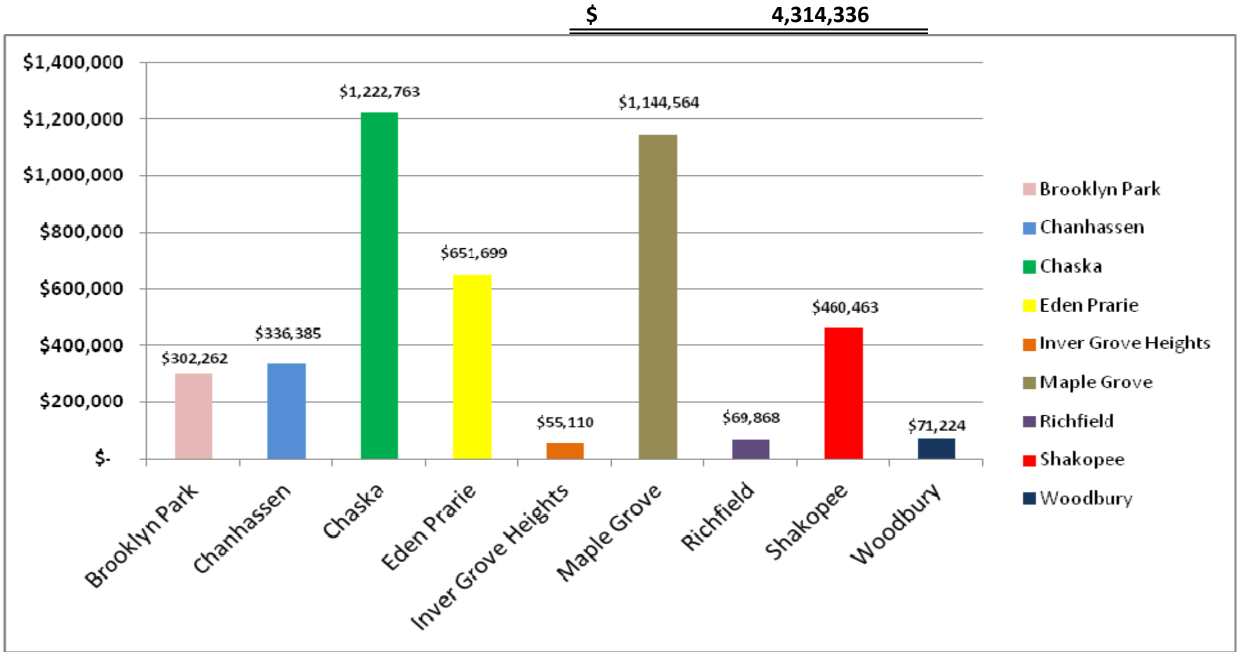
An example follows: Assume that within the next five to ten years MnDOT plans to expand a highway adjacent to a 40-acre parcel that is currently being farmed. This expansion will affect the entire length of the property. The land is on the brink of development and will be divided into 40 one-acre residential lots after the road is expanded. It is assumed that the farmland is currently valued at $5,000 per acre. After the developer has secured all the necessary zoning and building approvals, subdivided the property, and provided infrastructure to the property, each single lot could be sold to a builder for $80,000. Assuming that six acres (or six, one-acre lots) are needed for the highway right-of-way early acquisition under the RALF program, means the six acres of needed right-of-way could be purchased from one property owner for $30,000. Waiting until the road project commences to acquire right-of-way means the market value six lots could be $480,000. This increases the price of the land sixteen fold.

The location of the project and the likelihood of near-term development or redevelopment could make a significant difference in the magnitude of cost savings through advanced right-of-way acquisition. Coordination with local city or county planning and zoning departments could identify the locations most likely to be developed or redeveloped in the near future along road projects.

Exempt Properties and the Effect on City Property Taxes

ProSource also analyzed the implications for municipal tax revenue as a consequence of RALF acquired properties becoming tax exempt. By becoming publically owned land, the city no longer collects property taxes on the property. The methodology to calculate the lost revenue was done by multiplying the projected value of the property by year by the effective tax rate for each applicable year. Because specific tax rate data was not available for the subject cities, the effective tax rates were obtained through the Minnesota Tax Payers Association. The annual numbers were totaled to determine an estimate of what the cities lost in property taxes. The table below shows the total estimated property tax foregone for right-of-way parcels purchased with loans that have been since repaid.

