



Legislative Fiscal Bureau

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March 27, 2017

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Natural Resources: Stewardship Grant for Natural Heritage Land Trust Nelson Hook
Lake Project in Dane County -- Agenda Item II

REQUEST

On June 13, 2016, the Department of Natural Resources (DNR) requested approval under s. 23.0917(6m) of the statutes to provide a grant of \$346,100 from the land acquisition subprogram of the Warren Knowles-Gaylord Nelson Stewardship Program to the Natural Heritage Land Trust for the acquisition of 102.5 acres in Dane County. The project, known as the Nelson tract, is located in the Town of Dunn. The Department submitted a letter to the Committee Co-Chairs on June 30, 2016, noting their desire to use fiscal year 2015-16 funds for the grant project unless there was an objection by the Committee. Notice of an objection to the proposed grant was made on July 1, 2016.

ANALYSIS

Background

DNR would award the Natural Heritage Land Trust (NHLT), up to \$346,100 in the form of a matching grant from the land acquisition subprogram of the stewardship program to assist with the cost of acquiring 102.5 acres in the Town of Dunn, Dane County, from the estate of Richard W. Nelson and Arlene Nelson for approximately \$685,000. Total approved eligible grant costs are \$692,100, leaving \$346,000, or 50%, of eligible costs remaining after the requested stewardship award. The grant sponsor, NHLT, is expected to also receive support from other grant partners, including the Town of Dunn (with an anticipated funding commitment of \$60,000) and Dane County (with anticipated funding of up to \$286,000). The NHLT has a signed purchase agreement with the estate for a purchase price of \$685,000 to be closed on or before November 30, 2016, contingent on Stewardship grant funding approval. The seller has informally agreed to extend this deadline to allow for Committee review.

The property is contiguous to DNR's Hook Lake Wildlife and State Natural Areas and located within the DNR Hook Lake Bog/Grass Lake Wildlife Area acquisition boundary. The DNR and the Town of Dunn jointly hold a conservation easement on the property. The easement was purchased in March, 2003 (for \$207,000) and prevents subdivision and development of the property (with the exception of a 2.44-acre area where a homestead is currently located and where buildings may be renovated or replaced). The easement does not allow public access. According to the Department, acquisition of the parcel by the land trust will provide enhanced public access to the adjacent Wildlife Area, which currently has limited parking and limited access. Currently, there is space for about 12 cars total for the entire property. This is split into two parking/access areas, each one located approximately one mile from the center of the DNR property. The parking closest to the Nelson property is located off Hawkinson Road, north of the Wildlife area, and includes parking for four to five cars at the beginning of a 2,700 foot long, 30 foot wide, walk-in access easement that proceeds south to the DNR-owned land. The second parking access is on the south end of the DNR property, and includes a seven- to eight-car area off McManus Drive, a shared drive to a private land holding. There is currently no parking or access on the eastern boundary of the DNR property. If successful, the Nelson purchase would accommodate a third parking lot, off Hawkinson Road at a location about one-half mile from the core of the DNR Wildlife Area.

The land trust plans to coordinate management of the property with DNR in accordance with the DNR plan for the adjacent Wildlife Area. The property would be initially leased for sharecropping, and converted to natural grassland in approximately three to seven years. Land trust staff also indicate that grazing of the grassland, consistent with wildlife habitat goals, would also be considered. The conversion of the property to grassland habitat would, according to the Department, facilitate a viable core of contiguous grassland habitat. This would enhance the quality of pheasant hunting for the Wildlife Area, which is currently stocked with pheasants. The property would be open to the public for nature-based outdoor recreational activities including hunting, trapping, hiking, cross-country skiing, and wildlife viewing. There are no fishable waters on the property.

