

AN INVESTMENT LETTER FOR MINNESOTA PHILANTHROPISTS

Sunday, July 15, 2007

The formation of “Community Land Trusts” continues to gain momentum both nationally and in Minnesota as a vehicle to make home ownership affordable to low and moderate income families. In this issue we will review the progress made to date by “The City of Lakes Community Land Trust” which serves Minneapolis residents. CLCLT evolved from a collaboration of Powderhorn Residents Group, Seward Redesign, Powderhorn Park Neighborhood Association and Lyndale Neighborhood Development Corporation that began in late 2001. This study will develop a methodology for accessing the productivity and return on investment of CLCLT dollar investments during their first twenty six months of active home sales for the period ending December 31, 2006.

The concept of a “Community Land Trust” involves freezing to the extent possible increases in the cost of home ownership over a very long period of time. Based on twenty six months of experience and the experience of other land trusts, dollars invested by CLCLT made in September of 2004 could provide an average annual return to CLCLT after recovery of their original investment of 7.3% over a twenty year time frame and 10.6% over a thirty year time frame. These are average returns which with increasing frequency of resale could range higher for these same time periods. The best measure of the productivity of dollars invested by CLCLT is the fact that between 150 to 300 new home owners would have been created over these respective time periods. The community investors in CLCLT are a combination of private and public organizations.

WHAT’S THE PROBLEM?

The gap continues to widen between the cost of housing and wages earned by the average household. Over 171,000 low income metropolitan area households are currently paying more than they can afford (30% of their income) for housing. Many of these are renters who are not building equity through home ownership.

An estimated 22,000 households will lack affordable housing in the Twin Cities Metropolitan Area by 2010. While 35% of Minneapolis residents are people of color only 15% are “Communities of Color” homeowners.

When families pay more than 30% of their income for housing the family is stressed financially and moves frequently seeking affordable rent which in turn impacts school performance, job performance, child care costs and transportation logistics. Substandard housing impacts family health, results in overcrowding and often increases the chances of criminal justice system involvement.

HOW DOES THE “CLCLT” HELP?

CLCLT provides permanently affordable housing for low to moderate income home buyers by owning the land but selling the home on the land to an income qualified buyer. The home owner leases the land through a renewable ground lease. When the homeowner sells the house their equity plus 25% of the appreciated value returns to the homeowner while 75% of the appreciated value remains with CLCLT to make the same home affordable to future buyers.

A typical CLCLT family has 2.6 members, 30% headed by a single mom, are first time buyers, have an average income of \$31,065 and are 48% people of color.

CLCLT homes on average have had a market value of \$178,766 and sell for \$127,241 requiring a subsidy or non-owner investment of \$51,525. The sources for the non-owner investment include: Minnesota Housing Finance Agency, The Family Housing Fund, Hennepin County, The City of Minneapolis and eight others including neighborhood groups and family/corporate foundations.

From September 2004 to December 2006 50 homes were sold to qualified buyers. In 2007 CLCLT began to see some of the first re-sales of their homes permitting original owners to move on to other now affordable market rate homes and freeing up opportunity for new first time home owners. National experience shows that CLCLT type homes resell between five and ten years after purchase.

CASE STUDY

One of the first CLCLT homebuyers was a single mother with two young children who had been pursuing home ownership for numerous years. Living in the Lyndale neighborhood of South Minneapolis and working as a proof writer she had become discouraged over the cost of housing and/or the amount of rehab required on more affordable homeownership in South Minneapolis. At that time the neighborhood association had agreed to grant \$90,000 of their housing funding to CLCLT and the prospective homebuyer learned about the opportunity to purchase a home of her choice through a neighborhood newspaper.

She was pre-approved for a \$120,000 loan and was qualified for \$65,000 in affordability assistance from CLCLT. When she came up as the next buyer on the wait list she and her realtor found a home to purchase up to \$185,000. CLCLT ordered an inspection, the home passed and they signed a purchase agreement. Prior to the closing in the summer of 2006 she met with an attorney, paid for by CLCLT, who reviewed all the documents. She had purchased a home for \$120,000 and was entitled to her equity invested plus 25% of the appreciated value if she later decides to sell the home. Her two children attend the same neighborhood school as before and she is civically involved in the community.

WHO BENEFITS?

The purchasing family frees up an affordable rental unit and now benefits from becoming home owners and establishing equity in their home. In addition the family can now anticipate a growing equity base that enhances their credit rating and permits eventual ownership of a market rate home.