City	Estimated Tax Roll Losses on Loans that have been Repaid
Brooklyn Park	$ 302,262
Chanhassen	$ 336,385
Chaska	$ 1,222,763
Eden Prairie	$ 651,699
Inver Grove Heights	$ 55,110
Maple Grove	$ 1,144,564
Richfield	$ 69,868
Shakopee	$ 460,463
Woodbury	$ 71,224
	$ 4,314,336



ProSource Findings

Financial Value of the Repaid RALF Loans

Repaid RALF loans show a net savings of nearly $17 million. Parcels purchased in the mid-eighties and early nineties have shown the largest savings due to metro area real estate appreciation during that period. ProSource considers this an excellent use of taxpayer dollars with clear indications that the RALF program not only meets needs of the city and the participating individual landowners, but also provides a significant return on investment of public dollars.

Financial Value of the Outstanding RALF Loans

The more recent, outstanding loans, by contrast, reflect the reality of the declining real estate market, and show an estimated aggregate current value of $10.7 less than the total outstanding loan portfolio. Many of these outstanding loans (thirty loans, totaling $27.4 million) were issued in 2006 or later during which time real estate values have dropped significantly in both the metro and nationwide. In the case of the loans that have yet to be repaid it is impossible to determine if savings will be realized. While it is difficult to predict the future of the real estate market over the next ten years, it should be noted that real estate prices have had an upward trend and have outpaced inflation over the past thirty years.

Benefit of Acquiring "Transitional Land"

The location of the highway project and the likelihood of near term development or redevelopment near right-of-way can make a significant difference in the magnitude of savings realized through advanced right-of-way acquisition. Identifying these locations in coordination with local city or county planning departments can help target RALF acquisitions for optimum benefit. Wherever possible, undeveloped right-of-way or right-of-way that is likely to be redeveloped should be a priority for acquisition.

Property Tax Implications

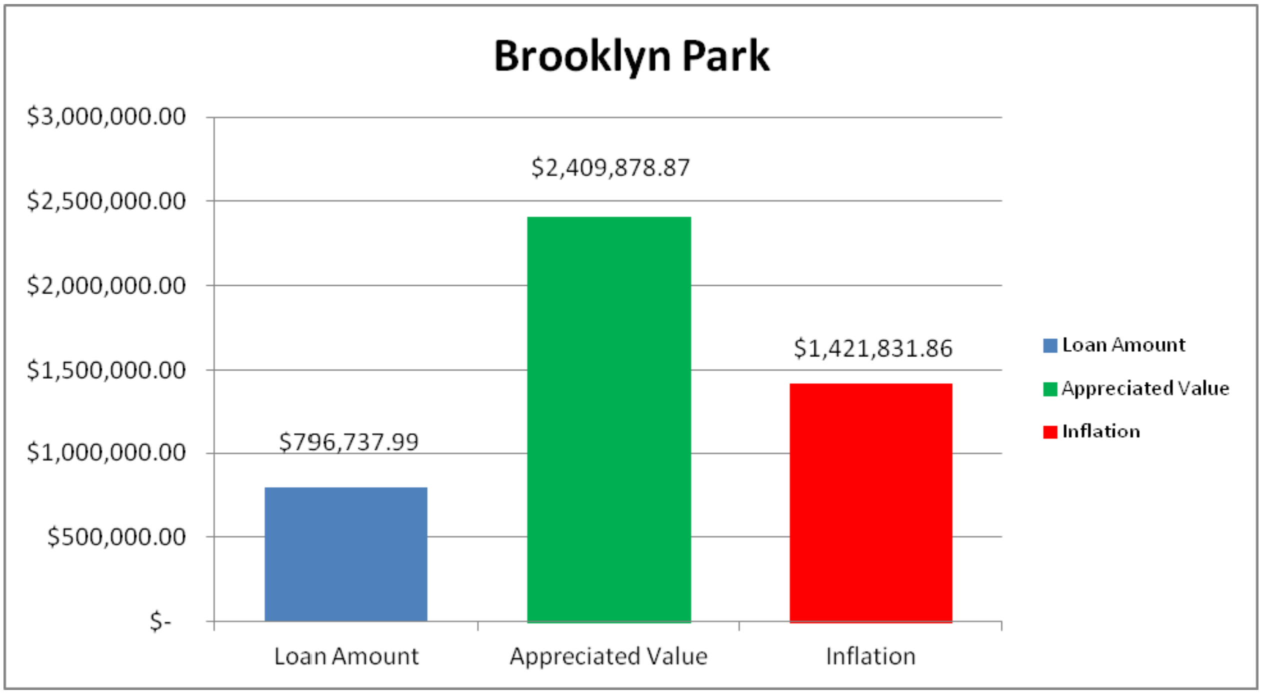
Although the ProSource analysis shows a net gain of about $17 million through the RALF program, it should be acknowledged that properties purchased with RALF loans become tax exempt. The calculated revenue on the repaid loans potentially foregone by the cities totals $4.34 million. These costs are partially offset by the overall $17 million in savings accrued to Mn/DOT.