2015 Act 55 reduced the amount of authorized bonding available for the stewardship program. Beginning in 2015-16, \$21 million of the \$33.25 million total available annually is available for the land acquisition subprogram. Of that amount, the Department is required to set aside at least \$7 million (previously \$12 million annually) for matching grants awarded only to non-profit conservation organizations (NCOs) such as the Natural Heritage Land Trust. Grants to NCOs for land acquisition are generally provided for up to 50% of the land's current fair market value, or 75% in certain circumstances, plus certain other acquisition costs as determined in rule by DNR. At the end of each fiscal year, any remaining NCO allocation is available for grants to county forests in the subsequent year. For fiscal year 2015-16, DNR awarded approximately \$5.1 million in grants to NCOs, not including this proposed grant to NHLT, leaving \$1.9 million available for county forest grants in fiscal year 2016-17. This would be in addition to the \$5 million each year set-aside specifically for county forest grants.

Appraisals Summary

DNR, local governments, and NCOs hire private real estate appraisers to determine the fair

market value of prospective land purchases. Under the stewardship program, DNR is statutorily required to utilize at least two appraisals for grants for the purchase of land valued at over \$350,000. DNR utilizes certified real estate appraisers to meet this requirement. The private appraisers estimate the fair market value of the property being considered for purchase utilizing a variety of approved standards.

Two appraisals were commissioned for the Nelson property. Appraisals were completed in June, 2015, for NHLT and in December, 2015, for DNR. The first appraisal (for NHLT) utilized both the cost approach and market approach to establish a final value of \$574,000. The market approach was utilized to value the land while the cost approach was utilized to value the improvements. The cost approach is based on the principle of substitution, which asserts that no prudent buyer or investor will pay more for a property than that amount for which the site could be acquired, and on which improvements that have equal desirability and utility can be constructed without undue delay. It is a method of appraising property based on the depreciated reproduction or replacement cost (new) of improvements, plus the market value of the site. (The appraisal also valued the parcel without the 3.5-acre developed parcel at \$454,000; however, as the grant was related to the property as a whole, DNR's review appraiser did not review this aspect of the appraisal.) The second appraisal (for DNR) utilized the market approach to establish a final value of \$685,000. DNR's review appraiser reviewed the appraisals and approved the second appraisal, for \$685,000 for the purposes of determining grant value.

TABLE 1

Appraisals (Conducted in 2015)

	<u>Land Value (per acre)</u>	<u>Improvements</u>	<u>Total Value</u>
Appraisal #1 (commissioned by NHLT)	\$512,500 (\$5,000 per acre)	\$61,500	\$574,000 (\$5,600 per acre)
Appraisal #2 (commissioned by DNR, approved for purposes of grant award)	\$605,000 (\$5,900 per acre)	\$80,000	\$685,000 (\$6,700 per acre)

The NHLT appraisal, completed in June, 2015, utilized a combination of the market and cost approach to establish a final value of \$574,000. The property is zoned Exclusive Agriculture (A1), which allows agricultural use and uses "consistent with agricultural use" and requires a minimum lot size of 35 acres. Uses "consistent with agricultural use" must meet the following conditions: (a) the activity will not convert land that has been devoted primarily to agricultural use; (b) the activity will not limit the surrounding land's potential for agricultural use; (c) the activity will not conflict with agricultural operations on the land subject to a farmland preservation agreement; and (d) the activity will not conflict with agricultural operations on other properties. The appraiser notes that the goal of this zoning is "to preserve productive agricultural land and to prevent land use conflicts between incompatible uses...and comply with the provisions of the Farmland Preservation Law." It is also noted that the Town of Dunn has adopted a more restrictive policy with regard to the size of parcel splits (land divisions) where the maximum size of a new parcel (split from a larger parcel) is two acres and new lots must be placed in an area of the larger parcel in a manner consistent with the town's use plan. The appraiser notes that the Town of Dunn "has been a leader

within the county in creating and enforcing a strong, comprehensive land use plan." As a result of the land use plan, the Town's Purchase of Development Rights Program, and other county and state programs, a large portion of the town is restricted from development. Due to the existing conservation easement, the appraiser noted that the subject property cannot be subdivided and there are no additional development rights.

