

STATE OF COLORADO

Colorado Water Conservation Board Department of Natural Resources

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TO: Colorado Water Conservation Board Members

FROM: Kirk Russell, P.E., Chief
Finance Section

DATE: May 4, 2012

SUBJECT: **Agenda Item 26a, May 15-16, 2012 Board Meeting**
Finance Section – Changes to Existing Loans
Tom Hill – McElroy Dam Rehabilitation Project

John W. Hickenlooper
Governor

Mike King
DNR Executive Director

Jennifer L. Gimbel
CWCB Director

Introduction

In November 2006 the CWCB approved a 30-year loan to Tom Hill, a rancher in Grand County, for \$862,540 from the Severance Tax Trust Fund Perpetual Base Account. The loan was used to breach and rehabilitate the McElroy Reservoir Dam which provides irrigation water to the Hill's Gore Pass Ranch. The loan was secured by land and water rights associated with the Gore Pass Ranch. The original Board approval has needed several modifications. A description of important events over the past five years is provided in the memo along with a table of an Approximate Timeline.

In April the Hills made a partial payment of \$40,000 towards the loan. Staff will ask the Board to consider a restructuring of the loan to improve the Hills ability to repay the loan until the Gore Pass Ranch is sold.

Staff Recommendation

Staff recommends the Board approve a loan amendment to restructure Loan Contract No. C150233 from its current 10 year term to a term of 27 years at the agricultural rate of 2.50% per annum for the remaining principal balance of \$715,942.01. Security for the loan shall not change and is in compliance with CWCB Financial Policy #5.

Background

The McElroy Reservoir (Reservoir) has been owned and operated by Tom and Linda Hill for the last 30 years. The Reservoir is located on State Land Board property and is authorized by a 10-year renewable lease terminating June 2016. The Hills use the water stored in the Reservoir to irrigate hay on the 2,588 acre Gore Pass Ranch. The Ranch is located upstream of Wolford Mountain Reservoir and diverts water from McElroy Creek.

In June, 2006, the Dam outlet works failed and the embankment material of the dam began migrating into the outlet pipe causing it to become unusable. With no way to release stored water, the Hills received a breach order from the Dam Safety Branch of the State Engineer's Office (SEO). The Hills hired URS Consultants to file a breach application with the SEO and hired Pryor Excavating to repair the dam. Rehabilitation of the dam began in the spring of 2007 and was completed in 2008.

A CWCB loan was approved in November 2006. Staff identified in the original board memo that the Hills were operating the Ranch at a loss, the Ranch was for sale, and that the Hills needed 100% funding for the project due to their hardship status. A recent review of the Hills tax returns indicate that the Gore Pass Ranch broke even in 2010 and had a positive revenue of approximately \$70,000 from hay and cattle production in 2011.

In May of 2008, the Hills notified the CWCB of their intention to sell a conservation easement on the Ranch to the Department of Wildlife (DOW), which would preserve all of the land and water rights associated with the Ranch for agricultural use. DOW informed the CWCB that the Ranch was chosen for a conservation easement because it is a valuable wildlife habitat and is a source of water for a downstream fishery. The easement sale was contingent upon the CWCB subordinating its interest in the Ranch to the DOW's easement. The value of the easement was \$3,750,000, leaving the Ranch with an appraised value after the easement of \$2,625,000 without improvements. The Board approved an amendment to the loan contract which included the subordination to the DOW conservation easement on Gore Pass Ranch and received a first position lien on all of the Gore Pass Ranch and added an undivided 100% interest in the Hills 40 acre Olathe property. In addition, the contract was changed from a 30-year loan to a 10-year loan with the first annual payment of \$96,023.58 due on May 1, 2010. The Hills had accumulated a significant amount of debt including a loan with Grand Mountain Bank (Bank) for approximately \$2,170,000. The sale of the conservation easement allowed the Hills to pay off all of their debt and free their property of liens.

The intent of this action by the staff/Board in 2008 was to increase the total value of hard collateral as security for the loan in a deliberate attempt to increase the pressure on the Hills to sell the Gore Pass Ranch and pay off the CWCB loan. Unfortunately, the real estate market remains difficult for the sale of this property.

In May 2010, the Board approved a one year principal payment deferment and the interest only payment was received in June 2010. In May 2011, the Hills made a full annual payment of \$96,023.58.

Discussion

This loan was problematic in the beginning since the Hills were in a land rich/cash poor situation when the SEO Breach Order was issued. The CWCB was in a position to help by financing the repairs with an understanding that the ranching revenue was marginal; however the loan could be secured by a significant amount of hard collateral and the Hills intent to sell the Ranch. Staff feels the strength of this collateral is still strong and will protect the Loan Program funds due to the value of the collateral in the event of a default.

Staff's recommendation is a change to the loan terms to better fit the Hills financial capacity to make the annual payment and remains within the CWCB Financial Policies. The loan term will return to its original 30-year term payoff date of May 1, 2039 (27 years out) and change the interest rate to the Agricultural interest rate for a 30-year loan in 2006 of 2.50% The new annual loan payment shall be approximately \$36,800.

Staff also requests that the Board establish a very clear message regarding its intent to act vigorously to engage Central Collection Services upon any future delinquent annual loan payments. The Board's Financial Policy #3 – Loan Delinquency, Loan Restructuring, and Collections states "If the delinquency continues, and is at least one year past due, staff will recommend that the Board Refer the bad debt to Central Collections and/or the Attorney General's Office to take appropriate legal action against the Project Sponsor".

Collateral: The security for the loan shall not be changed. Currently the loan is secured by:

1. Undivided 100% interest in 213 acre parcel in Grand County (\$1.1M appraised value)
2. "water rights owned in Grand County" (16 separate water rights total)
3. Undivided 100% interest in "remainder of Gore Pass Ranch" (\$2.6M value, current market price estimated at \$2.75M)
4. Undivided 100% interest in the Olathe property (40 acre +/-) (\$1.5M purchase price)

Approximate Timeline

Date	Event	Notes
2006		
Spring	Hills purchase Olathe property for \$1.5M	Close to Montrose for medical reasons
June	SEO dam breach order	URS hired
Nov	CWCB approves loan	Loan amount is \$862,540
2007		
Jan	Loan Contract C150233 Executed	Loan security is 1 st position on 213 ac. portion of Ranch and 2 nd position on Bank financed portion
Summer	Gore Pass Ranch for sale at \$6.4M	
2008		
Spring	Construction work complete	Final disbursed amount \$820,728.63
May	CWCB approves DOW subordination	
May	Contract Amendment #2 processed	Increase in collateral, loan terms changed
June	\$3.75M contract for conservation easement	Ranch value reduced to \$2.6M
Summer	Hills pay off Bank loan w/proceeds	Ranch and Olathe property free of liens
2009		
May	Substantial Completion	Hills pay \$27,441 towards const. interest const.
Summer	Asking price of Ranch is reduced to \$3.5M	
2010		
May	CWCB approves principal deferral	Payment for interest only received
June	Contract Amendment #2 processed	Extends loan from 10 to 11 years
Summer	Asking price of Ranch reduced to \$3.1M	
2011		
May	Loan payment received	Full payment received (\$96,023.58)
Summer	Asking price of Ranch reduced to \$2.75M	
2012		
Spring	Hills indicate an increase in buyer interest	
May	Partial payment received	Hills send \$40,000 towards loan

cc: Tom Hill, Owner Gore Pass Ranch
 Susan Schneider, AGO
 Peter Johnson, AGO