Appendix

City Data

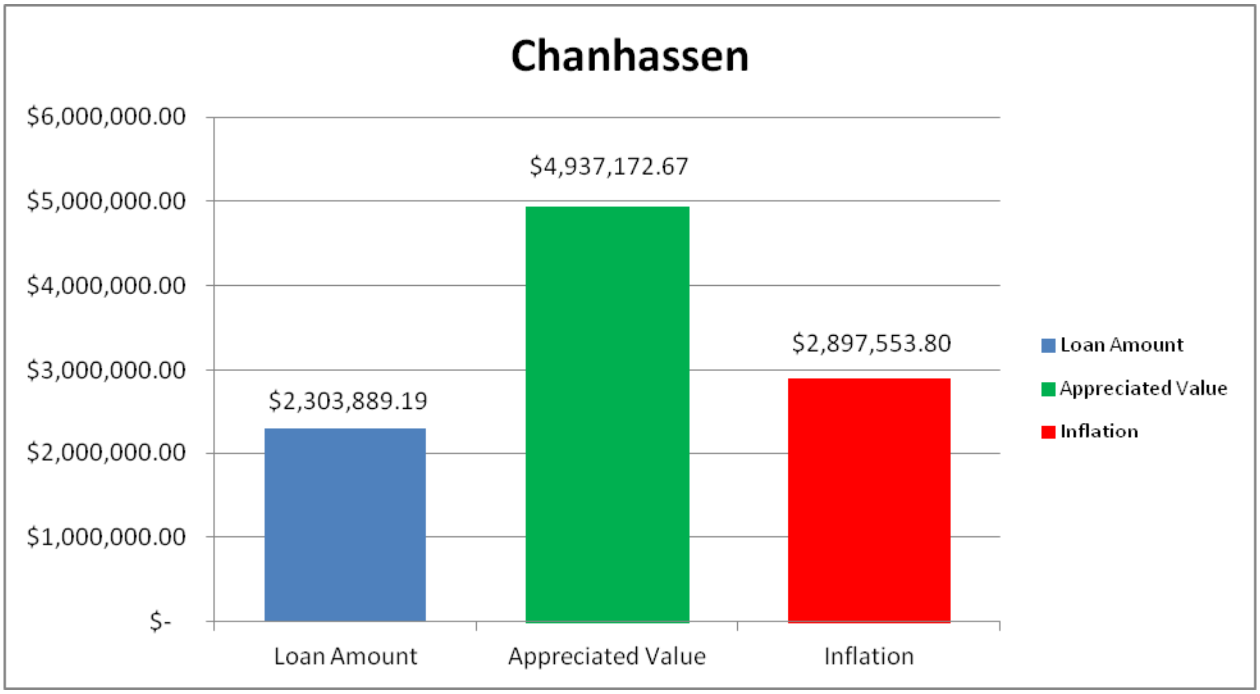
Brooklyn Park

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-86-8	$	65,961.68	$	206,626.95	$	119,718.11	**$**	**86,908.84**
L-87-2	$	730,776.31	$	2,203,251.93	$	1,302,113.75	**$**	**901,138.18**
	$	**796,737.99**	**$**	**2,409,878.87**	**$**	**1,421,831.86**	**$**	**988,047.02**



