

TAX INCREMENT FINANCING

Program Evaluation Division
Office of the Legislative Auditor
State of Minnesota

Program Evaluation Division

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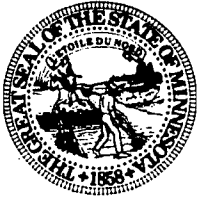


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January 1986



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STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

January 31, 1986

Senator Randolph W. Peterson, Chairman
Legislative Audit Commission

Dear Senator Peterson:

In June 1985, the Legislative Audit Commission directed the Program Evaluation Division to conduct a study of tax increment financing in Minnesota. This report describes tax increment financing and examines its use by cities throughout the state as a financing tool for a variety of local projects. The report shows that some cities have used the financing tool in ways not originally intended by the Legislature. It also recommends ways that the Legislature can better target the program in the future.

We appreciate the assistance given to us by numerous individuals at the Department of Energy and Economic Development, House Research, the law firm of Holmes and Graven, the Minnesota League of Cities, and the 44 cities we visited during the course of this study.

The study was conducted by Joel Alter and John Yunker (project manager).

Sincerely yours,

James R. Nobles
Legislative Auditor

Roger A. Brooks
Deputy Legislative Auditor
for Program Evaluation

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EXECUTIVE SUMMARY

This report examines the use of tax increment financing (TIF) in Minnesota. Tax increment financing is a tool used by cities to finance certain types of real estate development costs. The primary purposes of TIF are to attract private investment that will: 1) redevelop blighted areas, 2) provide housing for low and moderate income individuals and families, or 3) result in increased employment opportunities and tax base.

Over the last ten years, tax increment financing has become an increasingly popular development tool. In 1974, only four cities had development projects generating tax increments. By 1980, the number of cities grew to 81. Today, the number of cities using TIF is estimated to be over 210.

The growing popularity of TIF is due in part to the decline in federal resources available to cities for urban renewal and other development purposes. In addition, cities in Minnesota like others across the nation have become more interested and active in attracting private development over the last five years.

Despite the increasing use of tax increment financing, there is relatively little statewide information available on how Minnesota cities have used TIF. For this reason, the Legislative Audit Commission directed the Program Evaluation Division to conduct a study of tax increment financing. During our study, we visited 44 Minnesota cities and gathered information on how tax increment financing was used in each city. This report summarizes our findings and raises a number of policy issues for legislative consideration. An appendix to the report describes the use of TIF in nearly 200 tax increment districts.

A. BACKGROUND

Tax increment financing enables a city to use the additional property taxes generated by a new development to finance certain development expenses. Some common expenses financed with TIF include land acquisition and write-down, demolition, and construction of public infrastructure.

Most cities finance these costs by issuing tax-exempt bonds, and the tax increments from the resulting development are used to make annual principal and interest payments on the bonds. While TIF does not change the amount of taxes paid by a developer, it does change the distribution of these taxes. Instead of being shared by the city, county, and school district, tax increments typically go to the city to pay development costs. In theory, the various taxing jurisdictions will later benefit from TIF because it induces new developments that would not have occurred without this financing tool.

The Minnesota Tax Increment Financing Act of 1979 must be used to establish a tax increment district and its financing plan. According to the act, districts may be one of three types: (1) a *redevelopment* district, which is designed to induce development on blighted land; (2) a *housing* district, which is intended to encourage housing development for low and moderate income individuals and families; or (3) an *economic development* district, designed to increase cities' tax base and employment, as well as to discourage Minnesota businesses from moving to other states. Districts established prior to August 1, 1979 are a fourth type of district. These districts are not subject to the most of the 1979 law's provisions.

The 1979 law placed additional restrictions on new tax increment districts and modifications of existing districts. For example, the Legislature established blight criteria for cities to use when establishing redevelopment districts. Also, the Legislature placed restrictions on "excess increments," or those tax increments in excess of the amount required to finance project costs in a district's financing plan.

One of the important components of the 1979 law was the distinction between a "tax increment district" and its "project area." In general, a tax increment district consists of those parcels which generate tax increment revenue. The district's project area consists of those parcels on which tax increments may be spent. Prior to 1982, cities could not spend tax increments outside of the district in which those increments were generated. However, 1982 amendments loosened this restriction. The changes permitted cities to spend increments anywhere in the project area, even outside the tax increment district.

The creation of a tax increment district and the expenditure of tax increments are city actions. The county and school district are given the opportunity to comment on TIF plans prior to implementation. However, it appears that the state finances more TIF costs than these other taxing jurisdictions. This occurs indirectly, primarily through increases in state education aids. A forthcoming report by the Minnesota House Research Department estimates total state costs for 1985 to be more than \$22 million.

B. ISSUES

Tax increment financing has been used productively by many cities in Minnesota to induce commercial and retail development of blighted areas

and to help stimulate the construction of housing for low and moderate income persons. In addition, some cities have used TIF to promote the expansion of manufacturing businesses. However, not all uses of tax increment financing have been successful in reducing blight, stimulating needed housing construction, or increasing employment in the state. At times, TIF has been used in ways that are inconsistent with the basic intent behind TIF. Among the major problems with tax increment financing are:

- In some instances, cities have established tax increment districts that intentionally capture taxes from development that is already occurring rather than induce new development. This practice prevents other taxing jurisdictions from collecting taxes they would otherwise receive.
- The "but for" test, which many view as sufficient evidence of the need for a tax increment district, is interpreted by cities in many different ways. The test does not ensure that the public benefits of a project exceed the public costs.
- The statutory restrictions on the types of expenditures that can be financed with tax increments do not prevent a city from using tax increments to pay for general public improvements that are normally financed by special assessments or a city's own funds.
- Increasingly, cities are pooling tax increments among districts or establishing large project areas in which tax increments can be spent. These practices enable a city to spend excess tax increments from an existing district rather than decertifying the district. This weakens the statutory restrictions on the use of excess increments that apply to districts established after August 1, 1979. Furthermore, pooling and the creation of large project areas may encourage cities with pre-1979 districts to use tax increments for new expenditures rather than to retire the districts before August 1, 2009.
- Existing statutes do not require that the tax increments generated within a redevelopment district must be used to correct the blighted conditions that permit the district to be established. As a result, some cities have established redevelopment districts that have done little or nothing to improve the blighted conditions cited as reasons for establishing the districts. Some cities: 1) have established a redevelopment district on the basis of blighted conditions existing on certain parcels within the city, 2) are generating tax increments from other parcels where private development is occurring anyway, and 3) are spending the increments on projects unrelated to the blighted conditions. The permitted use of noncontiguous districts, the lack of an effective "but for" clause, and the fact that not all parcels in a district must be blighted permit tax increment financing to be used in these ways.

- The existing blight criteria that a redevelopment district must meet have been generously interpreted by some cities. As a result, the criteria have not provided a good mechanism for the state to target public subsidies to those areas most in need of redevelopment.
- Several cities have established housing districts to capture tax increments from a housing project being undertaken without assistance from tax increment financing and have not used the increments to induce the construction of low/moderate income housing.
- Some compliance problems exist because there is little state oversight of tax increment financing and because it is not clear who has the responsibility to ensure that cities and counties comply with key provisions of the statutes relating to tax increment financing.

In addition, there is the question of whether tax increment financing results in an excess public investment in development activities. To the extent that cities use tax increment financing to induce retail and commercial development, TIF may only succeed in shifting where that development occurs within the state. This is particularly true in the Twin Cities metropolitan area. A subsidized development that brings more jobs and tax base to one city may ultimately result in fewer jobs and decreased tax base elsewhere in the metropolitan area. Because the direct effects of tax increment financing (more jobs and tax base in the city using TIF) are easier to see and measure than its indirect effects (fewer jobs and decreased tax base elsewhere in the area), TIF may appear to be creating jobs and increasing the state's tax base when it is not.

There is reason to be concerned about this problem. Cities have used redevelopment districts primarily, though not exclusively, to induce retail and commercial development.

- To the extent that TIF's primary effect is simply to shift the location of jobs and tax base, it is important to ask whether TIF targets the redevelopment of those areas that need it the most.

The lack of adequate criteria defining blight and the lack of a requirement that tax increments generated within redevelopment districts be used to address blighted conditions are impediments to a reasonable targeting of the use of tax increment financing. It is also worth considering whether local incentives are an impediment to effective targeting. For example, small suburbs may have a greater ability than large central cities to shift the costs of public redevelopment activity to taxpayers outside the municipality. This may be inconsistent with the goal of encouraging TIF use in those areas most in need of redevelopment.

- The purpose of economic development districts can also be called into question.

According to law, a municipality can create an economic development district consisting of any parcel or parcels of property as long as the district meets one of three criteria: 1) it will discourage commerce, industry or manufacturing from moving to another state, or 2) it will increase employment in the municipality, or 3) it will preserve or enhance the municipality's tax base. The majority of the economic development districts we examined probably could not have qualified under the first criterion. Most of the districts involved retail, commercial, and other development that would qualify under the second and third criteria. The effect of using tax increment financing for these latter types of development may only be to determine where development occurs, not to cause any significant increase in jobs or tax base within the state. As a result, the use of economic development districts involving retail and commercial development that does not create jobs for the state and does not take place in blighted areas can be questioned. While there clearly is a role for TIF in attracting new businesses to Minnesota and keeping existing businesses in the state, it is worth asking whether the state should encourage (and financially support) districts that do not result in state-wide benefits.

C. LEGISLATIVE OPTIONS

There are two approaches that the Legislature could consider in addressing problems with the use of tax increment financing in Minnesota. The first approach would be to strengthen the Minnesota Tax Increment Financing Act so that current problems would be less likely to occur in the future. This approach would primarily consist of placing additional restrictions on the use of tax increment financing by municipalities. The second approach could also include statutory restrictions, but would focus on more fundamental changes in the development financing process. For example, the Legislature might consider whether the process for approval of the use of tax increment financing should be left to the discretion of city officials. Also, the Legislature could consider whether, or under what conditions, state aid should continue to pay for a portion of the costs of tax increment financing.

In considering various options, the Legislature should also take into account the impact that federal tax reform may have on tax increment financing. The tax reform bill recently passed by the United States House of Representatives, if enacted into law, would greatly restrict the use of tax-exempt bonds for tax increment financing and other development purposes. Such restrictions would increase the public costs of TIF by causing municipalities to issue taxable, rather than tax-exempt, bonds to finance new tax increment districts. Municipalities might also be more likely to fund new development projects by: 1) capturing tax increments from new development that is occurring without public assistance, or 2) using excess increments from existing districts.

1. CHANGES TO MINNESOTA'S TAX INCREMENT FINANCING ACT

State law should discourage cities from including property in tax increment districts that is developing without assistance from TIF. However, existing law permits cities to capture the increased assessed value from any new private development or improvements for which a building permit was issued within the three-month period immediately preceding the approval of a tax increment financing plan. This provision has encouraged some cities to include properties that are developing without public assistance in tax increment districts. Some cities have even established districts that consist primarily or exclusively of such properties, rather than properties whose development would be induced by tax increment financing. To correct this problem, we recommend that:

- The Legislature should eliminate the statutory provision that permits a tax increment district to capture the increased assessed value from development for which building permits were issued during the three months prior to approval of the district.

While eliminating the three-month window would address part of the problem, it would not prevent a city from including within a tax increment district parcels of land that are expected to be developed or redeveloped privately within the near future. City officials often are aware of sites where development is likely to take place in the near future even though building permits have not been issued or applied for. This problem may be as significant as the three-month window but is not as easily remedied. We recommend that:

- The Legislature should consider addressing this problem indirectly by increasing the percentage of parcels that must meet the blight definitions in order for a district to qualify as a redevelopment district.

Increasing the percentage of blighted parcels could have the desired effect by limiting the extent to which a city can include non-blighted parcels in a redevelopment district. Because noncontiguous districts are permitted, city officials sometimes look for non-blighted parcels that are likely to develop privately. Including such parcels in a district enables the city to use the taxes generated by private development for expenditures within the district and its associated project area. Currently, a city is able to establish a redevelopment district if as few as 35 percent of a district's parcels (50 percent of those with buildings) are found by the city to be substandard or needing renovation or clearance. Increasing the percentage of blighted parcels might limit the extent to which cities could intentionally capture tax increments from non-blighted parcels. Such a change would, however, only affect redevelopment districts and not economic development or housing districts.

Another option would be to clarify the intent of the "but for" clause. For example:

- The Legislature could consider requiring municipalities to make a "but for" finding for each parcel in a tax increment district.

Those parcels that are developing privately and do not need assistance from tax increment financing would not be permitted to be in the tax increment district. Of course, the effectiveness of such legislation might rest on the willingness of cities to implement its intent and, if implemented rigidly, it might affect the ability of some municipalities to undertake more risky, yet worthwhile, projects. Nevertheless, this option is worth considering. The existing "but for" clause has little or no significant effect on the properties placed in a tax increment district or the types of projects undertaken.

Another major concern that needs to be addressed is the lack of adequate targeting of redevelopment districts to blighted areas. We recommend that:

- The Legislature should examine ways to tighten the existing blight criteria for redevelopment districts. More restrictive definitions of a *structurally substandard* building and of conditions that require *substantial renovation or clearance* are needed.
- The Legislature should require that expenditures of tax increments generated by a redevelopment district be used exclusively to induce redevelopment of blighted parcels.
- The Legislature should examine whether, and under what conditions, unusual terrain or soil deficiencies should continue to be a criterion that can be used to establish a redevelopment district or whether it is more appropriately a reason to establish an economic development district.

