FUNCTIONAL REPLACEMENT

The transportation needs for the public must be balanced with the other peace, safety, and well-being needs for the public for whom Indiana’s government is instituted. When the Department of Transportation has determined that a publically owned property, essential to the peace, safety, and well-being needs of the public, must be acquired for a transportation project, fair market valuation is not the appropriate method for valuing such property, but rather, a replacement property must be provided to the public to ensure that the needs of the public does not suffer as a result of the highway project. To this end, the Department will functionally replace publicly owned properties that provide needed public services. Examples may include schools, police and fire stations, parks, recreational areas, municipal garages or maintenance facilities, libraries and city or county government buildings and other public-owned areas. For parks and recreation areas, Sec. 4(f) provisions of the US Department of Transportation (DOT) Act of 1966 may apply. The real property cannot be owned by a utility or railroad.

The functional replacement concept permits federal participation in costs of acquiring an adequate replacement site if one is required and the construction costs of the replacement improvements that duplicate the function of the acquired improvement. This concept requires that the facility must be needed by the public, must be actually replaced and the costs to presently replace the facility or cure damage to it be actually incurred by the public agency. Indiana Code Section 8-23-17-30 empowers the Indiana Department of Transportation (INDOT) to take actions as necessary in order to put into effect policies that comply with federal law and regulations, and pursuant to this, INDOT has the authority to create and implement provisions that assist INDOT with consistent application and administration of functional replacement benefits. The functional replacement concept may also be applied to state-funded projects.

The intention of functional replacement is to consider providing additional assistance when it is recognized that the Fair Market Value compensation for the acquisition of the public facility may be insufficient to restore it to the level needed to provide the same services which were being provided at the subject site. Costs of increases in capacity and other betterments or enhancements are not eligible for federal or state participation except where necessary to replace the facility’s utility, unless required by existing codes, laws or zoning regulations, or related to reasonable prevailing standards for the facility being replaced. Because of the added review, oversight and approval associated with the functional replacement process, the importance of early coordination cannot be over emphasized. If you anticipate functional replacement will apply to a project, contact the Real Estate Division as soon as possible to discuss specifics. The agency owning the public facility, at its option, may choose to accept conventional Fair Market Value compensation provided through INDOT’s standard acquisition process, in lieu of functional replacement.

When the department determines that functional replacement of real property in public ownership and public use may be necessary and in the public interest, state funds may participate in the payment to the public agency for:

• Functional replacement costs of improvements required to be replaced exclusive of increases in capacity or betterments; and
• Market value of land owned by the public agency when that public agency has land upon which to relocate facility; or

• Reasonable cost of acquiring a comparable, substitute site where lands owned by the public agency are not available for use in relocating the facility.

For federal participation in functional replacement, FHWA must provide prior approve for the acquisition. The provisions of 23 CFR Section 710.509 should be reviewed to assure compliance with federal regulations pertaining to functional replacement of real property in public ownership. The acquiring agency will prepare an early costs estimate of functional replacement to include all eligible costs.

Prior to the initiation of real estate services, the Project Manager should identify any parcel acquisitions that may meet the definition of functional replacement. If such a parcel is identified, the following approvals and steps must be followed:

1. The INDOT or LPA Project Manager must contact INDOT’s central office acquisition section manager regarding the possibility of functional replacement when publicly owned real property, including land/or facilities, is to be acquired for a federal aid or a state funded project.

2. INDOT and FHWA, if applicable, will agree on scope of required oversight prior to initiation of functional replacement. INDOT’s Real Estate Division Director will seek and provide all necessary approvals prior to initiation of functional replacement.

3. The acquiring agency should meet early in process with the public agency and inform the agency in writing of their right to just compensation based on appraisal of fair market value and of the option to choose either just compensation or functional replacement. Amount of functional replacement shall be limited to difference between approved offering price based on an appraisal of market value and actual cost to replace facility with an equivalent facility as defined in 23 CFR 710.509 provided below in this chapter.

4. Parcels approved for functional replacement, shall have a mutually acceptable course of action developed with owner via a Memorandum of Understanding (MOU) agreement. Action may include discussion on functional equivalency of facility and need to obtain bid estimates for necessary construction.

5. INDOT’s Real Estate Division management will have responsibility to review and approve final costs estimates for state funded projects. If federal funds are involved, estimates must be processed through INDOT’s Real Estate Division who will obtain necessary review and approval from FHWA.

6. Functional replacement funds over the approved acquisition amount will be processed through the established MOU agreement.
7. A portion of replacement funds will be held until construction is complete to ensure replacement actually takes place and costs have actually been incurred. The terms of the distribution of the function replacement funds will be outlined within the MOU agreement.

8. Total cost of functional replacement will be based on a written estimate of construction (approved by INDOT) and either market value or reasonable, actual cost of acquiring a comparable substitute site.

9. All other Real Estate service functions to include but not limited to; appraising, buying, relocation, finance, and property management services will be provided as needed and established within the INDOT Real Estate Division manual.

23 CFR 710.509 Functional replacement of real property in public ownership.

(a) General. When publicly owned real property, including land and/or facilities, is to be acquired for a project receiving grant funds under title 23, in lieu of paying the fair market value for the real property, the acquiring agency may provide compensation by functionally replacing the publicly owned real property with another facility that will provide equivalent utility.

(b) Federal participation. Federal-aid funds may participate in functional replacement costs only if the following conditions are met:

1. Functional replacement is permitted under State law and the acquiring agency elects to provide it;
2. The property in question is in public ownership and use;
3. The replacement facility will be in public ownership and will continue the public use function of the acquired facility;
4. The acquiring agency has informed, in writing, the public entity owning the property of its right to an estimate of just compensation based on an appraisal of fair market value and of the option to choose either just compensation or functional replacement;
5. The FHWA concurs in the acquiring agency determination that functional replacement is in the public interest; and
6. The real property is not owned by a utility or railroad.

(c) Federal land transfers. Use of this section for functional replacement of real property in Federal ownership shall be in accordance with Federal land transfer provisions in subpart F of this part.

(d) Limits upon participation. Federal-aid participation in the costs of functional replacement is limited to costs that are actually incurred in the replacement of the acquired land and/or facility and are -

1. Costs for facilities that do not represent increases in capacity or betterments, except for those necessary to replace utilities, to meet legal, regulatory, or similar requirements, or to meet reasonable prevailing standards; and
2. Costs for land to provide a site for the replacement facility.
(e) Procedures. When a grantee determines that payments providing for functional replacement of public facilities are allowable under State law, the grantee will incorporate within its approved ROW manual, or approved RAMP, full procedures covering review and oversight that will be applied to such cases.