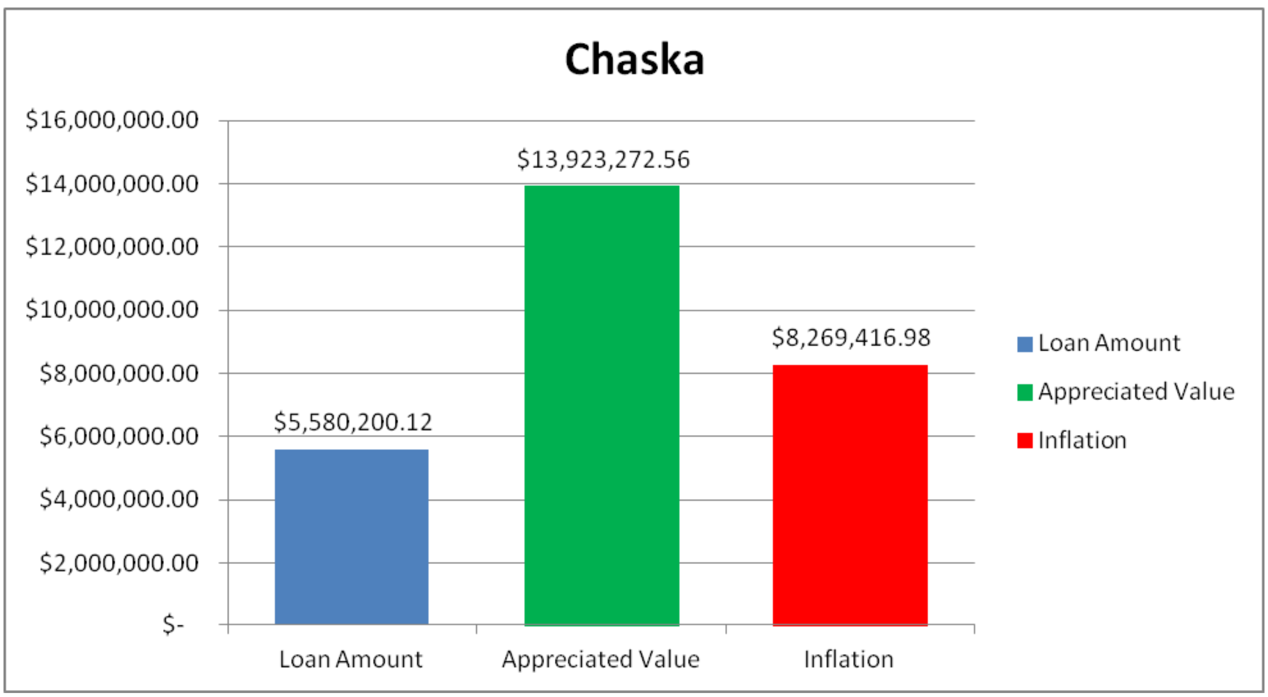
Chanhassen

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-95-6	$	407,889.19	$	945,618.71	$	537,493.43	**$**	**408,125.28**
L-97-3	$	1,896,000.00	$	3,991,553.96	$	2,360,060.37	**$**	**1,631,493.59**
	$	**2,303,889.19**	**$**	**4,937,172.67**	**$**	**2,897,553.80**	**$**	**2,039,618.87**