In addition, some more technical amendments concerning the blight findings for redevelopment districts are needed. These amendments seem appropriate in light of the difficulty we experienced in obtaining documentation of the blight findings from a number of municipalities with redevelopment districts. They attempt to ensure that municipalities are complying with the legal requirements for establishing a redevelopment district. We recommend that:

- The Legislature should require a municipality to specify in its tax increment financing plan which one of the blight criteria it is using and which parcels enable it to qualify a proposed district as a redevelopment district.
- A municipality should be required to maintain documentation on file that substantiates its finding that particular parcels meet the blight criterion used.
- The Legislature should require a municipality to document its blight findings again if it alters the size of a redevelopment district.

Another area needing attention is the increasing use of tax increments for general public improvements. These improvements--including improvements

to existing parks and recreation facilities, replacement of existing infrastructure, and similar municipal functions--are usually financed with a city's own funds, special assessments, or other sources of funding such as user fees. They often have little direct impact on development activity. Thus, tax increment financing is sometimes being used to provide a state and county subsidy for functions that most cities finance from other sources. In addition, some cities have used TIF to finance government buildings, and these are costs that most governmental bodies finance themselves. Current law restricts TIF expenditures only on certain types of municipal buildings. We recommend that:

- The Legislature should consider restrictions on the use of tax increment financing for various types of general public improvements normally financed from sources other than tax increment financing. Restrictions should apply to pre-1979 districts as well as districts created since the passage of the 1979 Minnesota Tax Increment Financing Act.
- The Legislature should consider the need for additional restrictions on TIF expenditures for government-owned or government-leased buildings.

Another issue raised in this report concerns the use of tax increments in housing districts for purposes other than to induce the construction of low and moderate income housing. We recommend that:

- The Legislature should require that tax increments generated by housing districts be used exclusively for the purpose of financing the development of low and moderate income housing.

We also recommend that:

- The Legislature should examine and clarify the purpose of economic development districts.

As long as the state continues to indirectly bear a major portion of the costs of a tax increment district, it seems reasonable that the purpose of an economic development district should be consistent with state goals. To the extent that economic development districts only result in shifting economic activity within the state, they serve no major state purpose. Existing law recognizes that the purpose of economic development districts is to create and retain jobs, as well as increase the property tax base. However, it assumes that creating jobs and increasing tax base at the local level is synonymous with creating jobs and increasing tax base at the state level. As pointed out earlier, the two are not always equivalent. One possibility the Legislature could explore would be to:

- require that the use of economic development districts be restricted to development activity that will increase or retain jobs for the state as a whole, and
- require that approval to establish an economic development district must be obtained from a state agency or entity such as the Minnesota Energy and Economic Development Authority.

There also needs to be legislative discussion of the increasing practices of tax increment pooling and establishment of large project areas. In some cases, cities employ these practices to spend tax increments for developments unrelated to the developments generating the increments. Furthermore, creating large project areas in which tax increments can be spent permits cities to extend the duration of districts to the maximum permitted by law. This conflicts with the statutory intent of Minn. Stat. §273.75, subd. 2., which requires that *excess tax increments* (tax increments that are in excess of the costs authorized by a tax increment financing plan) be used or set aside for the purpose of retiring a tax increment district early.

The report lists a number of options. One promising option would be to:

- permit expenditures outside a redevelopment district only if the expenditures directly address documented blight elsewhere within the project area (and place similar restrictions on the other types of districts).

These restrictions would prohibit pooling among districts of different types but permit expenditures within a project area for certain purposes.

Prior to August 1979, tax increment districts were not required to have tax increment financing plans. Consequently, there is no requirement on excess tax increments generated in pre-1979 districts. However, cities may expand the project area in which a pre-1979 district was located in order to find ways to use tax increments that were in excess of the district's original needs. This expansion may prevent pre-1979 districts that have served their purpose from being decertified prior to the final statutory deadline of August 2009.

As a result, the Legislature may wish to consider other restrictions to address how existing districts are being operated. We recommend that the Legislature consider the following options:

- prohibit any further expansion of existing project areas.
- prohibit a municipality from creating a new tax increment district or expanding an old district if the captured assessed value in existing districts plus the estimated captured assessed value in the proposed district or district expansion exceed a given percentage of the municipality's total assessed value.

A final area that merits attention is the lack of sufficient state oversight of tax increment districts. There is limited evidence that some tax increment districts do not comply with certain key provisions of the Tax Increment Financing Act. While our study did not include a comprehensive compliance audit, it is clear that certain types of compliance problems require greater state attention.

Specifically, there needs to be better compliance with those statutes that address the computation of captured assessed value and tax increments. These statutes directly affect the level of state aid and the development

subsidies which cities provide. The primary examples are statutes which describe 1) the method for computing original assessed value on tax-exempt property, 2) the "knock-down provision," and 3) the three-year limit on tax increment collection without the issuance of bonds, the acquisition of property, or the construction of public improvements.

Currently, no state agency audits or directly enforces these provisions. Also, while county auditors are generally presumed to have the primary responsibility for tax increment compliance, the tax increment financing law does not explicitly charge county auditors with this responsibility. As a result, county auditors are sometimes unfamiliar with tax increment financing provisions or unsure of their authority to enforce these provisions.

We recommend:

- The Legislature should provide clear authority for county auditors to enforce state tax increment financing laws affecting the determination of tax increments.
- The Minnesota Department of Revenue should provide additional guidance to county auditors on those TIF provisions that directly affect tax increment calculations. The department should ask county auditors to review existing districts and correct previous errors. Furthermore, the department should consider incorporating its communications to county auditors regarding tax increment financing into a broader property tax manual for counties, facilitating future application by the 23 counties which currently have no tax increment districts.

Some compliance problems may be beyond the scope of the county auditors' authority. For example, the question of whether certain expenditures are permitted by law is a legal issue, perhaps best addressed by the Office of the State Auditor. Currently, the State Auditor's compliance manual for city audits does not require reviews of tax increment districts for legal compliance. While we happened to find only a few cases in which the legality of TIF expenses is in question, we think there is a need for some oversight of these matters and of county auditors. Consequently, we suggest that the State Auditor's Office incorporate several key matters of legal compliance relating to tax increment districts into the State Auditor's compliance manual. Alternatively, the State Auditor could conduct periodic statewide studies of tax increment financing compliance.

2. FUNDAMENTAL CHANGES IN TAX INCREMENT FINANCING

At a minimum, the Legislature should consider tightening the state's TIF law as outlined above. However, tax increment financing is a complex program that is difficult to regulate, and it is not clear that additional restrictions will prevent future problems. In addition, it may not be possible to address TIF problems unless there are fundamental changes in the incentives cities have to create tax increment districts. These incentives stem from a divergence between *who funds* tax increment dis-

tricts, *who benefits* from tax increment districts, and *who initiates and controls* tax increment districts.

We think the Legislature should give some consideration to more fundamental changes in TIF. One option would be to change the tax increment district approval process. Currently, cities have sole authority to create tax increment districts. This change would require cities, counties, and school districts to jointly approve districts. In addition, the state would not pay state school aids on the captured assessed value in new tax increment districts. A second option would be to replace TIF with "redevelopment funds" financed from state and local sources. Under this option, cities would be permitted to use a variety of local revenue sources plus state funding to provide development subsidies. While neither of these options is a panacea for the problems with TIF, the Legislature should give some consideration to these and other alternatives that seek to make more fundamental changes in incentives.

INTRODUCTION

Chapter 1

This report examines the use of tax increment financing (TIF) in Minnesota. Tax increment financing is a tool used by cities to finance certain types of real estate development costs. The primary purposes of TIF are to attract private investment that will: (1) redevelop blighted areas, (2) provide housing for low and moderate income individuals and families, or (3) result in increased employment opportunities.

Over the last ten years, tax increment financing has become an increasingly popular development tool. In 1974, only four cities had development projects generating tax increments. By 1980, the number of cities grew to 81. Today, the number of cities using TIF is estimated to be over 210.

The growing popularity of TIF is due in part to the decline in federal resources available to cities for urban renewal and other development purposes. In addition, cities in Minnesota like others across the nation have become more interested and active in attracting private development over the last five years.

Despite this growth in TIF use, there has been little ongoing attention paid to tax increment financing at the state level in Minnesota. The Legislature passed a comprehensive tax increment financing law in 1979 and made modifications to the 1979 act in later years. However, little has been done at the state level to examine whether cities' use of TIF is consistent with legislative intent and is cost-effective. In fact, not much is known about how cities have used tax increment financing.

Three recent reports have raised questions about tax increment financing. An August 1984 report by the Minnesota State Auditor advocated a more selective use of public development subsidies. The report focused on tax-exempt financing of private development, particularly industrial revenue bonds, and addressed TIF to a lesser degree. A November 1984 report prepared by Hennepin County staff raised concerns about how TIF was being used in that county and made recommendations to the Legislature for changes in the Tax Increment Financing Act. There has been more use of TIF in Hennepin County than in any other county in the state. Finally, a June 1985 report by the Citizens League recommended tightening the use of tax increment financing and ultimately phasing it out. The Citizens

League recommended replacing TIF with city access to new redevelopment funds that would be initially financed from state and local sources.

Because of the recent concern about tax increment financing and the lack of statewide information on TIF, the Legislative Audit Commission directed the Program Evaluation Division to conduct a study of tax increment financing. During our study, we visited 44 Minnesota cities and conducted interviews with city officials familiar with their city's use of TIF. We gathered information on how tax increment financing was used in each city and reviewed the rationale used for establishing each tax increment district.

This report presents the results of our study. This chapter provides an introduction to tax increment financing. In particular, Chapter 1 answers the following questions:

- How does tax increment financing work?
- What governmental authorities can use TIF and for what purposes can it be used?
- What restrictions has the Legislature placed on the use of TIF and on the process for establishing a tax increment district?
- What changes has the Legislature made since 1979 that have permitted more flexible use of TIF?
- How has the use of tax increment financing grown over time?
- Who pays the costs of tax increment financing?

Chapter 2 presents the results of our research into how cities have used tax increment financing and analyzes various issues. A number of problems with the current use of TIF are examined. Chapter 3 discusses alternative methods of addressing these problems. An appendix describes the tax increment districts established within the 44 cities we visited.

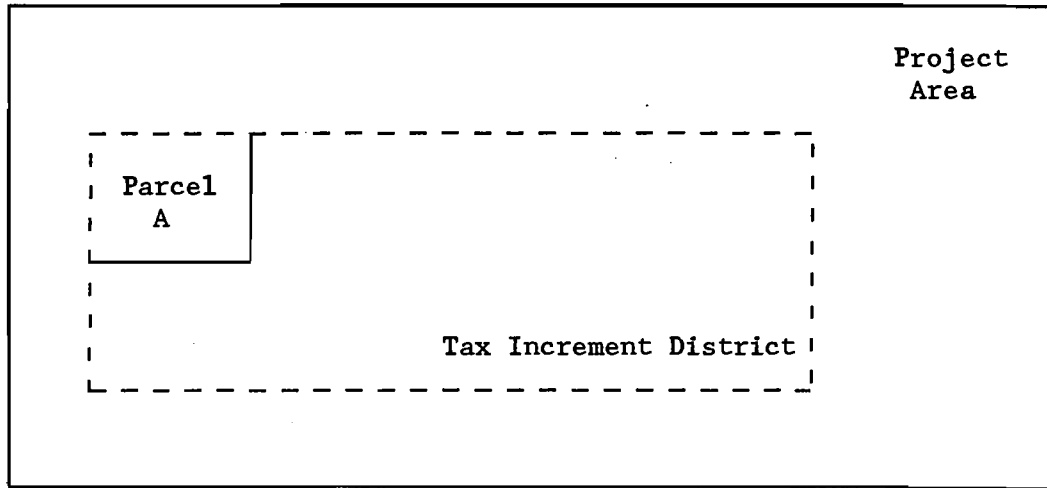
A. THE MECHANICS OF TAX INCREMENT FINANCING

Tax increment financing enables a city to use the additional property taxes that a proposed development would generate to finance land acquisition and write-down, demolition, and other costs necessary for that development to occur. Usually the issuance of tax-exempt bonds is necessary to finance these up-front public costs. The principal and interest on the bonds is repaid by the extra taxes that are generated by the new development. The taxes captured to repay the bonds come from all the taxing jurisdictions that normally levy a tax on property.

Figure 1.1 presents an example of how tax increment financing works. We will assume that a city has established a tax increment district in a

FIGURE 1.1

EXAMPLE OF TAX INCREMENT FINANCING



_____ = Project Area Boundaries

- - - - = Tax Increment District Boundaries

	<u>Original Assessed Value</u>	<u>Current Assessed Value (after development occurs)</u>	<u>Captured Assessed Value</u>
Parcel A	\$ 100,000	\$1,600,000	\$1,500,000
Rest of Tax Increment District	<u>2,000,000</u>	<u>2,000,000</u>	<u>-0-</u>
Total for District	\$2,100,000	\$3,600,000	\$1,500,000

Captured Assessed Value = \$1,500,000 (Current Assessed Value *minus* Original Assessed Value)

Mill Rate = 100 Mills

Tax Increment = \$150,000 (Mill Rate *times* Captured Assessed Value)

blighted section of the city. The district predominantly consists of vacant, substandard buildings. The city would like to revitalize this blighted section by inducing private redevelopment. The city would prefer new commercial office or retail development because that part of the city is zoned for commercial development.

A developer is considering building an office/retail development on Parcel A within the tax increment district, but has calculated that it would cost \$500,000 to purchase the property, demolish the vacant and substandard buildings, and install suitable public utilities. Since the developer can acquire a site in a neighboring city for just \$100,000, the developer is not inclined to build on Parcel A unless the city can reduce the costs of developing Parcel A to a comparable level. Consequently, the city agrees to pay for the costs (\$500,000) of land acquisition, demolition, and utilities and to sell the prepared site back to the developer for \$100,000.