The highest and best use of the property is considered to be a continuation of the current uses which are agricultural and related residential (the single farmstead). The property has been used for agriculture and farmstead activities for some time, and the Nelson family has owned the property since 1945. It contains approximately 75 acres of cropland which was leased for sharecropping at the time of the appraisal, 15 acres of pastureland, seven acres of woods, and the remainder farmstead. The farmstead includes a home, detached garage, and outbuildings (pig barn, barn, and tobacco shed). The appraiser notes that generally similar properties would be developed for home sites to the extent allowed by zoning, the physical features of the property, and the town use plan. However, the appraiser notes that given that the property is subject to a conservation easement, the development options are not available. Therefore, the appraiser determined the highest and best use of the property to be agricultural and farmstead residential, within the confines of the existing easement. As noted, the easement allows for the renovation or replacement of the existing buildings on a 2.44-acre homestead portion of the property.

The appraiser used four vacant land sales in Dane County, with the same zoning as the subject property (A1 Exclusive Agriculture), to determine a per-acre value for the land (one from 2015, one from 2014, one from 2013, and one from 2011 which was included because it was subject to a conservation easement). The original sale prices ranged from \$4,700 per acre to \$6,900 per acre. Adjustments were made between the subject property and each of the sales for sales date (a 2% per year adjustment was made for time), location, zoning (no adjustment necessary as all were zoned A1), topography/land cover soils, access/utilities, floodplain/wetlands, improvements, highest and best use and appeal. After adjustments, the indicated range for the subject property was \$4,600 to \$6,500 per acre. Sale #3 for \$5,300 per acre in 2011 was considered the most comparable; it was located in the same township, close to the subject property, and, like the subject, was subject to a conservation easement at the time of sale. However, the sale had superior cropland features to the subject property. The appraisal determined a final value of \$5,000 per acre, or \$512,500 for the 102.5 acres of land. The appraiser utilized the cost approach to estimate the replacement cost of the improvements to be \$329,000, with an additional \$25,000 for site improvements. Estimated depreciation was 10% functional depreciation for the outbuildings, and 60% physical depreciation for the home and 70-95% physical depreciation for the outbuildings [functional depreciation refers to a loss in the value of an improvement resulting from functional problems caused by age or poor design (a measure of how obsolete the improvement is), whereas physical depreciation refers to loss of value from all causes of age and action of the element such as breakage, deferred maintenance, effects of age on construction material, and normal wear and tear]. The appraiser estimated the depreciated value of the improvements at \$61,500 for a total value for the land and improvements of \$574,000.

The DNR-commissioned appraisal, in December, 2015, utilized the market approach to establish a final value of \$685,000 (including a land value of approximately \$605,000 and

improvements at \$80,000). The appraisal notes the property consists of 102.5 acres of agricultural land encumbered with a conservation easement including a 2.44-acre "building area" of improvements including a single family house, garage, pig barn, barn, and outbuildings (large storage building and several small miscellaneous buildings and storage structure), approximately 95.5 acres tillable or pasture, and approximately seven acres of woods. The buildings are noted as tenable but declining in condition and vacant. The appraisal notes the land was farmed by a relative of the owner at the time of the appraisal, although DNR indicates this sharecropping lease has since expired. As noted by the first appraisal, the zoning is A1 Exclusive Agriculture which the appraiser notes allows for primary and secondary farm family residences, day care services for no more than eight children, structures and improvements consistent with agricultural uses, and other ancillary agricultural storage, but no commercial storage. Conditional uses subject to approval would include single family residences, governmental and religious uses, private schools, stables, mineral extractions, the sale of agricultural products and asphalt and ready-mix plants. As noted in the first appraisal, the zoning generally limits the minimum lot size to 35 acres. The subject property conforms to zoning. Similar to the first appraisal, the DNR-commissioned appraiser noted that Dunn Township is "very active in land preservation and has been adamantly opposed to most forms of development" and makes note of the town's Purchase of Development Rights program, established in 1997, allowing landowners to sell off their development rights to a public entity while remaining the owner of record. According to the appraiser, several thousand acres in the Town of Dunn are currently owned or controlled by public or private entities in addition to DNR and Dane County, representing approximately 31% of town lands as of February, 2013. Again, as noted in the first appraisal, the current legal uses are limited by the zoning to one home site per 35 acres, with the conservation easement further limiting development to the 2.44-acre building area (buildings in this area may be restored, maintained, or replaced). The legally permissible use of the subject is therefore limited to agricultural production on the acreage, and owner occupancy or rental of the buildings. Highest and best use is considered to be a continuation of existing uses, agricultural production on the subject's tillable acreage and farmstead residential, either owner occupancy or rental of the buildings.