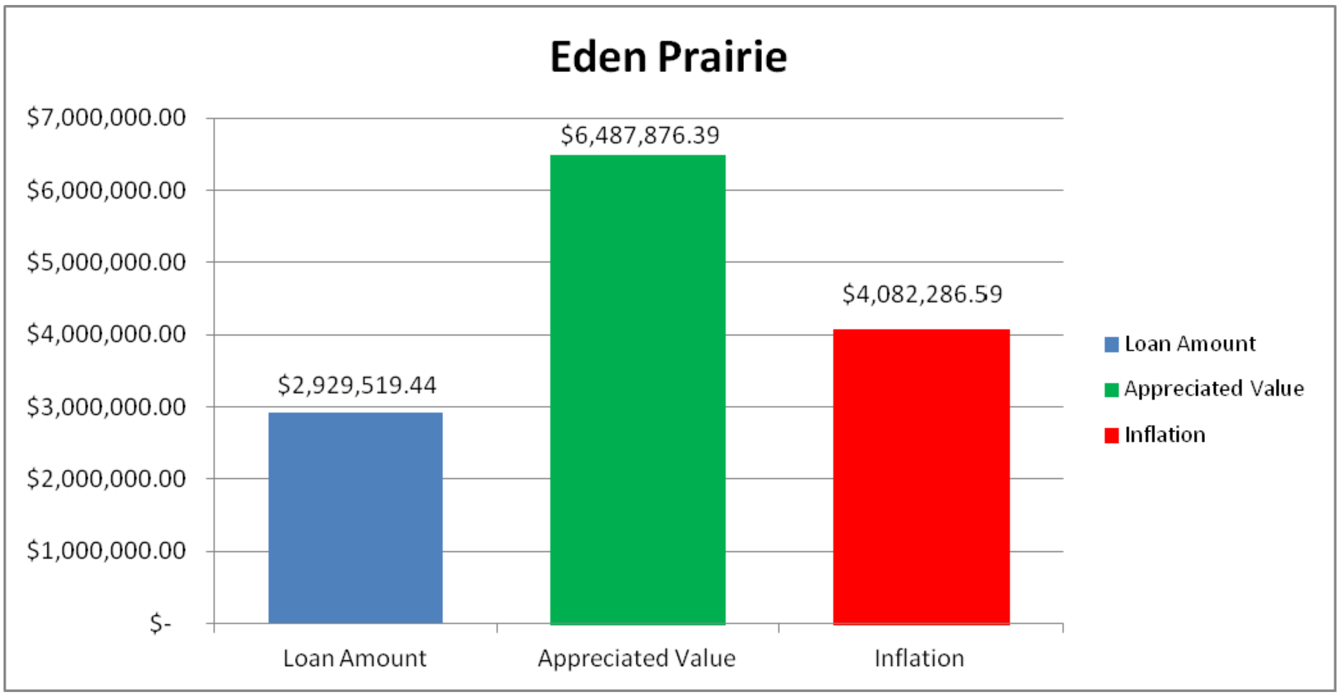
Chaska

Loan Number	Loan Amount	Appreciated Value	Inflation	Net Gain
L-90-1	$ 168,144.00	$ 421,462.51	$ 256,115.74	**$ 165,346.77**
L-92-3	$ 457,597.00	$ 687,741.31	$ 559,668.77	**$ 128,072.54**
L-92-6	$ 203,684.39	$ 523,411.92	$ 292,039.21	**$ 231,372.70**
L-92-12	$ 468,822.12	$ 1,204,741.73	$ 672,189.18	**$ 532,552.55**
L-92-13	$ 242,451.00	$ 623,031.26	$ 347,622.12	**$ 275,409.14**
L-92-14	$ 100,110.59	$ 260,086.04	$ 148,173.10	**$ 111,912.93**
L-92-15	$ 346,121.79	$ 899,220.00	$ 512,292.85	**$ 386,927.15**
L-93-3	$ 294,188.30	$ 744,929.29	$ 422,703.03	**$ 322,226.26**
L-94-1	$ 345,400.64	$ 833,420.70	$ 466,801.36	**$ 366,619.34**
L-94-2	$ 313,694.75	$ 756,917.24	$ 423,951.55	**$ 332,965.69**
L-94-5	$ 836,425.31	$ 2,040,419.50	$ 1,166,922.65	**$ 873,496.85**
L-94-6	$ 70,370.70	$ 171,665.95	$ 98,176.33	**$ 73,489.63**
L-94-7	$ 106,676.64	$ 1,375,060.73	$ 830,152.27	**$ 544,908.46**
L-96-3	$ 305,768.87	$ 679,370.98	$ 404,492.36	**$ 274,878.62**
L-97-4	$ 646,051.37	$ 1,375,060.73	$ 830,152.27	**$ 544,908.46**
L-98-9	$ 294,268.00	$ 592,995.91	$ 369,658.39	**$ 223,337.53**
L-98-12	$ 112,030.15	$ 223,301.90	$ 136,328.46	**$ 86,973.45**
L-99-3	$ 268,394.50	$ 510,434.86	$ 331,977.35	**$ 178,457.51**
	$ 5,580,200.12	**$ 13,923,272.56**	**$ 8,269,416.98**	**$ 5,653,855.58**