Tax increment financing and the sale of tax-exempt bonds enable the city to finance the up-front costs. The city might issue general obligation bonds totaling \$650,000 to pay for the project expenditures of \$500,000 and capitalized interest and administrative expenses of \$150,000. Capitalized interest is the interest that the city must pay to bondholders during the first several years following issuance of the bonds. It is necessary to build capitalized interest into the bond issuance because the new development will be in the construction phase during the first several years and will not be on the property tax rolls. No tax increment will be available to the city to pay bond interest or principal until the construction is complete and the development is on the tax rolls.

The principal and interest on the \$650,000 of bonds is eventually repaid from two sources: (1) tax increments collected during the life of the tax increment district and (2) the proceeds of land resale if any (\$100,000 in this example). The tax increments are calculated by applying the total mill rate to the additional assessed value generated by the development. In this example, we assume that at the time the district was established the *original assessed value* of the district at the time of district creation was \$2,100,000 (including \$100,000 for Parcel A and \$2,000,000 for the remainder of the district). After the redevelopment of Parcel A is complete, the city estimates that the then *current assessed value* of Parcel A will be \$1,600,000 while the remainder of the district will still be assessed at \$2,000,000. The total assessed value of the district will then be \$3,600,000. Tax increment financing permits the city to capture the taxes on the difference between the current assessed value and the original assessed value. The difference, or *captured assessed value*, is \$1,500,000 in this case. The captured taxes, or *tax increments*, are \$150,000 per year (100 mills times \$1,500,000). The amount of tax increment captured each year could increase (or decrease) if the assessed value of property in the tax increment district increases (or decreases) from \$3,600,000.

It should be noted that tax increment financing does not change the amount of property taxes a developer pays. In the above example, the developer of Parcel A pays taxes of \$160,000 (100 mills times an assessed value of \$1,600,000). This is the same as the developer would pay even if the

development had been undertaken without the use of tax increment financing. Tax increment financing instead determines who will receive that \$160,000. Without tax increment financing (assuming the project would have been undertaken anyway), the entire \$160,000 would have been distributed to the city, county, school district, and other taxing jurisdictions according to their mill rates. With tax increment financing, only \$10,000 (100 mills times the original assessed value of \$100,000 on Parcel A) will be distributed to the various taxing jurisdictions according to their mill rates. The remaining \$150,000 in taxes on Parcel A are distributed to the city to pay the costs of the tax increment district. Thus, the county, school district, and other minor taxing jurisdictions share in providing the funding for city development projects using tax increment financing.

It should also be noted that tax increment financing provides a means for cities to provide subsidies to developers. In our example, if the city had sold the cleared land in Parcel A to the developer for \$1 instead of \$100,000, then the developer would have received a subsidy of \$99,999 over what was required to make the project occur. In such a case, it would have cost the developer \$99,999 less to undertake the project on Parcel A than in the neighboring city where land acquisition and preparation costs were \$100,000.

Alternatively, assume that Parcel A was really worth \$500,000 to the developer because of the additional retail business and office rentals that would be conducted there. While the next best site only cost \$100,000 to acquire and prepare for development, it would not generate as much business and consequently was not as valuable as Parcel A. If the city cleared and prepared Parcel A and sold it for \$100,000, the developer would have received a subsidy of \$400,000.

B. USERS AND USES OF TAX INCREMENT FINANCING

Tax increment financing is generally used by cities or development authorities, such as city housing and redevelopment authorities (HRAs) and port authorities, under the direct or indirect control of the city or municipality. Additional entities that can use TIF include county HRAs, rural development financing authorities, and the Iron Range Resources and Rehabilitation Board.

Approximately two-thirds of the captured assessed value (CAV) and tax increments collected in Minnesota are from tax increment districts set up by housing and redevelopment authorities. Slightly less than one-third of the CAV and tax increments collected are from districts set up by cities directly. Port authorities account for less than two percent.¹

¹Minnesota House Research Department analysis of Minnesota Department of Revenue data, October 23, 1985.

Use of tax increment financing requires the use of two statutes. First, the 1979 Minnesota Tax Increment Financing Act (Minn. Stat. §273.71 to 273.78) must be followed in establishing a tax increment district and a tax increment financing plan. The Minnesota Tax Increment Financing Act of 1979 permits the establishment of three different types of tax increment districts: (1) redevelopment districts, (2) housing districts, and (3) economic development districts. The general purpose of a *redevelopment district* is to remove blighted buildings or improve blighted land in order to induce redevelopment. To qualify as a redevelopment district, the properties in a district must meet one of five blight criteria in Minn. Stat. §273.73, subd. 10(a). These criteria are shown in Figure 1.2. A redevelopment district may last for up to 25 years after the receipt of the first tax increment.

The purpose of a *housing district* is to encourage the development of housing for individuals and families of low and moderate income. Although other programs exist to subsidize the development of such housing, tax increment financing provides cities and authorities with a tool to write down the costs of land and public improvements. TIF is also used to provide an interest rate write-down on loans to home buyers. Like redevelopment districts, housing districts may last up to 25 years after receipt of the first tax increment. However, housing districts need not be established on blighted property.

An *economic development district* is a district that does not meet the requirements of a redevelopment or housing district but is found by a city or authority to be in the public interest because it will:

- discourage commerce, industry or manufacturing from moving their operations to another state, or
- result in increased employment in the city, or
- result in preservation and enhancement of the city's tax base.²

It was thought that the use of economic development districts would generally involve vacant or under-utilized land with smaller acquisition and relocation costs than other types of districts. As a result, the maximum duration of an economic development district is less than that of a redevelopment or housing district. An economic development district is limited to the lesser of: (a) ten years from approval of the tax increment financing plan or (b) eight years from receipt of the first tax increment.

Prior to August 1, 1979 when the Minnesota Tax Increment Financing Act became effective, cities and authorities were able to establish tax increment financing districts through six statutory provisions found in five different statutes.³ Consequently, districts certified prior to

²Minn. Stat. §273.73, subd. 12.

³"Tax Increment Financing: Funding Community Development with Future Tax Receipts," prepared by the law firm of Holmes and Graven for the Department of Energy and Economic Development, May 1984, p. 3.

FIGURE 1.2

BLIGHT CRITERIA FOR REDEVELOPMENT TAX INCREMENT DISTRICTS

To qualify as a redevelopment tax increment district, *one of the following conditions*, reasonably distributed throughout the district, must apply:

- (1) Seventy percent of the parcels in the district are occupied by buildings, streets, utilities or other improvements, and more than 50 percent of the buildings, not including outbuildings, are structurally substandard to a degree requiring substantial renovation or clearance;¹ or
- (2) Seventy percent of the parcels in the district are occupied by buildings, streets, utilities or other improvements, and 20 percent of the buildings are structurally substandard, and an additional 30 percent of the buildings are found to require substantial renovation or clearance in order to remove such existing conditions as: inadequate street layout, incompatible uses or land use relationships, overcrowding of buildings on the land, excessive dwelling unit density, obsolete buildings not suitable for improvement or conversion, or other identified hazards to the health, safety and general well-being of the community; or
- (3) Less than 70 percent of the parcels in the district are occupied by buildings, streets, utilities or other improvements, but due to unusual terrain or soil deficiencies requiring filling, grading or other physical preparation for use at least 80 percent of the total acreage of such land has a fair market value upon inclusion in the redevelopment district which, when added to the estimated cost of preparing that land for development (excluding costs directly related to roads) exceeds its anticipated fair market value after completion of said preparation; or
- (4) The property consists of underutilized air rights existing over a public street, highway or right-of-way; or
- (5) The property consists of vacant, unused, underused, inappropriately used or infrequently used railyards, rail storage facilities or excessive or vacated railroad rights-of-way.

Source: Minn. Stat. §273.73, subd. 10.

¹"Structurally substandard" means containing defects in structural elements or a combination of deficiencies in essential utilities and facilities, light and ventilation, fire protection including adequate egress, layout and condition of interior partitions, or similar factors, which defects or deficiencies are of sufficient total significance to justify substantial renovation or clearance.

August 1, 1979 constitute a fourth type of district. Throughout this report, any district certified prior to the 1979 act will be referred to as a *pre-1979 district*. The 1979 act permitted pre-1979 districts to last up to another 30 years -- until August 1, 2009. Consequently, the maximum duration of a pre-1979 district ranges from 30 years to slightly more than 40 years, depending on when the district was originally established.

Besides the 1979 act, a city or authority establishing a district after August 1, 1979 must use a second statute in order to: (1) create the project area in which the tax increment district is located and within which tax increments must be expended and (2) specify the public purpose served by the project. This second statute must be one of five different acts:

- The Minnesota Housing and Redevelopment Authority Act (Minn. Stat. §462.411 to 462.82).
- The Municipal Development District Act (Minn. Stat. §472A).
- The Minnesota Port Authorities Act (Minn. Stat. §458.09 to 458.1991).
- The Municipal Industrial Development Act (Minn. Stat. §474).
- The Rural Development Finance Authority Act (Minn. Stat. §362A).

The Minnesota Housing and Redevelopment Authority Act permits cities to create housing and redevelopment authorities (HRAs) to deal with sub-standard conditions in housing and other buildings. The members of a city's governing body often serve as commissioners of the city's HRA. Commissioners are appointed by the mayor subject to the approval of the city's governing body.

The Municipal Development District Act permits cities to establish development project areas in order to provide employment opportunities, improve the tax base, and improve the general economy of the state.⁴ The Minnesota Port Authorities Act allows municipal port authorities to establish industrial development project areas and expend public funds to stimulate the private development of marginal lands. The Municipal Industrial Development Act permits cities, urban towns, HRAs, port authorities, and counties (for projects outside of incorporated areas) to use tax increment financing for projects using industrial revenue bonds. The act attempts to prevent, through governmental action, the emergence of blighted and marginal lands and areas of chronic unemployment.⁵ The Rural Development Finance Act authorizes counties to create rural development financing authorities to assist in developing agricultural processing facilities.

⁴Minn. Stat. §472A.01

⁵Minn. Stat. §474.01, subd. 2.

These five statutes provide viable development tools themselves even if tax increment financing is not used. For purposes of tax increment financing, these statutes define what entities can use TIF. In addition, they govern the types of expenditures that can be made using tax increments. While the 1979 Tax Increment Financing Act lists some purposes for which tax increments *cannot* be used, these five statutes define the purposes for which tax increments *can* be used. Generally, tax increment financing is used for site acquisition and preparation costs. However, these five statutes authorize the use of TIF for a variety of other purposes. Figure 1.3 contains a list, prepared by the Minnesota House Research Department, of a number of the authorized uses of TIF. This list, while extensive, is not exhaustive. Some potential uses of tax increment financing are the subject of dispute among development attorneys because of the vagueness of the language in these statutes.

C. LEGAL RESTRICTIONS

The Minnesota Tax Increment Financing Act places a number of restrictions on tax increment financing. These restrictions are of three types: (1) procedural requirements, (2) reporting requirements, and (3) substantive limitations on its use.

Major procedural requirements include the following:

- The city or authority proposing to use tax increment financing must prepare a tax increment financing plan, which includes a statement of objectives, a list of proposed development activities, an estimate of the type of development expected to occur and when it is likely to occur, estimates of project costs and revenues, and an estimate of the impact TIF will have on the assessed values of all taxing jurisdictions in which the proposed tax increment district is located.
- The city or authority must provide an opportunity for the affected county and school boards to comment on the tax increment financing plan.
- When the city and the authority are not the same, the governing body of the city must be given an opportunity to approve or disapprove of the proposed TIF plan.
- A public hearing on the plan must be held.
- The city must make a number of findings of which the most important is that the proposed development would not be reasonably expected, in the city's opinion, to occur solely through private investment within the reasonably foreseeable future and therefore the use of tax increment financing is necessary.

FIGURE 1.3

AUTHORIZED USES OF TAX INCREMENT FINANCING

- Acquisition of "blighted" properties, "marginal land," vacant or under-utilized land or properties or of any property as part of a development plan to eliminate or prevent the development of "blight" or the causes of blight (See, e.g., Minn. Stat. §§458.191-458.192, 462.421, subd. 13)
- Sale, lease or other disposition of acquired properties at or below market value (i.e., "land write-downs") (See, e.g., Minn. Stat. §§458.192, subd. 9 and 10; 462.421, subd. 13(5))
- Demolition and removal of "blighted" buildings or other structures (see, e.g., Minn. Stat. §§458.192; 462.421, subd. 13)
- Elimination of physical characteristics of the land that make development difficult (e.g., ground water problems (See, e.g., Minn. Stat. §462.421, subd. 13)
- Engineering, planning, and administrative costs (including the allocated administrative costs of the authority) (See, e.g., Minn. Stat. §462.545, subd. 1)
- Installation of streets, utilities, and other site improvements (See, e.g., Minn. Stat. §462.421, subd. 13(4))
- Relocation payments to displaced residents and businesses (See, e.g., Minn. Stat. §462.445, subd. 4(17))
- Construction of housing for low and moderate income persons or veterans (See, e.g., Minn. Stat. §462.421, subd. 12)
- Relocation, restoration, or rehabilitation of buildings of historical or architectural value (Minn. Stat. §462.421, subd. 13; 462.445, subd. 4(3))
- Interest rate reduction payments for low and moderate income housing developments, both rental and owner occupied, and small commercial developments (Minn. Stat. §462.445, subd. 10 to 12)
- Acquisition and construction of agricultural processing projects including forest products (site, building, and equipment) (See Minn. Stat. §362A.01, subd. 2(a))
- Capital investment loans for rail line rehabilitation (made indirectly to rail users) (Minn. Stat. §362A.01, subd. 2(h))
- Acquisition and construction of parking lots and ramps, pedestrian skyways and related facilities (See Minn. Stat. §472A.03)
- Guarantees or insurance for industrial development or mortgage subsidy bonds (See, e.g., Minn. Stat. §§462C.07, subd. 3; 474.10, subd. 10)

Source: Minnesota House Research Department, October 23, 1985.