The appraiser used four agricultural land sales in Dane County, within eight miles of the subject property, to determine an opinion of value (one sale from 2011, two from 2013, and one from 2015). Three of the sales were unimproved and one sale had improvements. The original sale prices ranged from \$5,200 to \$6,300 per acre. No adjustments were made for terms or motivation and a 3% per year adjustment was made for time of sale. Adjustments were also made between the subject property and each of the sales for location/soils, size/scale, topography/cover, building rights and encumbrances. After adjustments, the indicated range for the subject property was \$6,200 to \$7,000. This included the appraiser's valuation of the improvements to the subject property at \$80,000 based on two similar properties that sold within approximately the year prior to the appraisal. The DNR-commissioned appraiser concluded that a mid-range value for the subject parcel was appropriate, although leaning toward the high end of the range. The appraiser noted that Sale #1 at an adjusted value of \$6,200 was the lowest; while it was in close proximity to the subject and had similar soil, the appraiser noted that the property was sold to the Department of Corrections (who had been renting the property as an extension of the Oregon State Farm), a different type of buyer than the subject property would expect. The appraiser noted the similarity of Sale #2, which was the same sale from 2011 that was used in the NHLT-commissioned

appraisal, which had a conservation easement; however in this case the appraiser valued the property after adjustments at \$6,700 per acre (including improvements), whereas the appraiser for the NHLT-commissioned appraisal valued the property at \$5,600 per acre after adjustments. Sale #3, at an adjusted value of \$6,500, did not have a conservation easement, but did have similar improvements to the subject property (an old house and outbuildings), but had more tillable land (100% tillable versus the subject property being approximately 93% tillable) and sold in 2013 so was adjusted upward for time of sale. The appraiser established a final value of \$6,700 per acre, or \$686,750 for the 102.5 acres, and concluded that fair market value was \$685,000, rounded.

The Department's appraisal reviewer, after reviewing both appraisals, approved the DNR-commissioned appraisal (Appraisal #2) amount of \$685,000 for the purposes of awarding the grant. Regarding the land value, according to the reviewer, the DNR-commissioned appraisal used sales in closer proximity to the subject property. The reviewer also noted that the range in sale prices was \$5,200 to \$6,200, a difference of \$1,000, for the DNR-commissioned appraisal (Appraisal #2) versus \$4,700 to \$6,900 for the NHLT-commissioned appraisal (Appraisal #1), a difference of \$2,200. The reviewer noted that the larger difference in the sale range and the more adjustments made, the more subjective the indicated value may become. Under this reasoning, the DNR-commissioned appraisal was viewed as less subjective. Regarding the improvement value, Appraisal #2, for DNR, concluded that the value of the improvements was \$80,000, a value which was tied to market sales. While noting that the appraiser's information regarding the improvement value was limited, the reviewer was able to find additional sales to establish that the appraiser's indicated value was supported in the market. The NHLT-commissioned appraisal, which valued the improvements at \$61,500, used a cost approach to determine the value of the improvements. According to the reviewer, the cost approach is most accurate when the improvements are new or nearly new because this limits the amount of subjectivity in determining the amount of depreciation. The improvements on the subject property are older, and the reviewer notes that some of them could be considered obsolete. The reviewer concluded that the value of the improvements was more accurately estimated through a market approach than a cost approach. Overall, the reviewer considered the DNR-commissioned appraisal to have less subjectivity and more market support, and approved the \$685,000 value.