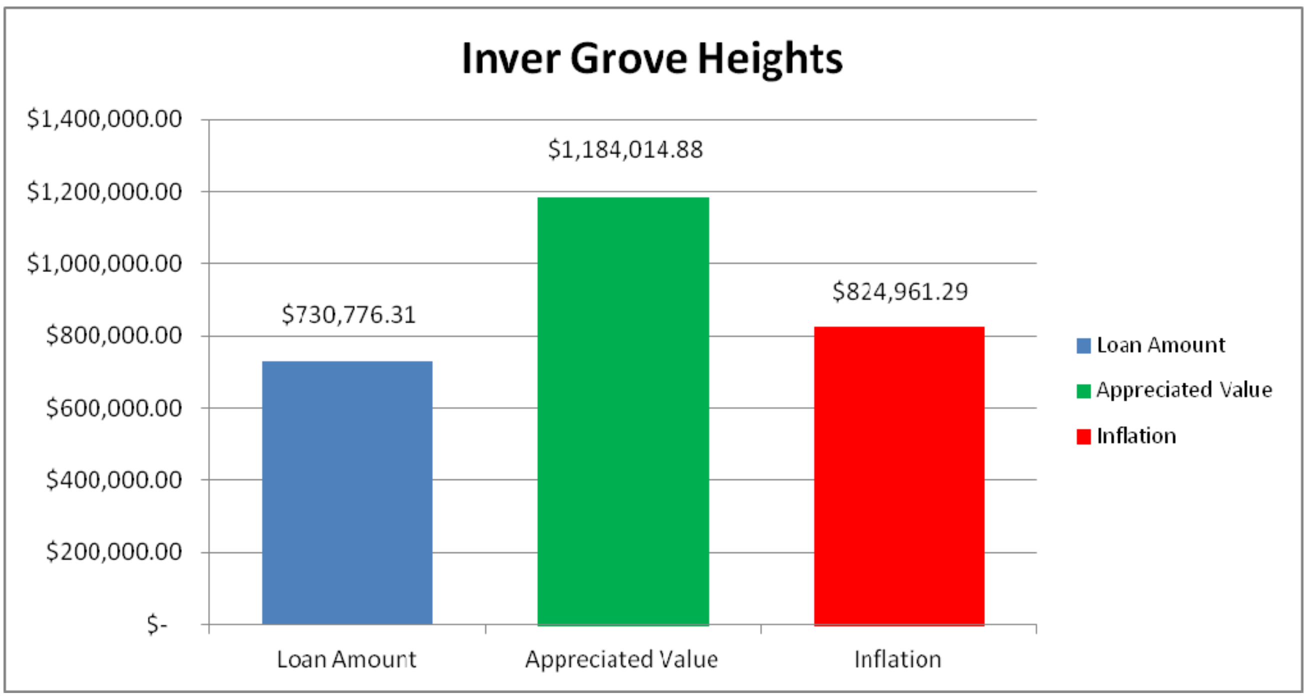
Eden Prairie

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-89-3	$	99,350.00	$	237,500.83	$	154,513.23	**$**	**82,987.60**
L-89-6	$	562,409.47	$	1,344,466.18	$	874,682.45	**$**	**469,783.72**
L-89-7	$	522,854.22	$	1,249,907.50	$	813,164.49	**$**	**436,743.00**
L-91-2	$	135,000.00	$	310,211.43	$	190,040.77	**$**	**120,170.65**
L-94-4	$	1,609,905.75	$	3,345,790.46	$	2,049,885.64	**$**	**1,295,904.81**
	$	**2,929,519.44**	**$**	**6,487,876.39**	**$**	**4,082,286.59**	**$**	**2,405,589.79**