This last finding is typically referred to as the "but for" clause and is considered by many to be the key requirement that restricts the use of tax increment financing to only those situations in which it is necessary and desirable. However, as we will see in Chapter 2, the "but for" clause is subject to a variety of interpretations that diminish its impact on decisions to use tax increment financing.

The city or authority is also required to meet certain reporting requirements including the following:

- After adoption, a tax increment financing plan should be filed with the Minnesota Department of Energy and Economic Development.
- For all tax increment districts, an annual financial disclosure report must be made to the county board, school board, Department of Energy and Economic Development, and, if the authority is not the same as the city, the affected city.⁶
- An annual financial statement must be published in a newspaper of general circulation in the affected city.

Finally, and most importantly, the Tax Increment Financing Act imposes certain limitations on tax increment districts established after August 1, 1979. These limitations are of three types: (1) limitations on the ability of cities to receive tax increments on increasing assessed value that was not induced by tax increment financing, (2) limitations on the type and amount of expenditures that can be made from tax increments, and (3) restrictions designed to prevent excessive risk-taking by cities.

The Legislature has placed limitations on the ability of cities to capture tax increments from development not stimulated by TIF. Without such limitations, cities could capture increments at a relatively low cost to them, thus depriving other taxing jurisdictions of taxes. These limitations include the following:

- The increased valuation of improvements for which building permits were issued between 3 and 18 months prior to approval of a TIF plan cannot be captured by a tax increment district.
- Tax increments cannot be collected on any parcel in a tax increment district if that parcel has not developed or the city has not acquired the parcel or made improvements to or adjacent to the parcel within four years from the certification of the district.⁷

⁶Beginning in 1986, annual financial disclosure reports must be submitted to the State Auditor instead of the Department of Energy and Economic Development.

⁷This provision is commonly referred to as the "knockdown provision." Amendments in 1982 reduced the time period from five to four years.

- No tax increment can be paid for a tax increment financing district if the city or authority has not issued bonds, acquired property within the district, or constructed or caused the construction of public improvements within the district within three years of the date of certification. (This provision also applied to pre-1979 districts if such activity did not occur prior to August 1, 1982.)
- The act attempts to prevent general inflation in property values from being captured in an economic development district. State law requires county auditors to increase the original assessed value of an economic development district each year by the average percentage increase in the assessed value of all property in the district during the five years prior to establishment of the district.

The act imposes the following limitations on the type and amount of expenditures that can be made from tax increments:

- Beginning in 1982, newly established districts cannot expend tax increments to construct or renovate a municipally-owned building used primarily and regularly for conducting city business. (Parking structures, parks, and facilities used for social, recreational, or conference purposes and not primarily for conducting city business are exempted from this restriction.)
- Administrative expenses cannot exceed 10 percent of a district's total tax increment expenditures or the total tax increment expenditures authorized by the TIF plan, whichever is less.
- Tax increment financing cannot be used to circumvent levy limitations.
- If a district generates more tax increments ("excess increments") than are necessary to pay the costs authorized by the tax increment financing plan, then the excess increments must be used to prepay outstanding bonds, placed in an escrow account dedicated to the payment of existing bonds, or returned to the affected taxing districts in proportion to their mill rates.

The latter restriction appears to establish a clear policy that excess increments should be used to retire a district early or at least diminish the tax impact on other taxing jurisdictions. However, since a city may adopt a very ambitious tax increment financing plan that includes long lists of possible expenditures, this restriction may not be as effective as it appears.

Finally, the act contains limitations intended to prevent cities and authorities from taking excessive risks. They include the following:

- The act prohibits a city or authority from owning at any one time, with the use of tax increment bonds, more than 25 percent of the acreage to be acquired within a project area that contains

a redevelopment district without having concluded a development agreement that provides recourse if the development is not completed. The limit for a housing or economic development district is 10 percent.

- The act prohibits using unusual soil or terrain deficiencies as a reason for establishing a redevelopment district unless the city or authority has development agreements for at least 50 percent of the acreage having such deficiencies and those agreements provide for recourse if development does not occur.

D. REDUCED RESTRICTIONS SINCE 1979

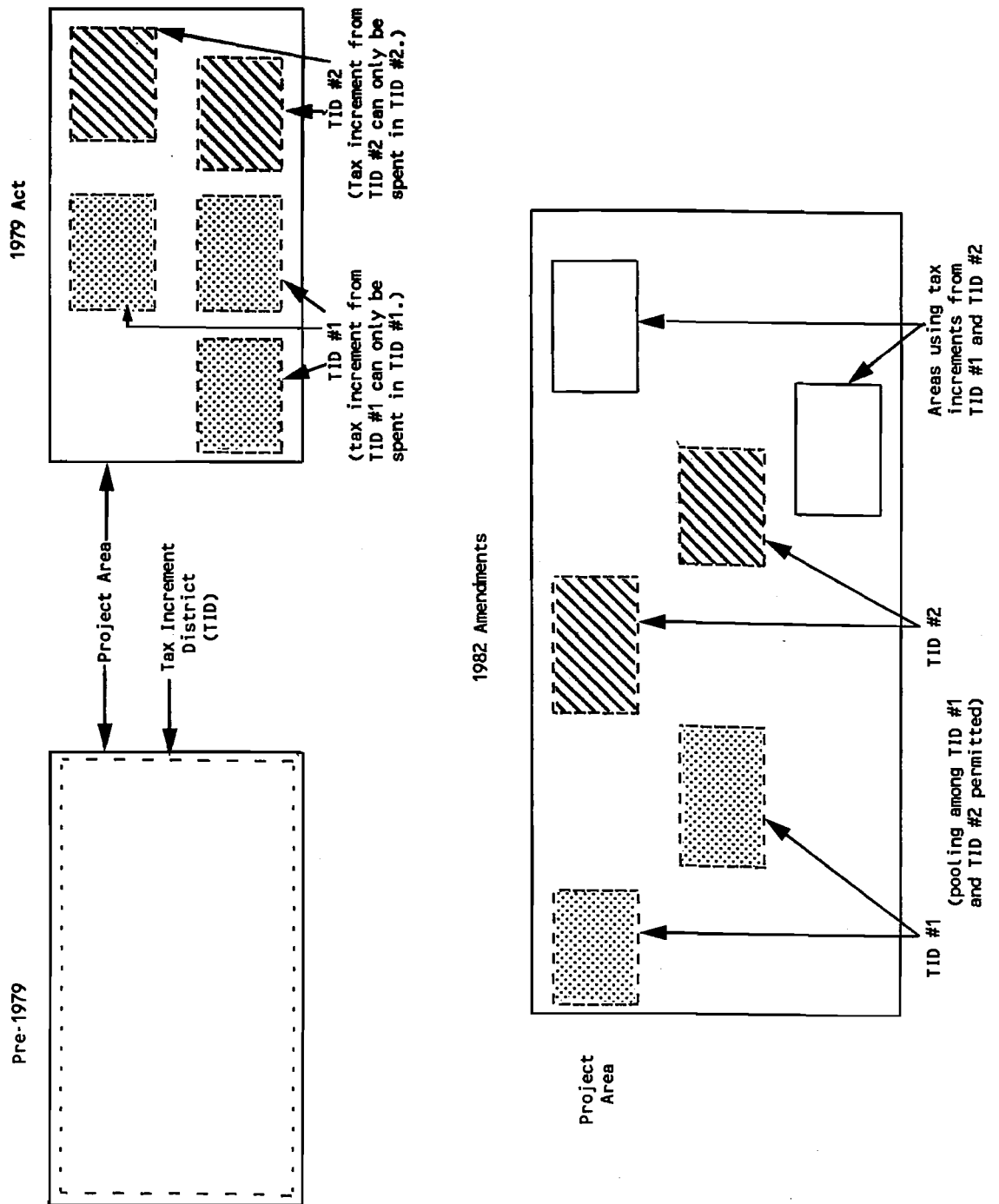
In general, the 1979 Tax Increment Financing Act and subsequent amendments placed additional restrictions on the use of tax increment financing that did not previously exist. In at least one key respect, however, the act loosened restrictions that had existed prior to August 1, 1979. Previously, tax increment districts were required to be coterminous with development project areas. As a result, if a large downtown business district was designated as a redevelopment project area and TIF was used for the project, the entire downtown business district was also placed in a tax increment district. Because large amounts of commercial property were being placed in tax increment districts and increased valuation from this property was not available for general tax purposes, the 1979 Legislature permitted cities and authorities to establish tax increment districts that were smaller in size than their associated project areas. The 1979 act also allowed *non-contiguous* and *multiple* tax increment districts within a single project area. However, the tax increments generated by a district had to be spent only within that district and not within any other districts or any other part of the project area. In order for a city to expend tax increments outside the district, the city would have to expand the district. Figure 1.4 illustrates the difference between the arrangements authorized by the 1979 act and those previously permitted.

In 1982, amendments to the act permitted cities and authorities to expend tax increments from a district anywhere within the associated project area. As a result, tax increments from one district in a project area could be used to support development activity in: (1) other districts in the same project area, including other types of districts, or (2) portions of the project area in which no district exists. The use of tax increments from two or more districts to fund a particular development within a project area is commonly referred to as *pooling*. Figure 1.4 illustrates how the 1982 amendments further loosened the restrictions on tax increment expenditures.

Subsequently, cities and attorneys active in the development business determined that existing law may permit a city or authority to create a *master project area* in order to permit pooling among any number of a city's tax increment districts or within non-district parts of the broadly defined master project area. Since the master project area could conceivably be an entire city, the use of master projects may permit the

FIGURE 1.4

CHANGES IN THE CONFIGURATION OF
TAX INCREMENT DISTRICTS AND PROJECT AREAS



expenditure of tax increments from a district anywhere else within the city.⁸ Figure 1.5 illustrates the use of a master project.

The ability of cities to establish master projects, to pool tax increments among districts or spend them elsewhere within a project area, and to establish non-contiguous districts has raised a number of important policy issues. In Chapter 2, we discuss these issues and review the sorts of districts and project areas that cities have established in response to the reduced restrictions.

E. GROWTH IN THE USE OF TAX INCREMENT FINANCING

Minnesota was one of the first states to implement tax increment financing enabling legislation. In 1968, Robbinsdale established Minnesota's first tax increment district, using a provision of Minnesota Statutes Chapter 462 that permitted the capture of tax increments for housing projects. In 1971, special legislation allowed for the creation of three more districts (one in Robbinsdale, two in Minneapolis). In 1974, the Legislature passed legislation permitting any Minnesota municipality to establish a tax increment district.

1. NUMBER OF CITIES USING TIF

Table 1.1 shows the growth since 1974 in the number of cities using TIF, the tax increments collected, and the captured assessed value. The 1985 figure of 190 cities is based on the House of Representatives Research Department's review of Department of Revenue data for taxes payable in 1985.

We asked the Department of Energy and Economic Development (DEED) to maintain a record of newly submitted plans during the course of our study. As a result, we learned of many additional cities that established their first tax increment district between July and December 1985. Based on existing data and the DEED records, we estimate that:

- A minimum of 214 Minnesota cities now use tax increment financing.

This estimate is a minimum because it does not include: (1) those cities that created their first district between October 1984 and June 1985; (2) cities that created their first district after July 1985 but have not yet submitted TIF plans to DEED.

⁸Our discussion of the historical relationship between tax increment districts, project areas, and expenditures of tax increments borrows heavily from James S. Holmes, "Tax Increment Financing--A Calm Before the Storm," *Minnesota Cities*, June 1985, p. 5.