When the Department purchased the conservation easement on the subject property in March, 2003, two appraisals were commissioned to determine the value of the easement. The two appraisals used a before and after approach (valuing the land before and after the easement) to determine the value of the easement. These appraisals valued the land only, as the easement was not expected to affect the value of the improvements. The first appraisal valued the land at \$512,500 before the easement and \$310,000 after the easement, for an easement value of \$202,500, while the second appraisal also valued the land at \$512,500 before the easement, but at \$256,250 after the easement for an easement value of \$256,250. The Department negotiated a price of \$207,000 (approximately \$2,000 per acre) for acquisition of the easement. The easement was purchased using approximately \$149,800 in stewardship funds and approximately \$57,200 in federal funds from the former USDA Farm and Ranchland Protection grant program. The Town of Dunn contributed \$1 and holds the easement jointly with DNR.

TABLE 2

Appraisals Used for Purchase of Easement (Conducted in 2002)

	<u>Land Value Before Easement (per Acre)</u>	<u>Land Value After Easement (per Acre)</u>	<u>Easement Value (per Acre)</u>
Appraisal #1	\$512,500 (\$5,000 per acre)	\$310,000 (\$3,025 per acre)	\$202,500 (\$1,976 per acre)
Appraisal #2	\$512,500 (\$5,000 per acre)	\$256,250 (\$2,500 per acre)	\$256,250 (\$2,500 per acre)

Valuation Considerations

One approach to determine the current value of the parcel could be to adjust the value of the parcel "after" the easement in 2003 to reflect the change in the value of agricultural land in Dane County from 2002 (when the easement appraisals were conducted) to 2015 (when the new appraisals were conducted for the purposes of the DNR grant). As shown in Table 2, the two easement appraisals determined the "after" value of the 102.5-acre parcel to be \$256,250 (\$2,500 per acre) and \$310,000 (approximately \$3,025 per acre) in 2002. The U.S. Department of Agriculture (USDA) National Agricultural Statistics Service (NASS) publishes annual reports on agricultural land sales by county in each state. Using the change from year to year for each year of reported data for agricultural land sales, without buildings, in Dane County from 2002 when the average price per acre of land sold was approximately \$3,900, through 2015, when the average price per acre of land sold was approximately \$9,300, the adjusted value of the 102.5-acre parcel (land only) would be expected to be between \$5,900 per acre (based on the change from the original 2002 value of \$2,500 per acre) and \$7,200 per acre (based on the original value of \$3,025 per acre) as shown in Table 3. Although it is not known the extent to which factors other than agriculture use (such as development potential) may influence the sales data, the lower value of \$5,900 is consistent with the DNR-commissioned appraisal value of \$5,900 per acre for the land and would support approval of the DNR-requested amount.

TABLE 3

**USDA NASS Dane County Land Sales in Continued Agricultural Use
(Land Without Buildings)
2002 to 2015 and Adjusted Value of Nelson Parcel (Land Only)**

	<u>Average Price/Acre</u>	<u>Change in Average Price/Acre</u>	<u>Number of Transactions</u>	<u>Number of Acres</u>	<u>Nelson Parcel Land Value after Easement Appraisal #1</u>	<u>Nelson Parcel Land Value after Easement Appraisal #2</u>
2002	\$3,914		36	2,635	\$3,025	\$2,500
2003	4,138	6%	27	1,397	3,200	2,600
2004	5,411	31	24	1,526	4,200	3,500
2005	4,340	-20	14	1,035	3,400	2,800
2006	7,625	76	6	302	5,900	4,900
2007	6,603	-13	16	1,174	5,100	4,200
2008	7,435	13	12	864	5,700	4,700
2009	5,625	-24	14	1,024	4,300	3,600
2010	6,158	9	32	4,113	4,800	3,900
2011	6,482	5	27	1,943	5,000	4,100
2012	7,826	21	33	2,100	6,000	5,000
2013	7,544	-4	23	1,348	5,800	4,800
2014	9,903	31	14	876	7,700	6,300
2015	9,272	-6	28	1,700	7,200	5,900

While the appraised land value approved by the Department for purposes of the grant appears to be reflective of Dane County agricultural land sales data, it may be more difficult to establish an appropriate value for the improvements on the property. As noted, the DNR appraisal reviewer argued that the value of the improvements was more accurately estimated through a market approach (the \$80,000 value) than a cost approach (the \$61,500 value). However, the reviewer also noted that the improvements on the subject property are older, and some of them could be considered obsolete. Given the significant age of the buildings, the Committee could consider approving a grant award based on the lower improvement value (\$61,500), or perhaps an intermediate value (\$70,800) could be considered.

