Request for City Council Committee Action from the Department of Finance

Date: February 14, 2008
To: Council Member Robert Lilligren, Chair, Committee of the Whole

Subject: Legacy Fund Status Report – Framework for the Future Follow-up

Recommendation: Receive and file.

Previous Directives: On December 20, 2007, as part of its review of Framework for the Future, the Committee of the Whole directed staff as follows:

> Report back in three cycles, explaining the consequences to: a) the Legacy Fund, b) the City's present and future discretionary development funding, and c) Neighborhood Revitalization Program (NRP) funding, if we stopped transferring funds from the Common Project to the Legacy Fund.

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Presenter in Committee: Jack Kryst

Supporting Information

The December 20 presentation to the Committee on NRP Track III spoke in part to the role of the Common Project, the collection of Minneapolis Tax Increment Districts authorized under special law to be the primary funding source for both phases of the Neighborhood Revitalization Program (NRP). The original level of funding was $400 million for NRP and was $600 million for City general development, over the 20-year period ending in 2009. Although Phase I of the NRP and the first year of Phase II were fully funded, legislative changes in property tax law significantly reduced the revenue available for Phase II and left no revenue available for City general development with the exception of debt service.

In 2003, the City Council took companion actions to amend the NRP ordinance and provide for City development funding. An amendment to the NRP ordinance and the Discretionary Development Resolution were adopted.

This report responds to the specific question posed on December 20 concerning the consequences of revisiting an element of the Discretionary Development Resolution that includes the Legacy Fund, NRP capitalization and revenues for City discretionary development.

Legacy Fund
The Legacy Fund represents the proceeds from the 1999 sale of the Minneapolis Community Development Agency's (MCDA) and City's interests in the Hilton Hotel. Net proceeds were received in the amount of $39,970,062. There were no statutory restrictions on how the City could use the revenues in the Legacy Fund; those revenues were not part of the Common Project, and therefore not an obligated part of the funding for NRP.

On July 30, 1999, the Council authorized the City Finance Officer to invest these sale proceeds "...to maximize investment earnings consistent with protecting the principal" and directed that "the investment program be structured so that the principal is retained and the earnings are available for annual appropriation to MCDA community development programs..." Following authorization, $39,970,062 less $50,000 in transaction-related costs was deposited into the Legacy Fund (Fund SPH0). Almost immediately after the fund was created, investment conditions deteriorated. Except for a relatively small return in 1999, the fund continued to accrue losses through 2002 and did not generate earnings to support development.

The Legacy Fund balance as of December 31, 2003, prior to any transactions related to the Discretionary Development Funding Plan, was $33.8 million. In 2003, the Council authorized expenditures to cover costs related to $12.5 million of pension-related debt. A gross expenditure of $13.6 was made and is accounted for in the discussions below.

Discretionary Development Funding Plan
In August 2003, unrelated to the Legacy Fund but as a response to reduced tax increment revenues caused by legislative action, the NRP Ordinance was amended to prioritize the use of the diminished tax increment and other revenues of the Common Project as follows: 1) debt service and other contractual obligations; 2) administrative costs of the Common Project; 3) NRP, up to $20 million per year through 2009; and 4) general development activities of the City. This prioritization of Common Project revenues is often referred to as the NRP waterfall.

At the same time it was recognized that this mechanism would provide no revenues to fund the City's general development needs until 2009. Therefore, the City Council, with the concurrence of the NRP Policy Board (relying on the same City projections), adopted Resolution 2003R-404, which established a Discretionary Development Funding Plan to allow the City (via the MCDA, later CPED) to borrow up to $22 million ($3.679 million annually) from the Legacy Fund for the City's discretionary development needs from 2004 through 2009 and to repay those loans with the subset of Common Project revenues generated from the Brookfield/Gaviidae project. If these Common Project revenues were not used in this way to repay the Legacy Fund, they would have by default been available to capitalize the NRP program.

Consistent with the Discretionary Development Funding Plan, the Council has authorized CPED Legacy Fund expenditures for discretionary development activity in each annual budget from 2004 through 2008, for a cumulative total of approximately $18.5 million. The purposes and allocations are shown in Attachment 1. An additional $3.5 million is to be made available from the Legacy Fund in 2009.

Through 2007, approximately $7 million in revenue has been transferred from the Common Project to the Legacy Fund as repayment for these loans.

Interaction between Common Project Revenues and NRP Funding, Legacy Funding and Discretionary Development Resources

The relationship between Common Project revenues and the available funding for NRP, the available amount of City discretionary development dollars and the Legacy Fund balance is somewhat complicated and at times confuses the funding discussion.

Under both the original and amended NRP ordinance, NRP capitalization and discretionary development are funded from the same Common Project revenues. The amended ordinance goes further and provides that NRP has the first claim to funding, up to $20 million a year.

Since Common Project revenues have not been sufficient to fully fund NRP Phase II, there have not been sufficient revenues to fund discretionary development. The Discretionary Development Funding Plan attempts to address this problem by borrowing from the Legacy Fund, but complicates the issue by repaying these loans from the Common Project, the same revenue stream that would otherwise fund both NRP and discretionary development. This works if the revenue stream is adequate, but is problematic in the post-2001 environment of diminished Common Project revenues. There exists an essentially closed system, with the objectives of NRP capitalization, discretionary development and sustaining the Legacy Fund sharing the same revenues.