FIGURE 1.5

MASTER PROJECT

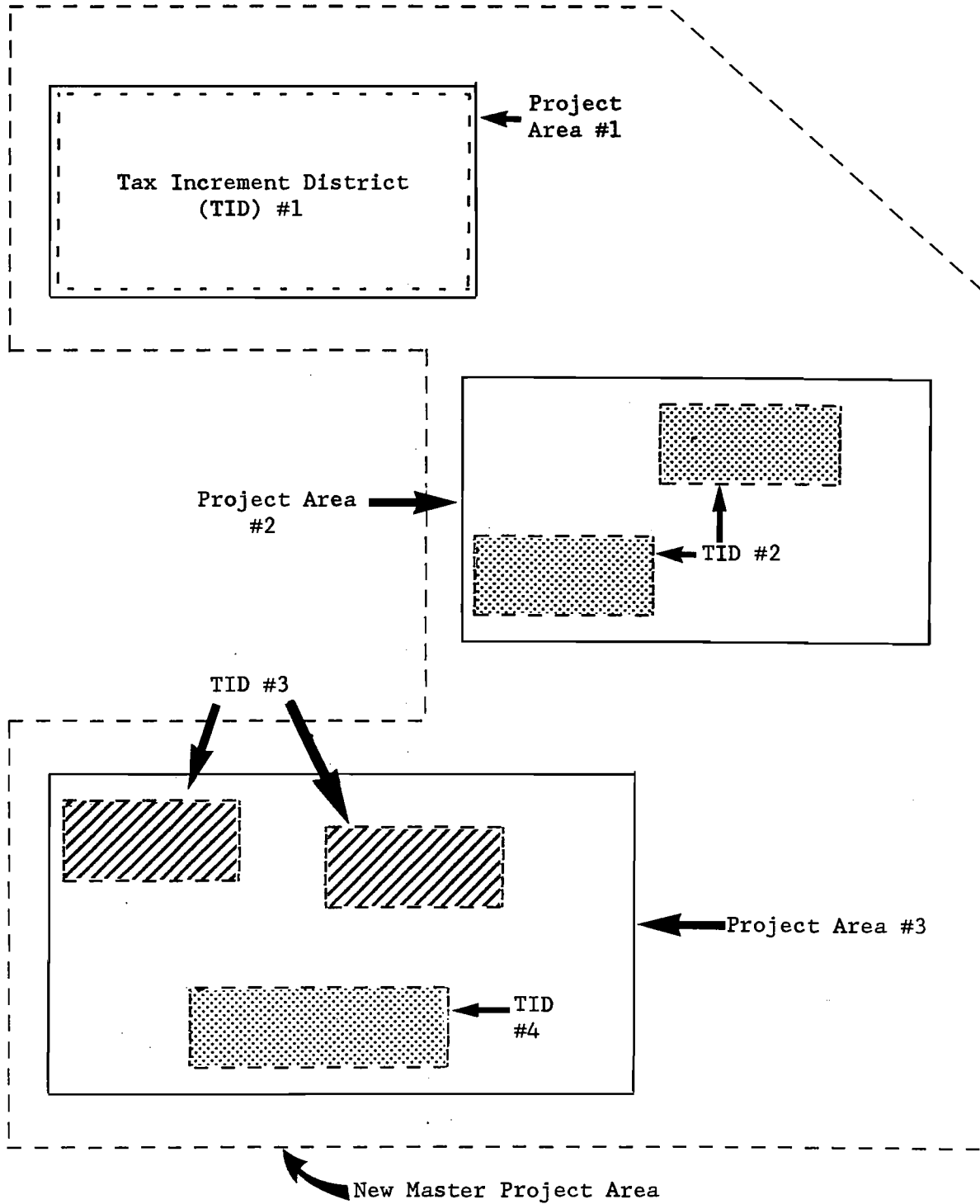


TABLE 1.1

HISTORICAL STATEWIDE USE OF TIF: NUMBER OF CITIES,
CAPTURED ASSESSED VALUE, TAX INCREMENT

<u>Year^a</u>	<u>Cities Using TIF</u>	<u>Captured Assessed Value (CAV)</u>	<u>Percent of Assessed Value Captured^b</u>	<u>Tax Increment</u>
1974	4	\$ 3,634,483	0.24%	\$ 437,085
1975	10	20,036,557	0.81	2,689,574
1976	21	26,220,175	0.77	3,181,516
1977	29	32,127,149	0.83	3,939,863
1978	42	43,380,473	0.88	5,306,640
1979	57	62,286,066	1.08	7,418,288
1980	81	102,280,206	1.43	11,305,114
1981	99	223,310,857	2.39	22,489,390
1982	122	332,367,840	3.02	35,141,374
1983	127	437,195,546	3.45	46,425,859
1984	153	516,465,249	3.55	58,154,910
1985	190	635,897,268	3.95	70,761,119

Source: Minnesota Department of Revenue Local Government Aids and Analysis Division. The 1985 estimate of the number of cities using TIF was made by the Minnesota House of Representatives Research Department, based on a review of Department of Revenue tax data.

^aYear in which taxes are payable.

^bPercentages represent the portion of total assessed value that is captured in cities with tax increment districts.

Of the 60 cities filing plans for new districts between July and December, 23 were cities that had no previous tax increment districts. Most of the cities establishing new districts were from outside the seven-county Twin Cities area.

Most large cities in Minnesota have at least one tax increment district. Table 1.2 shows the largest cities in Minnesota that do not use tax increment financing.

2. NUMBER OF DISTRICTS

It is far more difficult to estimate the number of tax increment districts in Minnesota than it is to estimate the number of cities using TIF. For example, the Department of Revenue's data on TIF districts do not always include those districts that have no captured assessed value. In addition, since some cities have not submitted annual financial disclosures of

TABLE 1.2

LARGEST MINNESOTA CITIES THAT HAVE NOT USED TAX INCREMENT FINANCING

<u>City</u>	<u>1983 Population Estimate^a</u>
Maplewood	27,780
Eagan	25,080
Cottage Grove	20,120
Shoreview	18,830
Oakdale	13,000
Mounds View	12,800
Bemidji	11,285
Andover	10,170

Source: Program Evaluation Division analysis.

^aOffice of the State Demographer estimate.

TIF districts, DEED's information on the number of TIF districts is even less complete than the Department of Revenue's.

To make a rough estimate of the number of TIF districts in Minnesota, we combined and compared data from a variety of sources: the Department of Revenue, the Department of Energy and Economic Development, the Office of the State Auditor, our visits to 44 cities, and DEED's record of districts created in the last half of 1985. Based on this information, we estimate that:

- At least 475 tax increment districts currently exist in Minnesota.

During the last half of 1985, DEED received TIF plans for 97 new districts. Thus, cities were creating tax increment districts at a rate of about 200 per year. If this rate of increase continued, one would expect the total number of districts to continue to increase dramatically in the near future. The number of district terminations would be relatively small in comparison to the number of new districts.

The future growth in districts is, however, uncertain. On the one hand, some of the new districts created in the latter half of 1985 may have been established in response to pending federal legislation affecting the tax-exempt status of tax increment bonds. As a result, the rate of district creation might not continue at its recent rapid pace. On the other hand, as other development tools and resources are restricted at the federal level, TIF may continue to be a popular development option for cities.

While it is interesting to note the rate of increase in tax increment districts, one should not equate the number of districts a city has with the amount of captured value in those districts or the amount of tax increments generated. The primary reason is that district size varies considerably among cities. For example, Northfield has six districts and Princeton has two. However, Northfield's districts are relatively small; Princeton's districts contain a large portion of the city's commercial and industrial development. Princeton has more captured assessed value, as a percentage of its tax base, than any other Minnesota city. Thus, the captured assessed value in tax increment districts and the tax increments generated are probably more useful measures of the use of TIF than the number of districts.

3. CAPTURED ASSESSED VALUE AND TAX INCREMENTS

The captured assessed value in tax increment districts and the tax increments collected by cities has increased sharply statewide in recent years. In 1979, the year the Legislature passed the Tax Increment Financing Act, just over one percent of the assessed value of cities using TIF was captured in districts. By 1985, tax increment districts captured nearly four percent of the assessed value in those cities with districts. Table 1.1 shows the trend between 1974 and 1985. When the entire state is included, the percentage of captured assessed value is somewhat smaller. In 1985, tax increment districts captured 3.2 percent of the state's total assessed value, compared with 0.5 percent in 1979. Table 1.3 shows the cities that have the highest percentage of their assessed value captured in tax increment districts.

The amount of tax increments generated statewide has grown sharply along with captured assessed value. As Table 1.1 indicates, the amount of tax increments has risen from \$0.4 million in 1974 and \$7.4 million in 1979 to \$70.8 million in 1985.

F. THE COSTS AND BENEFITS OF TAX INCREMENT FINANCING

1. COST AND BENEFIT SHARING

While we discuss specific tax increment expenditures and results in Chapter 2, it is important to first discuss how tax increment financing affects various taxing jurisdictions. One of the unique features of tax increment financing is that it requires different governmental jurisdictions to share the costs of development finance with the understanding that these jurisdictions will share in the benefits (and recoup their investment) at a later date. Many of the policy issues surrounding TIF stem from this notion of shared costs and benefits.

When a city creates a tax increment district, three governmental jurisdictions appear to have a major financial stake in this decision: the city, the county, and the school district. However, as we will discuss later,

TABLE 1.3

MINNESOTA CITIES WITH MORE THAN TEN PERCENT OF THEIR ASSESSED VALUE
CAPTURED IN TAX INCREMENT DISTRICTS

<u>City</u>	<u>Percent of City Assessed Value That Is Captured</u>	<u>1985 Net Tax Increments^a</u>
Princeton	17.9%	\$ 394,932
Chanhassen	16.7	1,215,708
Annandale	15.0	95,472
Appleton	11.9	72,171
Benson	11.6	95,680
Cottonwood	11.2	36,854
Rushford	11.0	70,345
Waconia	10.9	193,719
Buffalo	10.8	210,107
Marshall	10.4	546,203
Rush City	10.2	78,327

Source: Taxes payable 1985 data from the Minnesota Department of Revenue, Local Government Aids and Analysis Division.

^a"Net tax increments" represent the gross tax on captured assessed value minus homestead credits and enterprise zone credits.

state aid compensates school districts for most of their TIF investment, so school districts typically have only a minor stake in tax increment district creation. As a result, the state, the city, and the county are the jurisdictions that finance most of the costs of tax increment financing.

It is beyond the scope of this study to calculate the degree to which the state, cities, counties, and others bear the costs of tax increment financing. However, it appears that:

- The state bears a significant portion of the costs of a new tax increment district, perhaps more than either the city or county.
- The extent to which cities bear the costs of new tax increment districts may vary significantly.

The extent of the state's contribution can be seen by examining mill rates. The taxpayer in a typical Minnesota city pays more property taxes to a school district than to a city or county. In the seven-county Twin Cities metropolitan area, the average school district accounts for 48 percent of the total mill rate. The city and county account for 21 and 26

percent of the total mill rate, respectively. Other taxing jurisdictions account for five percent. Outside the Twin Cities area, the average school district accounts for 43 percent of the total mill rate, the city accounts for 31 percent, and the county accounts for 25 percent. When cities create new tax increment districts, they capture taxes from the various governmental jurisdictions in roughly these proportions. Because state aids reimburse about 90 percent of the captured school district taxes on average, the state indirectly bears a major portion of TIF costs.⁹

The degree to which cities bear the costs of TIF appears to depend primarily on two factors: 1) the ratio of a city's mill rate to the total mill rate in that city, and 2) the ratio of a city's tax base to the tax base of the county and school district in which the tax increment district is located.¹⁰ The greater a city's mill rate as a percentage of its total mill rate and the greater the city's tax base in relation to those of the county and school district, the greater the portion of TIF costs borne by the city.

These factors seem to work against the large central cities in the Twin Cities metropolitan area and in favor of smaller suburban communities. For example, Minneapolis and St. Paul had city mill rates that were 32 percent and 28 percent respectively of their total mill rates for taxes payable in 1985. The metropolitan area average was 21 percent. Among suburbs that have used TIF, the lowest city mill rate percentage was 11 percent. Thus, the typical suburb may be able to shift a greater portion of the costs of a new tax increment district to other taxing jurisdictions than the larger central cities.

The issue of "who benefits" from tax-increment financing is as important as the issue of who pays the costs. Tax increment districts may result in a variety of benefits. The most obvious is a higher tax base. In addition, tax increment districts may result in new employment, new housing, aesthetic improvements, social benefits, and community pride. Many tax increment benefits are difficult to quantify.

Taxing jurisdictions may be willing to forego taxes on property if the benefits of that property's development outweigh the costs of the foregone taxes. Determining the benefits of tax increment districts depends on one's perspective. While construction of a new grocery store may benefit a small city, there may be few net benefits for the county (since the new store may simply take business from other stores in the county). Similar-

⁹Cities may have an additional TIF cost. If a development generates insufficient tax increments to repay general obligation bond debt, the city is legally obligated to levy taxes or otherwise pay for the remaining debt service. However, as we discuss in Chapter 2, city levies for debt service are not very common.

¹⁰See Jack R. Huddleston, "Variations in Development Subsidies Under Tax Increment Financing," *Land Economics*, August 1981, pp. 373-384, for a detailed discussion of how these factors work.

ly, while one city may benefit greatly from TIF-subsidized soil corrections, the county may realize few benefits if the same development could have occurred elsewhere in the county without subsidized soil work. As a general rule, if a development would occur in a taxing jurisdiction without public subsidy, that jurisdiction realizes few or no benefits from subsidizing that development to occur at a particular site. As a result,

- Perhaps the greatest TIF financial risk faced by taxing jurisdictions is the possibility of subsidizing development that would occur without subsidies.

A final issue related to TIF affects only the Twin Cities metropolitan area. In this region, the benefits of new commercial and industrial construction are partially shared through the "fiscal disparities law" (Minn. Stat. §473F). Under this law, metro area cities and other taxing jurisdictions contribute 40 percent of the increase in commercial/industrial assessed value since 1971 to an area-wide pool. Metropolitan taxing jurisdictions receive a portion of this shared base (according to population and fiscal capacity), thus lessening some of the revenue-raising disparities among taxing jurisdictions.

Increases in commercial/industrial assessed value in tax increment districts are generally counted when contributions to the area-wide pool are calculated. The exception to this rule is that housing and redevelopment authority districts established before August 1, 1979 are exempted from making contributions. For other districts, contributions must be made, but a city may choose from two options. The tax increment district can either directly make the contribution to the fiscal disparities pool or its contribution can be made by commercial/industrial property elsewhere in the city but-outside the district.

The primary effect of the fiscal disparities law on tax increment financing is that a metropolitan area city does not receive the full benefit from increased commercial/industrial property valuation it is able to attract. A portion of the benefits must be shared with other cities and taxing jurisdictions throughout the area.

2. STATE COSTS

As noted in the previous section, the state indirectly pays for a significant portion of the costs of tax increment financing. The most reliable estimate of these costs is made in a soon to be published report by the Minnesota House of Representatives Research Department.¹¹

According to the House Research study, the total state TIF cost for taxes payable in 1985 is about \$22.6 million. State education aids account for \$17.6 million of this amount. The state guarantees each school district a certain amount of revenue per pupil. If districts cannot raise this reve-

¹¹Minnesota House Research Department, "An Estimate of the State Costs of Tax Increment Financing," forthcoming.

nue through application of a specified mill rate to the district's equalized assessed value (and most cannot), state aid makes up the difference. Tax increment districts affect this level of aid by keeping portions of local assessed value off the tax rolls. The only cases in which the state does not fully reimburse school districts for captured TIF taxes are those districts which generate the state-guaranteed revenue levels entirely from local property taxes. Statewide, education aids reimburse school districts for over 90 percent of the taxes captured in tax increment districts.