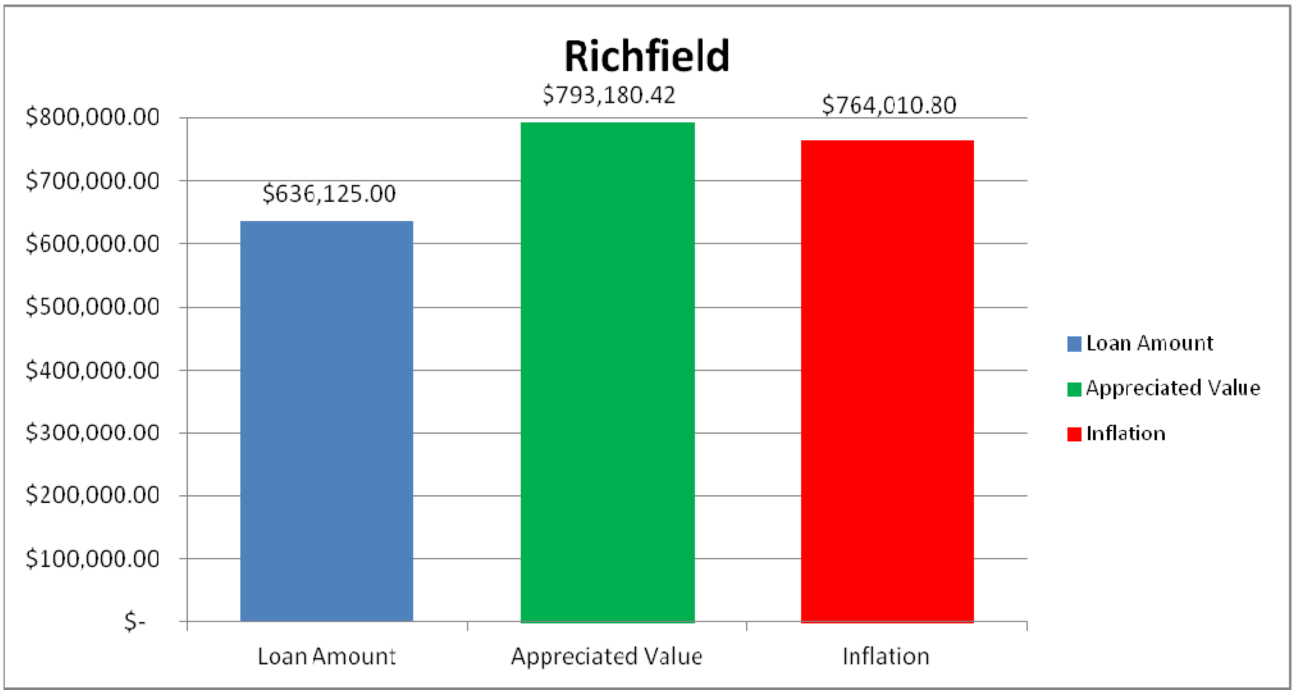
Inver Grove Heights

Loan Number	Loan Amount	Appreciated Value	Inflation	Net Gain
L-99-2	$ 730,776.31	$ 1,184,014.88	$ 824,961.29	**$ 359,053.59**
	$ 730,776.31	**$ 1,184,014.88**	**$ 824,961.29**	**$ 359,053.59**