Minnesota taxpayers benefit from the stability home ownership brings to the family which in turn keeps the children in the same school longer, permits the home owner to focus on their employment career more effectively and reduces the social costs related to families constantly on the move seeking affordable, safe and often subsidized rental housing.

WHAT'S THE RETURN ON INVESTMENT?

Returns have been calculated based on the \$2,577,400 original investment by CLCLT (philanthropic investors and neighborhood organizations). The gain in appreciated value of the 50 homes initially purchased was about \$120,000 per year for the first 26 months of CLCLT's active operations. This same dollar amount is used for the five and ten year increments used in this study. Since this gain amounted to 4.65% annually this same rate has been used in discounting future values over the 20 and 30 year time periods. The results vary widely over the years depending upon the frequency of resale of homes purchased. Condominiums tend to resell much faster than free standing single homes. It is not clear what the pattern will be in future years. We have assumed the proportion will be about even in this analysis and that condominiums resell every five years and single homes every ten years. These time frames are thought to be conservative.

The average value of homes purchased was \$179,544 and the price paid by homeowners \$127,966 requiring an investment of \$51,548 by CLCLT. Each home appreciated \$6,822 during the first 26 months or an annual rate of about \$3,146. Since CLCLT retains 75% of this appreciation their gain amounts to about \$2,400 per home or \$120,000 gain per year for the 50 homes. Real estate taxes are estimated at 1% of market value. Experts vary on the economic value of moving a family from market rate rental to homeownership status. There is agreement that the equity build up from homeownership increases family income and net worth over time. This benefit to the economy is estimated to be \$1,000 per family annually over time for purposes of this study.

We have assumed when a home resells that the benefit to MCLCT (75%) from helping the previous owner continues as well as the new increment added by the new owner. In other words each new owner of a MCLCT home represents a homeowner that otherwise would not have existed so there is a cumulative effect by each resale over time. Where we assume a ten year turnover for single homes 150 new home owners are created over 30 years. Where we assume a five year turnover for condominiums 300 new home owners could be created over a thirty year time frame. The program is designed for long term impact and therefore long time periods to calculate productivity and return on investment are appropriate.

CALCULATING THE RETURN ON INVESTMENT

Facts & Assumptions

Initial Investment by CLCLT: \$2,577,400

Number of Homes (50% Condominiums & 50% Single Homes): 50

Average annual gain in value: \$2,400

CLCLT Share of Annual Appreciation: 75%

Turnover Rate for Condominiums: 5 Years

Turnover Rate for Single Homes: 10 Years

Discount Rate for Present Value Analysis: 4.65%

		50		
<u>Calculating Returns for Condominiums</u>	<u>Unit</u>	<u>Units</u>	<u>20Yrs.</u>	<u>30Yrs.</u>
CLCLT 75% Equity Annual Gain	\$ 2,400	\$120,000	\$6,000,000	\$12,600,000
Real Estate Taxes Paid	2,000	100,000	5,000,000	10,500,000
Homeowner Economic Contribution	<u>1,000</u>	<u>50,000</u>	<u>2,500,000</u>	<u>4,000,000</u>
Total	\$5,400	\$270,000	\$13,500,000	\$27,100,000
Average Annual return to CLCLT			12.0%	15.0%
New Homeowners			200	300
<u>Calculating Returns for Single Homes</u>	<u>Unit</u>	<u>Units</u>	<u>20Yrs</u>	<u>30 Yrs.</u>
CLCLT 75% Equity Annual Gain	\$2,400	\$120,000	\$3,600,000	\$7,200,000
Real Estate Taxes Paid	2,000	100,000	3,000,000	6,000,000
Homeowner Economic Contribution	<u>1,000</u>	<u>50,000</u>	<u>1,500,000</u>	<u>3,000,000</u>
Total	\$5,400	\$270,000	\$8,100,000	\$16,200,000
Average Annual Return to CLCLT			2.6%	6.3%
New Homeowners			100	150
<u>Blended Return</u>			7.3%	10.6%

The purpose of “An Investment letter for Minnesota Philanthropists” is to demonstrate how return on investment calculations can be applied to the public and private investments made in our non-profit organizations. An accounting system does not exist in the non-profit world comparable to that in the for-profit world and therefore assumptions must be made in the absence of definitive longitudinal studies. The assumptions made in this study are thought to be conservative.

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