The other large source of state TIF costs is homestead credit payments. Tax increment financing affects homestead credit payments by keeping captured assessed value off the tax rolls. Higher mill rates are thus necessary to finance given local government levies. Increased mill rates result in higher residential property taxes and the payment of greater homestead credits by the state. The study by House Research estimates these costs at \$4.5 million in 1985. Other state TIF costs include those that occur through agricultural credits (\$300,000) and the local government aid formula (\$100,000).

These cost estimates were calculated by including TIF captured assessed values in local tax bases and then recomputing state aids and property tax credits. It could be argued that this approach measures the gross costs of TIF but not the net costs. If TIF subsidized development would not have occurred within the state without TIF, then the TIF captured assessed values would not have even been in local tax bases without TIF. These cost estimates would then overestimate the true net costs of TIF.

The House Research report clearly recognizes the importance of this point and discusses at length the possible effects TIF may have on development. The report finds that TIF subsidies may somewhat increase the amount of investment in taxable real estate in Minnesota. This increase would come from two primary sources. First, TIF may attract development that would have otherwise occurred in other states. This is most likely to occur when TIF is used for manufacturing facilities. It may also occur for some commercial development, particularly when TIF is used in border areas or for the regional offices of national firms that could locate in other states. Second, TIF subsidies will tend to lower the cost of commercial real estate development in Minnesota and cause investors to shift more investment to taxable real estate in the short run. In the long run, the real estate prices rise and the cost of real estate development rises back up to earlier levels. The net effect is more commercial real estate development than without TIF.

The House Research report concludes that these two factors have fairly small effects. For example, the use of TIF for manufacturing or other footloose facilities is rather limited. As a result, the House Research report also concludes that estimates of state TIF costs based on the assumption that captured assessed value would be available to local governments are probably reasonable estimates of the net state costs. Their estimates may tend to slightly overstate state costs since TIF probably results in some statewide increase in real estate development. However, this effect is likely offset by other factors, including the fact that

their estimates did not attempt to take into account increased state costs under the property tax refund program.¹²

¹²House Research's report on state costs provides a much more complete explanation of their methodology and conclusions.

TAX INCREMENT FINANCING: USES AND ISSUES

Chapter 2

Due to the increasing number of tax increment districts in Minnesota and changes in tax increment law since 1979, there is considerable legislative interest in the local use of TIF. However, statewide information on specific city uses of TIF is not readily available. As a result, we visited 44 Minnesota cities, evaluating the uses of TIF in each. This chapter presents a summary of major policy issues that merit legislative attention. The discussion focuses on the following questions:

- What types of expenditures have Minnesota cities made with TIF, and what issues do these expenditures raise?
- To what degree does the "but for" test, an important part of Minnesota's TIF law, protect the public interest?
- How successful have tax increment districts been in achieving public objectives? Which governmental jurisdictions benefit from these achievements?

A. THE STATE'S INTEREST IN TAX INCREMENT FINANCING

Historically, state executive agencies have collected data on tax increment financing as required by law, but they have played no further role in the oversight of TIF. Until 1986, the Department of Energy and Economic Development (DEED) collected cities' TIF plans and annual expenditure disclosures, but the department had no responsibility to formally review or comment on these documents. Beginning in 1986, the Office of the State Auditor will collect the annual disclosures. The State Auditor also collects data on the bonded indebtedness in tax increment districts, and the Department of Revenue collects information on the captured assessed value in districts.

The branch of state government most active in TIF oversight has been the Legislature. It created TIF for general use in 1974 and subsequently enacted restrictions on the process for tax increment district creation

and on permitted uses of TIF. Since the late 1970s, the Legislature has made several significant revisions to the tax increment statutes.

While the creation of a tax increment district and the expenditure of tax increments are local actions (requiring no consent by other taxing jurisdictions), there are several reasons why the state should have an interest in TIF. One reason is TIF's financial impact on the state. State dollars are involved when a city creates a tax increment district. The state's financial involvement is indirect, occurring primarily through school aid and homestead credit payments. As reported in Chapter 1, the overall annual cost of TIF to the state is estimated to be more than \$22 million, assuming that TIF has only a limited effect on the amount of real estate development occurring in Minnesota. We examine the validity of this assumption later in this chapter. Tax increment financing also affects the state's trunk highway expenditures. Several cities have used TIF in place of state highway user funds to finance highway improvements. While TIF-financed improvements may save the state some highway funds, these improvements occur outside the state's normal project selection process and may increase state highway maintenance workloads.

Second, the state has an interest in the achievement of public objectives at the lowest possible cost. The redevelopment of blighted areas, the provision of affordable housing, and the development of viable local economies that encourage job retention and creation are general state goals. It is appropriate to consider whether the developments made possible by tax increment financing confer significant local and state benefits. At the same time, however, the state wants to ensure that inter-city competition for development does not create incentives for unnecessary or excessive public subsidies.

A third reason for the state's interest in tax increment financing is equity. The Legislature has placed levy limitations on local units of government to restrain property tax growth. It is important to consider whether tax increment financing has been used to circumvent these limits. It is also worth considering whether TIF restrictions developed by the Legislature have succeeded in limiting city TIF uses to appropriate purposes. There are equity implications if cities interpret state law differently or if compliance with TIF restrictions is not universal.

B. THE USE OF TAX INCREMENT FINANCING IN MINNESOTA

1. THE STUDY SAMPLE

To obtain detailed information on the use of tax increment financing in Minnesota, we visited 44 cities currently using TIF. For each city visited, we reviewed the TIF plans on file with the state. After this review, we travelled to cities to discuss the districts with city officials (typically city administrators, economic development directors, and finance directors). As time permitted, we visited tax increment sites. Following the visits to cities, we verified district information by phone

and we asked cities to review the summaries contained in the appendix for accuracy.

In selecting cities to visit, we included a combination of large and small cities from various parts of the state. We included many cities with large amounts of captured assessed value or with several tax increment districts. We also included "new" users of TIF, some of whom have relatively small amounts of captured assessed value. Although the sample is technically not a random sample, we think it is reasonably representative of the wide variety of cities in Minnesota that have used TIF and the range of TIF uses in those cities.

The cities visited represent approximately one-fifth of the Minnesota cities using TIF. The TIF districts of these cities contain \$488 million in captured assessed value, or 77 percent of the total captured assessed value in Minnesota. Table 2.1 shows the captured assessed value of cities we visited; Table 2.2 shows the types of districts in these cities.

TABLE 2.1

1985 CAPTURED ASSESSED VALUE IN CITIES VISITED

<u>City</u>	<u>Number of Districts</u>	<u>Total City Assessed Value</u>	<u>Total Captured Assessed Value</u>	<u>Percent of City Assessed Value That Is Captured</u>
Coon Rapids	7	\$ 200,969,924	\$ 1,587,192	0.79%
Fridley	5	233,417,232	5,458,497	2.34
Chanhassen	2	63,230,032	10,583,672	16.74
Chaska	3	51,188,244	341,413	0.67
Brooklyn Park	3	271,067,425	9,856,390	3.64
Eden Prairie	7	311,320,027	26,122,325	8.39
Golden Valley	4	284,389,037	14,777,658	5.20
Robbinsdale	3	79,256,409	5,522,781	6.97
New Brighton	8	147,502,861	1,140,018	0.77
Roseville	4	369,593,575	1,290,068	0.35
Savage	6	37,402,718	2,830,603	7.57
Shakopee	5	96,610,423	7,559,129	7.82
Blaine	4	148,301,025	1,666,086	1.12
Mendota Heights	1	76,504,706	2,432,970	3.18
Bloomington	17	848,777,898	5,735,665	0.68
Minneapolis	35	2,979,696,566	261,569,512	8.78
St. Paul	6	1,755,031,684	75,214,197	4.29
Lakeville	6	91,691,057	1,975,893	2.15
New Prague	4	11,909,847	643,214	5.40
METRO TOTALS	130	\$7,954,259,786	\$433,688,176	5.45%

<u>City</u>	<u>Number of Districts</u>	<u>Total City Assessed Value</u>	<u>Total Captured Assessed Value</u>	<u>Percent of City Assessed Value That Is Captured</u>
Mankato	13	\$ 13,184,424	\$ 9,677,728	7.05%
Dodge Center	3	7,120,898	315,572	4.43
Rushford	1	5,600,994	614,664	10.97
Albert Lea	4	74,657,508	249,271	0.33
Zumbrota	1	12,039,503	582,988	4.84
Willmar	3	72,130,337	2,279,499	3.16
Cottonwood	1	3,663,974	408,965	11.16
Marshall	5	57,278,795	5,979,500	10.44
Glencoe	3	17,638,944	804,690	4.56
Winsted	2	5,393,874	138,029	2.56
Princeton	2	15,791,258	2,824,871	17.89
Faribault	5	61,843,253	2,076,288	3.36
Northfield	6	41,035,928	528,942	1.29
Aurora	2	6,021,582	195,648	3.25
Duluth	8	292,388,119	14,324,304	4.90
Hibbing	3	66,453,833	1,066,911	1.61
Mountain Iron	2	14,657,309	20,468	0.14
Proctor	1	9,078,230	11,205	0.12
Virginia	7	41,621,299	2,514,759	6.04
Benson	2	9,384,462	1,090,113	11.62
Winona	8	84,120,537	1,622,140	1.93
Hutchinson	1	44,863,754	3,258,772	7.26
Annandale	2	6,993,381	1,049,883	15.01
Buffalo	1	22,275,686	2,399,820	10.77
North Branch	3	5,388,704	0	0.00
GREATER MN TOTAL	89	\$1,114,626,585	\$ 54,035,030	4.85%
STATEWIDE TOTALS	219	\$9,068,886,372	\$487,723,206	5.38%

Source: The Program Evaluation Division determined the number of districts. The assessed value data is from the Minnesota Department of Revenue's data for taxes payable in 1985.

2. GENERAL FINDINGS

From our visits to 44 cities and from other existing sources, we gathered a variety of descriptive data on the use of tax increment financing. The appendix contains a summary of TIF use in about 200 districts in these cities. We also made some general findings about the way cities use TIF. While we discuss several of these findings in greater detail later in the report, our summary of findings includes the following:

- Most cities finance developments in TIF districts with bonds, the vast majority of which are general obligation bonds.

TABLE 2.2

TYPES OF TAX INCREMENT DISTRICTS IN CITIES VISITED

(Includes Only Those Cities In Our Sample)

<u>City</u>	<u>Pre-1979</u>	<u>Redevelopment</u>	<u>Economic Development</u>	<u>Housing</u>	<u>Total</u>
Coon Rapids	0	6	0	1	7
Fridley	1	2	2	0	5
Chanhassen	1	0	1	0	2
Chaska	0	2	0	1	3
Brooklyn Park	0	1	2	0	3
Eden Prairie	0	0	7	0	7
Golden Valley	2	1	0	1	4
Robbinsdale	2	0	0	1	3
New Brighton	0	8	0	0	8
Roseville	0	3	0	1	4
Savage	0	2	2	2	6
Shakopee	1	3	1	0	5
Blaine	0	1	2	1	4
Mendota Heights	0	1	0	0	1
Bloomington	6	3	7	1	17
Minneapolis	21	8	3	3	35
St. Paul	2	1	2	1	6
Lakeville	0	2	3	1	6
New Prague	<u>0</u>	<u>3</u>	<u>0</u>	<u>1</u>	<u>4</u>
METRO TOTALS	36	47	32	15	130
Mankato	3	3	7	0	13
Dodge Center	0	2	0	1	3
Rushford	0	1	0	0	1
Albert Lea	1	2	1	0	4
Zumbrota	0	1	0	0	1
Willmar	1	2	0	0	3
Cottonwood	1	0	0	0	1
Marshall	0	4	0	1	5
Glencoe	1	1	0	1	3
Winsted	0	1	0	1	2
Princeton	1	0	1	0	2
Faribault	0	4	1	0	5
Northfield	3	1	2	0	6
Aurora	1	0	1	0	2
Duluth	3	4	1	0	8
Hibbing	0	2	1	0	3
Mountain Iron	0	2	0	0	2
Proctor	0	1	0	0	1
Virginia	2	5	0	0	7
Benson	2	0	0	0	2
Winona	1	7	0	0	8

<u>City</u>	<u>Pre-1979</u>	<u>Redevelopment</u>	<u>Economic Development</u>	<u>Housing</u>	<u>Total</u>
Hutchinson	0	1	0	0	1
Annandale	1	1	0	0	2
North Branch	0	1	1	1	3
Buffalo	<u>1</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>1</u>
GREATER MN TOTALS	22	46	16	5	89
STATEWIDE TOTALS	58	93	48	20	219

Source: Program Evaluation Division interviews with cities, current as of December 1985.

The cities that do not issue bonds usually finance development using city funds, federal community development funds, or the tax increments generated by developments. Typically, cities that use city or federal funds to finance developments later reimburse those accounts with tax increment revenues.

In our reviews of tax increment district and project area configurations, we found that:

- Many districts established prior to the 1979 revisions in TIF law are very large, sometimes encompassing entire downtowns. However, we also found that some districts created after the 1979 revisions are also very large, ranging up to 873 parcels.
- Over half of the cities we visited have a tax increment district that is part of a larger project area. This configuration permits cities to spend tax increments outside the boundaries of the tax increment district.
- Of the cities in our sample with two or more districts, 32 percent have pooled tax increments from two or more districts or have fairly certain plans to do so. Another 16 percent of the cities are considering pooling and have a project area configuration that will permit this.¹
- Over one-third of the cities we visited drew boundaries in a tax increment district to include parcels that would have developed

¹We define pooling as the use of tax increments from two or more tax increment districts for the same development project within a single project area. Pooling does not occur if tax increments from two or more districts are used for different development projects within a single project area and are not commingled.

without TIF. Cities included these parcels to generate revenues for later development subsidies.