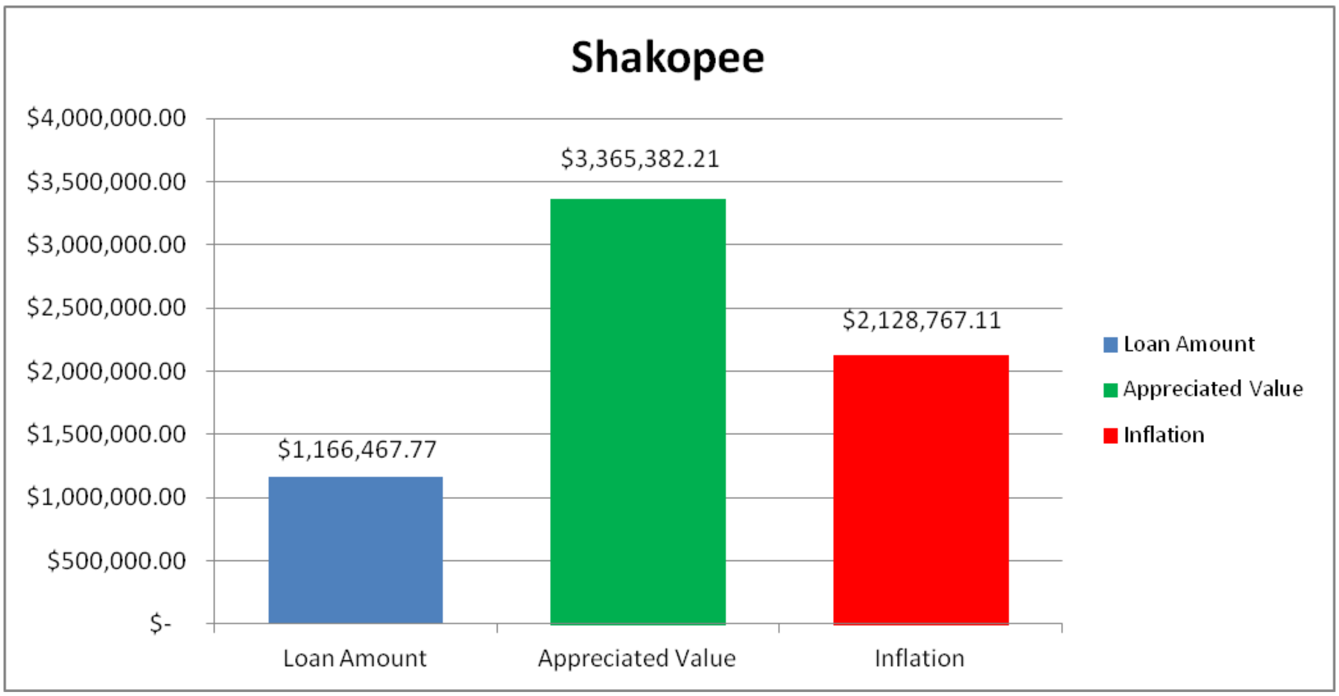
Richfield

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-90-3	$	84,000.00	$	106,843.09	$	106,274.22	**$**	**568.86**
L-90-4	$	148,000.00	$	188,247.34	$	187,245.06	**$**	**1,002.28**
L-91-6	$	103,050.00	$	130,590.39	$	123,696.11	**$**	**6,894.28**
L-92-2	$	110,525.00	$	134,909.56	$	127,309.02	**$**	**7,600.54**
L-92-9	$	100,000.00	$	122,062.48	$	115,185.72	**$**	**6,876.76**
L-92-11	$	90,550.00	$	110,527.58	$	104,300.67	**$**	**6,226.91**
	$	**636,125.00**	**$**	**793,180.42**	**$**	**764,010.80**	**$**	**29,169.63**



Shakopee

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-84-1	$	895,603.00	$	2,616,550.70	$	1,654,487.54	**$**	**962,063.16**
L-85-3	$	182,490.57	$	510,392.19	$	323,162.39	**$**	**187,229.80**
L-86-5	$	88,374.20	$	238,439.32	$	151,117.18	**$**	**87,322.15**
	$	**1,166,467.77**	**$**	**3,365,382.21**	**$**	**2,128,767.11**	**$**	**1,236,615.10**



Woodbury

Loan Number		Loan Amount		Appreciated Value		Inflation		Net Gain
L-91-5	$	247,613.00	$	660,602.67	$	369,969.79	**$**	**290,632.88**
	$	**247,613.00**	**$**	**660,602.67**	**$**	**369,969.79**	**$**	**290,632.88**