Table 1 below shows how the allocation among these uses changes, if the repayment to the Legacy Fund changes.

	NRP PhaseII Funding Total	Discretionary Funding from Legacy Fund and Common Project	Legacy Fund Balance on 01/01/2010	Discretionary + Legacy Bal. on 01/01/10	Total
Under Current Authorities	$72.9	$22.0	$30.4	$52.4	$125.3
Revised Authority Suspending Repayments to Legacy Fund	$79.5	$30.5	$15.3	$45.8	$125.3
Change Increase/(Decrease)	$6.6	$8.5	($15.1)	($6.6)	$0.0

All projections assume Brookfield repayment in 2009 of $27.7 million.
All dollars in millions.

Table 2 shows these changes in greater detail: if pending payments to the Legacy Fund were suspended, those Common Project dollars would flow into the NRP Waterfall and:

1) increase NRP funding in 2008 by $3,538,000 (the maximum amount available);
2) increase NRP funding in 2009 by $3,026,996 (the maximum amount allowable under the annual $20 million cap);
3) increase revenue for discretionary development in 2009 in the amount of $8.5 million, (increasing the discretionary development total to $30.5 million); and
4) reduce the January 1, 2010 Legacy Fund balance to $15.3 million; and
5) reduce combined discretionary and Legacy Fund Balance by $6.6 million.

The size of the Legacy Fund balance on January 1, 2010 (and its capacity to generate investment revenue) is an important consideration if the City expects to continue its existing policy to use this fund for discretionary development purposes after 2009. No other funding source has been identified for discretionary development.

Table 2

IMPACT ON NRP - PHASE II & DISCRETIONARY COMMON PROJECT REVENUE

Year	Oct 2007 NRP Capitalization Projections*	Adjusted NRP Capitalization Projections w/o repayments to Legacy Fund*	Increase or (Decrease) in NRP Capitalization		Oct 2007 Projected Discretionary Common Project Revenue	Adjusted Discretionary Common Project w/o Repayments to Legacy Fund
2001	20,000,000	20,000,000			0	
2002	11,000,000	11,000,000			0	
2003	10,749,791	10,749,791			0	
2004	4,751,683	4,751,683			0	
2005	1,314,824	1,314,824			0	
2006	1,244,191	1,244,191			0	
2007	2,075,351	2,075,351			0	
2008	4,802,177	8,340,177	3,538,000		0	
2009	16,973,004	20,000,000	3,026,996	**	0	8,465,004
Total Phase II	72,911,021	79,476,017	6,564,996	***	0	8,465,004

79,476,017	allows for Phase II plan allocations to be funded at 76%.
73,006,476	allows for Phase II plan allocations to be funded at 70%.
104,294,966	allows for Phase II plan allocations to be funded at 100%.

* Capitalization includes interest earned from unspent NRP fund balance, the sole source of funding in 2005-2006.
** Amount needed to meet $20,000,000 annual funding threshold.
*** Total additional capitalization of NRP if no further repayments are made to Legacy Fund.

NRP Phase II Capitalization

Table 2 also shows that, if no additional revenue was transferred from the Common Project to the Legacy Fund, the funding for Phase II of the NRP would increase by approximately $6.6 million, and provide approximately 76 percent of the Phase II plan allocations.

In Summary

If the Discretionary Development Ordinance was amended to stop the repayment of Legacy Fund loans made to fund discretionary development and <u>no other changes were made to the NRP Ordinance, Discretionary Development Resolution or Legacy Fund policy</u>, the following consequences would result:

1) The total Phase II capitalization of NRP would increase by $6.6 million.
2) The Legacy Fund balance available on January 1, 2010 would decrease by $15.1 million, with a corresponding reduction in its ability to generate ongoing revenues for development.
3) Additional discretionary development resources in 2009 would increase by $8.5 million.

4) The net effect of items 2 and 3 above would be a reduction of $6.6 million to the discretionary development resources available on January 1, 2010.

Attachment 1

Legacy Fund Allocations 2004 - 2008

	2004 Allocated	2005 Allocated	2006 Allocated	2007 Allocated	2008 Allocated	Program Totals
Commercial Corridors Dev. (Great Streets)				1,150,000	250,000	1,400,000
Close the Gap Employment Initiative	1,000,000	200,000	1,500,000	1,100,000	900,000	4,700,000
Heritage Park Project Management	400,000			500,000		900,000
MILES		1,000,000	600,000	375,000	750,000	2,725,000
Emerging Entrepreneur				325,000		325,000
NEDF/CEDF				250,000		250,000
Planning	300,000	300,000	350,000			950,000
Commercial Corridor Small Business Loan Fund	1,000,000	500,000	500,000			2,000,000
Capital Acquisition Revolving Fund			750,000			750,000
Partnership Matching Fund (EQ2)					1,000,000	1,000,000
Riverfront Development		100,000				100,000
It's All About Kids		200,000				200,000
Affordable Housing Trust Fund	1,000,000				0	1,000,000
Project Liability Funding		1,400,000				1,400,000
5 Point Strategy (Foreclosure)					385,000	385,000
Mortgage Foreclosure Prevention Prog					415,000	415,000
Total	**3,700,000**	**3,700,000**	**3,700,000**	**3,700,000**	**3,700,000**	**18,500,000**