In reviewing the financial status of tax increment districts, we found that:

- The vast majority of districts generate sufficient tax increments to pay for debt service. Only a few cities have needed to levy general taxes to make up for revenue shortfalls.
- In recent years, most cities we visited minimized the financial risk of TIF through development agreements and assessment agreements.

Development agreements represent the developer's guarantee that the project will proceed as planned. In addition, developers may agree to pay taxes on a minimum assessed value, as determined by agreement with the city.

The healthy financial status of tax increment districts is not always attributable to TIF. In some cases, non-subsidized developments, inflation, or routine changes in assessed value contribute large amounts of captured assessed value to districts. As a result, the financial status of TIF districts is not a particularly good measure of tax increment financing's effectiveness.

On the topic of tax increment expenditures, we found that:

- While the use of TIF is widely varied, the most common use of TIF is land acquisition, typically accompanied by a land write-down.
- Four Minnesota cities have made trunk highway improvements (such as interchanges) with TIF. Several cities have used TIF for large infrastructure projects, such as bridges, dikes, and major storm sewer additions.
- More than one-third of the cities in our sample established at least one TIF district to improve land with poor soils.
- The vast majority of TIF expenditures appear to be made for legally permissible activities.

In our discussions with cities on development philosophy, we found that:

- While cities differ in their approach to development finance, many cities believe that land should be written down to the fair market value of cleared land to compete with other sites. In addition, many cities believe that developments "pay their way" if they generate tax increments equal to the subsidy granted.

State law requires districts established after August 1, 1979 to have TIF plans on file with the state. We found that:

- Of the districts in our sample subject to this 1979 provision and created before 1985, 68 percent had plans on file.

3. REASONS FOR ESTABLISHING DISTRICTS

Minnesota cities create tax increment districts to serve a broad range of public and private purposes. It is not unusual to find single districts created to meet multiple objectives.

In part, the variety of reasons for creating tax increment districts stems from the range of problems that currently face different parts of the state. In rural Minnesota, the downturn in the farm economy threatens the economies of small cities. While rural cities would like to attract new businesses, many must focus their efforts on maintaining the existing businesses. Proposals for major new development are infrequent, and there is a lack of investment in existing buildings. The small budgets and taxing power of these cities sometimes preclude major public projects (such as streets or sewers), and some city officials feel that their voters will not support tax increases.

In metropolitan areas, low-income neighborhoods suffer from lack of investment. Aging strip commercial areas cannot compete effectively with shopping malls. Downtowns continue to have some physical blight and low-intensity land uses. Most parts of the cities are built up.

In inner-ring suburbs, some of the inner city development problems are emerging. Older commercial areas cannot accommodate heavy traffic and large businesses. Some of these suburbs have little vacant land to use for commercial and industrial sites, and some older housing developments need repairs.

To meet their unique challenges, many cities have found tax increment financing a useful tool. Figure 2.1 provides a list of some specific reasons for district creation. The most common TIF use is land acquisition, often accompanied by a write-down to the developer.

4. CONFIGURATION OF PROJECT AREAS AND TAX INCREMENT DISTRICTS

Prior to the 1979 changes in the tax increment statutes, most cities' tax increment districts were coterminous with their project areas.² As a result, many tax increment districts were very large, freezing sizable amounts of assessed value. The 1979 TIF revisions permitted cities to establish tax increment districts that were smaller than the project areas of which they were part.

²One exception was Robbinsdale, which established a scattered site district in 1968 and created a citywide project area several years later.

FIGURE 2.1

SOME REASONS WHY CITIES ESTABLISH TAX INCREMENT DISTRICTS

- *To assemble land.* Many cities use TIF to acquire multiple parcels of land that might be difficult to purchase privately (e.g., because of absentee owners).
 - *To provide land write-downs.* Cities purchase land for private development so that the land may be re-sold to the developer below the price paid by the city.
 - *To address physical deterioration of property.*
 - *To address the economic obsolescence of old commercial or industrial areas.*
 - *To implement local planning preferences.* These preferences may relate to the intensity of development, the size of parcels, the location of parking, building set-backs, etc.
 - *To encourage the development of land that has soil or terrain problems.*
 - *To increase the local tax base.*
 - *To increase or retain the local supply of jobs.*
 - *To capture tax increments from developments already occurring.*
 - *To provide city services in newly-developing areas and to provide access to these areas.*
 - *To replace streets and utilities in developing areas.*
 - *To help cities make offers of financial incentives to business that are competitive with offers of other cities.*
 - *To address shortages of certain types of housing.*
 - *To assist other tax increment districts financially.*
 - *To meet the local share of state or federal grants.*
-

We visited a number of cities that have most or all of their central business districts in pre-1979 districts. These include:

Princeton	77 parcels
Cottonwood	64 parcels
Glencoe	72 parcels
Duluth	372 parcels
Aurora	87 parcels
Chanhassen	132 parcels
Annandale	201 parcels
Buffalo	408 parcels
Golden Valley	770 parcels
Robbinsdale	447 parcels
Mankato	183 parcels
St. Paul	827 parcels ³

One might expect to find smaller tax increment districts after 1979, when new state laws introduced objective blight criteria, the five-year "knock-down provision," and the opportunity to create non-contiguous districts. Some cities have created very small districts, containing only the area directly benefitted by TIF. But we also found that:

- Some cities have continued to create large tax increment districts.

Table 2.3 lists the largest districts created since 1979 in cities we visited. While we further discuss large districts later in this chapter, it is worth noting the following: large districts probably benefit cities more than other taxing jurisdictions. Particularly for redevelopment and housing districts (which do not have assessed value adjustments for inflation), the inclusion of large numbers of parcels probably prevents counties and school districts from gaining routine and inflationary increases in assessed valuation that occur.

We also examined the size of cities' project areas. While the tax increment district consists of the properties from which revenues will be generated, the project area consists of those properties on which tax increments can be spent. We found that:

- Some cities have very large project areas in which tax increment expenditures can be made.

For example, the entire city of Mendota Heights constitutes a project area for the city's single tax increment district. The entire city of Robbinsdale lies in two project areas. The entire "built-up" portion of Hibbing is also in a project area.

³The number of parcels listed is the current number of parcels in the district, as reported by cities to the Department of Revenue for taxes payable in 1985.

TABLE 2.3

LARGE TAX INCREMENT DISTRICTS ESTABLISHED AFTER 1979^a

(Includes Only Cities From the Study Sample)

<u>City</u>	<u>District</u>	<u>Parcels</u>
Duluth	West Duluth/Oneota Industrial Park TID	873
	Waterfront and Eastern TID	487
Chaska	Floodplain TID	833
St. Paul	Scattered Site Housing TID	827
Faribault	Old Town TID	546
	Heselton Industrial Park TID	139
	West TID	109
Savage	TID 5	505
Willmar	Downtown TID	293
Eden Prairie	TID 2	284
Hutchinson	TID 1	222

Source: Information on the number of parcels is from the Department of Revenue, *Tax Increment Financing District Supplement to the Abstract of Tax Lists*, p. 1985.

^aThese are the largest districts in our sample in terms of the number of parcels. Some districts in our sample may have acreages equal to those listed, but they have fewer parcels than the districts listed.

Some cities create large project areas to facilitate the pooling of TIF funds of two or more districts in a single project area. For example, Roseville is pooling the increments of two districts to finance a bridge over an interstate highway. Other cities have large project areas that accommodate the expenditure of funds from financially successful districts. For example, Shakopee's single project area encompasses five districts, and the city may use excess increments from a successful district (perhaps the Canterbury Downs race track) to make downtown improvements. Of the cities in our sample with more than one district, nearly one-half have pooled TIF revenues between districts or are considering future pooling.

5. FINANCIAL STATUS OF MINNESOTA TAX INCREMENT DISTRICTS

Some of the recent concern over TIF in Minnesota stems from a few well-documented cases in which a development's tax increments proved insufficient to pay debt service expenses. For example, Minneapolis has had three such districts: Loring Park (which once had financial difficulties but now generates increments far in excess of its original debt service requirements), Nicollet-Lake, and Centre Village.

In our review of nearly 200 tax increment districts, we found that:

- The vast majority of districts generate sufficient tax increments to pay for project costs. Only a few cities have needed to levy general taxes to make up for revenue shortfalls.

The most notable exception to this finding is Zumbrota, which must levy \$130,000 over the next five years to finance its single district. In part, Zumbrota's problems stem from the revaluation of the city's primary TIF development, a subsidized housing complex. Other cities have experienced minor problems. For example, Duluth levied \$91,000 between 1977 and 1979 to support its now-viable Truck Center district. Currently, the city's West Duluth/Oneota district also generates insufficient increments to meet debt service on its bonds, requiring part of the debt service to be paid with tax increment bond proceeds. In addition, Brooklyn Park's first district failed to generate as many increments as planned, so the city established a second district and pools increments from the two.

There are several reasons why the majority of districts are financially sound. One reason is that cities are increasingly shifting the financial risk to developers. Many, if not most, cities now have development agreements in hand before creating tax increment districts. Development agreements are construction commitments for particular land parcels; the agreements provide for city recourse if the development is not completed. In addition, most recent districts have assessment agreements, in which the developer agrees to a minimum assessed value for the development. Such agreements guarantee revenue streams for the city which, typically, are sufficient to meet future debt service. Some cities also require developers to finance any future shortfalls in the city's tax increment debt service. One city we contacted requires developers to pay annually for basic city service costs (e.g., police, fire, inspections) related to the development. We concluded that, in recent years:

- Most cities have minimized the financial risks they face when establishing tax increment districts.

While the financial risks for cities have declined, they have not been eliminated. Some cities use TIF in a speculative manner, hoping to induce developments not yet in hand. For example, Hibbing recently issued nearly \$1 million in tax increment bonds to help finance infrastructure for an industrial park. The city had just one development lined up at the time of the issue, and this project will produce insufficient revenues to cover debt service. Hibbing city officials are hopeful that the infrastructure investments will lure other businesses. A second risk borne by cities is

an unexpected change in property valuation. In several municipalities outside the Twin Cities metropolitan area, stable or declining property values have produced districts that are less financially viable than originally anticipated. A third risk to cities is the possibility of statewide changes in property tax classification, which could affect the amount of tax increments generated.

While most Minnesota tax increment districts are financially viable, we found that:

- The healthy financial status of tax increment districts is not always attributable to tax increment financing.

We found five primary sources of assessed value increases aside from TIF-induced increases. These sources are: 1) development induced by government subsidies other than TIF, 2) development that occurs without public assistance, 3) inflation, 4) property revaluation, and 5) zoning changes.

The first source of increases in assessed value is development induced by public funds other than tax increment financing. There are many cases in which TIF and other subsidies work together to produce development. Cities often use tax increment financing for land clearance and they use industrial development bonds for building construction. However, some cities capture tax increments from developments induced entirely by subsidies other than TIF. For example, about \$500,000 of the \$1.7 million captured assessed value in Princeton's industrial park comes from a firm induced to locate in Princeton solely by an Urban Development Action Grant; the tax increment district did not exist when the firm started construction. In Mountain Iron, the city has spent virtually no tax increment funds to induce the five businesses that now occupy the city's first district. Instead, the city used a state grant to make soil corrections and to build frontage roads.

Some cities capture large amounts of assessed value produced with no public subsidies of any sort. Fridley created its Moore Lake TID in 1981, after determining the district to be blighted. The city has issued no bonds and has made no substantive TIF expenditures in the district. Nevertheless, the private development of 17 housing units since 1981 has produced sizable tax increments. As of 1985, the district had nearly \$500,000 in captured assessed value, and the district generates close to \$50,000 in tax increments annually.

A third cause of assessed value increases is inflation. By state law, counties adjust the original assessed value of economic development districts annually for inflation; there is no such adjustment for redevelopment and housing districts. While lesser inflationary increases occurred in many cities' assessed values in recent years, we found that older tax increment districts often had large increases during the 1970s.

Fourth, revaluation of properties may affect captured assessed value. For example, it appears that Winsted's downtown tax increment district benefitted enormously from a recent revaluation by the county assessor. Most

of the properties in this 1982 district had not been revalued for several years. A 1984 revaluation resulted in 25 percent assessed value increases on some properties. Without this revaluation, it is doubtful that Winsted's tax increments would cover the city's TIF expenses.

Fifth, zoning changes sometimes contribute to assessed value increases. The clearest example of this is the rezoning of agricultural land. Because farmland is assessed lower than other classes of land, the mere act of rezoning land from "agricultural" to "commercial/industrial" following creation of a tax increment district may result in assessed value increases.

Finally, it is worth noting that many pre-1979 tax increment districts remain subject to the laws that applied at the time of district creation, and this often enhances the financial viability of these districts. In general, the Legislature has "grandfathered" the pre-existing districts when making changes in the TIF law. As a result, the older Minnesota tax increment districts have fewer restrictions than newer districts. For example, current law prohibits collection of tax increments from parcels on which no development occurs in the district's first four years. No such law existed prior to 1979, and this contributes to the continued large size (and often the large captured assessed value) of pre-1979 tax increment districts.

6. TAX INCREMENT EXPENDITURES

State law requires cities to disclose their tax increment expenditures to the state each year. However, we found the annual disclosures to be of limited value in reviewing TIF expenditures for two reasons. First, some cities do not comply with the disclosure requirement. In 1983, we found that 64 cities with active tax increment districts (as verified by Department of Revenue and State Auditor's Office data) did not submit disclosures. Second, the reporting forms used through 1985 provided little insight into expenditure details. The forms had only four categories of expenditures (bond payments, administration, land acquisition, and capital expenditures).

The appendix of this report provides a description of tax increment expenditures in each city we visited. For most expenditure items, we do not provide data on dollar amounts (due in part to space requirements and the lack of this data in some cities). However, the appendix offers a detailed overview of the primary uses of TIF in 44 Minnesota cities.