Some might argue that because the Department already holds a conservation easement on the property, providing the grant is unnecessary to protect the land from future development and the request should be denied (Alternative 3). Or, if the grant were to be provided, as the Department utilized stewardship program funds for the purchase of the conservation easement on the property, some might argue that a reduced amount of stewardship program funds should be utilized for the grant (Alternatives 1B through 2B). Others might argue that, while the conservation easement protects the property from future development, it does not allow public access or recreational conservation management. As noted, if the grant were approved, it would increase public access to the adjacent Hook Lake Bog/Grass Lake Wildlife Area, and DNR indicates that pheasant hunting would be available on the property, as the Wildlife Area is stocked with pheasants. Current parking at the Wildlife Area is insufficient to meet demand during pheasant

season. As noted, if the parcel were acquired, an additional parking lot would likely be added.

TABLE 4

Alternatives

<u>Alternative</u>	<u>Land Value (per acre)</u>	<u>Improvement Value</u>	<u>Additional Eligible Costs</u>	<u>Total Eligible Costs</u>	<u>Grant Award</u>
1.A. DNR Request	\$605,000 (\$5,900 per acre)	\$80,000	\$7,100	\$692,100	\$346,100
1.B. DNR Requested Land Value + Lower Improvement Value	\$605,000 (\$5,900 per acre)	61,500	7,100	673,600	336,800
1.C. DNR Requested Land Value + Intermediate Improvement Value	\$605,000 (\$5,900 per acre)	70,800	7,100	682,900	341,500
2.A. Lower Land Value + Lower Improvement Value	\$574,000 (\$5,600 per acre)	61,500	7,100	642,600	321,300
2.B. Lower Land Value + Intermediate Improvement Value	\$574,000 (\$5,600 per acre)	70,800	7,100	651,900	326,000

When the request was submitted in June, 2016, Department officials indicated that they planned to utilize fiscal year 2015-16 funds for the grant. However, since the 2015-16 fiscal year has ended and the state's books have closed (the state's annual fiscal report is issued in October each year), DNR would be required to utilize its 2016-17 stewardship bonding allocation at this time. The \$346,100 set-aside from the NCO allocation for this grant in 2015-16 is instead available for county forest grants in 2016-17, as DNR may not formally encumber, or obligate, stewardship funds until the project is approved by Joint Finance. Approximately \$6.9 million is available for 2016-17 county forest grants, consisting of the \$5 million annual base allocation, plus \$1.9 million carried over from unallocated 2015-16 NCO grants.

ALTERNATIVES

1.A. Approve the Department's request to provide a stewardship grant of up to \$346,100 in 2016-17 land acquisition NCO funds to the Natural Heritage Land Trust for the purchase of 102.5 acres in the Town of Dunn, Dane County.

1.B. Approve the Department's request, but specify that DNR may obligate no more than \$336,800 in 2016-17 funds from the stewardship program for the grant (based on the DNR requested land value and the lower appraised improvement value).

1.C. Approve the Department's request, but specify that DNR may obligate no more than \$341,500 in 2016-17 funds from the stewardship program for the grant (based on the DNR requested land value and intermediate improvement value).

2.A. Approve the Department's request, but specify that DNR may obligate no more than \$321,300 in 2016-17 funds from the stewardship program for the grant (based on the lower appraised land value and lower appraised improvement value).

2.B. Approve the Department's request, but specify that DNR may obligate no more than \$326,000 in 2016-17 funds from the stewardship program for the grant (based on the lower appraised land value and intermediate improvement value).

3. Deny the request.

Prepared by: Erin Probst