While the types of TIF expenditures made by cities varies considerably, the most common TIF expenditure is land acquisition. Figure 2.2 provides a summary of the public improvements financed with TIF in the cities we visited. The figure shows that many cities use TIF to extend city services to newly-developing parts of cities. In addition, several cities have used or plan to use tax increment financing to fund major structures such as interchanges, railroads, dikes, and water storage tanks.

In addition to the public improvement expenditures shown in Figure 2.2, cities have found other uses for TIF. Four cities in our sample used tax

FIGURE 2.2

TYPES OF PUBLIC IMPROVEMENTS FINANCED WITH TIF^a

(Includes only those cities in our sample)

Extension of roads, sewers to large, new developing areas:

Annandale	Chanhassen	Duluth	Hibbing
Lakeville	Mankato	Marshall	Mendota Heights
Mountain Iron	New Brighton	New Prague	Northfield
Roseville	Savage	Shakopee	Benson
Albert Lea	Chaska	Coon Rapids	Glencoe
Winona	Winsted	Bloomington	Blaine
Hutchinson	North Branch		

Improvement of existing local streets and roads

Brooklyn Park	Buffalo	Chaska	Cottonwood
Faribault	Fridley	Golden Valley	Lakeville
Mankato	Marshall	Willmar	Mendota Heights
Dodge Center	North Branch	Roseville	Shakopee

Construction of major new highway improvements

Brooklyn Park (interchange)	Eden Prairie (ring road)
Proctor (bridge)	Roseville (bridge)
Bloomington (bridge, roads)	Shakopee (road)

General downtown improvements (e.g., sidewalks, lighting, street furniture):

Duluth	Buffalo	Dodge Center	Willmar
North Branch	Aurora	Cottonwood	New Prague
Winona	Hibbing	Benson	Glencoe
Zumbrota			

Skyways:

Duluth	St. Paul	Minneapolis
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Public parks

Annandale	Coon Rapids	St. Paul	Virginia
Marshall	New Brighton	Fridley	

Government-owned or -leased buildings

Coon Rapids (fire station)	Dodge Center (airport)
Fridley (police garage)	Lakeville (fire station)
St. Paul (civic center)	Mendota Heights (fire station)
Princeton (flight service station)	

Figure 2.2, continued

Construction of railroad extensions:

Hutchinson	Marshall	Virginia
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Construction of lift stations, water wells or water towers:

Chaska	Shakopee	Annandale	Blaine
Mankato	Winona		

Flood control projects:

Chaska	Mankato
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Soil corrections (in some cases, the corrections were not made using TIF):

Albert Lea	Coon Rapids	Mankato	Mountain Iron
New Brighton	Fridley	Robbinsdale	Lakeville
Marshall	Roseville	New Prague	Virginia
Savage	Winona	Blaine	Mendota Heights
Hutchinson			

Burying of power lines:

Golden Valley

Parking ramps:

Mankato	Minneapolis	St. Paul
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Source: PED interviews with city officials.

^aIncludes completed or planned improvements

increments as a security device for development projects, typically funding a reserve account for industrial development bonds. Another four cities used (or plan to use) tax increments or TIF bonds to make business loans. Four cities used TIF to provide interest rate write-downs to developers or to home buyers.

Some cities have used TIF in particularly unusual ways. Duluth currently uses TIF to provide free parking at several downtown parking ramps. Winona had a debt in its downtown parking fund (due to the removal of parking meters), so the city used \$122,000 in tax increments from a downtown housing development to pay off the debt. And in St. Paul, tax increments have funded a portion of the Town Square Park maintenance and operations budget since completion of the park as part of a TIF-financed development in 1980 (in 1986 tax increments will pay \$100,000 of these costs).

7. DETERMINING THE LEVEL OF TIF SUBSIDY

While it is worth asking whether cities over-subsidize developments, answering this question is extremely difficult. Such determinations are best made on a case-by-case basis through a review of development proposals. This kind of review was beyond the scope of our study. However, we did examine the general views of cities on the topic of development subsidies.

Our discussions with cities revealed a variety of city approaches to development finance, particularly land write-downs. Cities sometimes provide developers with write-downs to compensate for clearance or soil preparations at the development site. But it is more common to see land write-downs provided as a business subsidy, not merely to compensate for land preparation costs.

Cities determine the amount of TIF subsidy in various ways. Some city officials believe developers will only be interested in land if it is sold at the fair market value of cleared land. These officials think that writing down land costs to the value of cleared land helps a city make an offer that is competitive with those of other cities. A second point of view is voiced by those city officials that question whether such a write-down is always necessary. They argue that the developer's financial status should be a prime consideration when determining the level of subsidy. Intensive developments may generate high returns on investment, necessitating lower subsidies than less intensive projects.

A third point of view on subsidies was reflected by those cities that determined their subsidy by calculating the tax increments generated by the development. Several cities believe that developments "pay their own way" if the subsidy is no greater than the tax increments generated by the development.

Cities also differ in their approach to assessing properties for public improvements. While some cities try to minimize their TIF use through assessments, other cities see less need to assess if a development's tax increments cover the city's expenditures. Some large TIF projects involve no property owner assessments, such as Annandale's planned construction of a \$715,000 well and storage tank to benefit an industrial park. In Bloomington, the city's policy is that properties will not be assessed for public improvements such as new sewers if the properties have already been assessed for sewers at some point in the past.

C. THE "BUT FOR" TEST

When local governments create tax increment districts, state law requires the governing body to make several findings. Perhaps the most important finding is the "but for" test:

That the proposed development or redevelopment, in the opinion of the municipality, would not reasonably be expected to

occur solely through private investment within the reasonably foreseeable future and therefore the use of tax increment financing is deemed necessary.⁴

The "but for" test is intended to serve two primary purposes. First, the test is intended to encourage the use of tax increment financing as a tool of last resort rather than first resort. Through prudent use of TIF, local governments would avoid excess subsidization of private development. Second, and more important, the "but for" test is supposed to provide some protection for the financial interests of jurisdictions other than the city (particularly the county, school district, and state). If tax increment financing induces worthwhile developments to occur that otherwise would not have occurred, then these jurisdictions may have little to lose by permitting assessed values to be frozen. In fact, these jurisdictions will ultimately benefit when the property returns to the tax rolls at higher assessed values. However, if cities use tax increment financing for developments that would occur without TIF, then counties, school districts, and the state forego tax revenues that they otherwise would receive.

State law currently implies that meeting the "but for" test is sufficient evidence of the need for a tax increment district. When a municipality finds that development will not occur solely through private investment, the law states that "therefore the use of tax increment financing is deemed necessary." This implies that TIF makes sense provided the district meets the "but for" test. Given this prominent role of the "but for" test in the statutes, an important TIF issue is: To what extent does the "but for" test protect the public interest? In the sections that follow, we examine this issue in greater detail.

1. ESTIMATING OF PUBLIC COSTS AND BENEFITS

The principal shortcoming of using the "but for" test as sufficient evidence of the need for public financing of development is that:

- The "but for" test provides no indication of the public costs and benefits of a subsidized development.

Two examples illustrate the point. Eden Prairie spent \$18 million to build a ring road system near the intersection of three major highways. The existing highway configuration was confusing and provided inadequate access to properties in the area. It probably is true that intensive development of this area would not have occurred without changes in the road system. Nevertheless, it is worth asking whether the benefits of this project are worth the cost. The office and commercial developments in Eden Prairie's seven tax increment districts might have located elsewhere in the region (perhaps at sites requiring fewer public expenditures) had they not located at the Eden Prairie site. Thus, while Eden Prairie's

⁴Minn. Stat. §273.74, Subd. 3(b). The term "but for test" comes from the notion that but for TIF the development would not occur.

districts may have met the "but for" test, the districts are more debatable on a cost-benefit basis.

In Virginia, the city established a redevelopment tax increment district at the site of a parking lot, and the city council determined that development would not be possible without TIF. The city provided a \$600,000 write-down to the site's developers, one of the largest write-downs we found outside the Twin Cities metropolitan area. Developers built an office building at the site. While the city council's "but for" determination may have been correct, the more fundamental question is: Do the benefits stemming from redevelopment of the parking lot justify a \$600,000 write-down?

As these examples suggest, the "but for" test alone does not ensure the wise expenditure of public dollars. Only by a more rigorous consideration of the costs and benefits could one determine whether TIF makes sense in cases such as these. Weighing the costs and benefits of development projects is difficult and often subjective. Furthermore, the benefits that a development provides to a city may differ from, and often exceed, those it provides to a county or the state. However, a review of costs and benefits should be a part of TIF project evaluation, one that is no less necessary than meeting the "but for" test. The "but for" test, while a unique and important part of the Minnesota tax increment financing law, cannot by itself guarantee protection of the public interest.

2. DIFFERENT INTERPRETATIONS OF THE "BUT FOR" TEST

As with any state requirement, the usefulness of the "but for" test depends on its clarity, its conciseness, and the consistency with which it is applied. In our visits to 44 cities, we examined local applications of the "but for" test. It is clear that:

- Existing law permits cities to interpret the "but for" test in a variety of ways.

Figure 2.3 shows seven ways in which the "but for" test is open to interpretation. Given the variety of interpretations available, it is difficult to imagine a development that would not meet the "but for" test in some sense.

For example, the "but for" test is open to interpretation with regard to the "quality" of the development. Coon Rapids considered several proposals for a low/moderate income housing project, some of which would not have required public assistance. But the city selected a proposal for development with features that would not have been possible without TIF (e.g., swimming pool, underground parking). Thus, "but for" TIF, a development of this quality would not have been possible.

Some cities meet the "but for" test by finding that TIF permits faster, more intensive development of sites than would occur without TIF. For example, the construction of Interstate 394 west of Minneapolis certainly will spur new development. However, Golden Valley city officials believe

FIGURE 2.3

VARIOUS INTERPRETATIONS OF THE "BUT FOR" TEST

The "But For" Test is Open to Interpretation With Regard To:	Examples
(1) The geographic area it pertains to	A city makes a finding that development of a grocery store will not occur at Site A without tax increment financing. Would the store develop elsewhere in the city without TIF? Elsewhere in the county? Elsewhere in the state?
(2) The timing of the development	Site B is a prime parcel of land that several developers are interested in. However, the developers say that, without TIF, they cannot afford to build at this site for several years. But for tax increment financing, would development occur "in the reasonably foreseeable future?"
(3) The scope of the development	Next to a major highway, commercial development will occur at Site C without TIF. But the city prefers development of a more intensive, high-rise office building at the site. Does this site meet the "but for" test?
(4) The quality of the development	Development of a housing complex could occur at Site D without public assistance. The city wants the development to have better construction and extensive landscaping, which will increase costs beyond what the developer can privately finance. But for TIF, the development quality would be lower.
(5) The availability of financing other than TIF	Site E requires sewer and street improvements. The city decides to write down all sewer construction costs with TIF, and the developer pays no assessments. The city could use municipal state aid highway funds for the street work needed, but TIF funds are used instead. Without TIF, would development of this site have been possible?
(6) "Secondary" TIF developments	A city establishes a tax increment district at Site F, which is developing without public assistance. The city wants to capture increments from Site F to use for a land write-down at Site G. Site G is in the project area but not in the district. Without TIF, Site F would have developed; without TIF, Site G would not have. Does this district meet the "but for" test?
(7) Public Improvements	A private development occurs without TIF assistance in a tax increment district. The city established the district because it felt that but for the captured increments, sidewalk improvements on nearby properties would not occur. Should the "but for" test apply to public improvements rather than the development that generates the increments?

that TIF will facilitate more intensive development of the area in the next four years. Golden Valley determined that redevelopment of the desired intensity would not occur in the foreseeable future without TIF.

Three of the interpretations in Figure 2.3 (interpretations 1, 6, and 7) raise especially important policy issues. Interpretation 1 suggests that it is not clear which geographic area the "but for" test applies to. For example, a city could find that a restaurant will not develop at a particular site or in the city as a whole without tax increment financing. From the city's perspective, the restaurant meets the "but for" test. However, taxing jurisdictions other than the city have a financial stake in the district's creation. The state, county, and school district do not want to subsidize developments that will occur within their boundaries without subsidies. Applying the "but for" test from these jurisdictions' perspectives may result in a different "but for" finding. Without tax increment financing, this restaurant or one like it would likely be built elsewhere in the county or state. From these broader perspectives, TIF may result in no net job creation or tax base additions. We discuss this issue further in part 4 of this section.

Interpretation 6 and 7 of Figure 2.3 also raise serious policy issues. Some cities create tax increment districts to capture the taxes of development that is occurring without public assistance. These cities then use the tax increments to finance later business developments or public improvements. We discuss this issue in the next section.

3. "CAPTURING" DEVELOPMENT THAT WILL OCCUR ANYWAY

Traditionally, literature on TIF describes this financing tool as an inducement to business development and a means of leveraging site activity. However, our study revealed that many cities use TIF to capture (not induce) new development, thus creating a supply of funds for later projects. In such cases, taxes that otherwise would go primarily to counties and the state instead remain with cities. While state law does not expressly prohibit this, the practice appears contrary to the spirit of the "but for" test.

Two provisions of the tax increment financing law facilitate this "capturing" of development and appear to run counter to the purported intent of the "but for" test. First, state law permits cities to include parcels in tax increment districts on which cities have issued building permits within the three month period prior to district certification.⁵ The rationale for this provision is not entirely clear, but some people suggest that city consideration of tax increment district establishment may itself induce some development before the district is formally created. However, this provision may defeat the purpose of the "but for" test since it also permits a city to create a tax increment district after learning that construction will occur. Thus, a city could capture the tax increments from the non-induced development for which the building permit was issued and use the tax increments for other purposes.

⁵Minn. Stat. §273.76, Subd. 4.

A second set of statutory provisions that can act counter to the "but for" test are the blight criteria for redevelopment districts. State law does not require that conditions of blight exist on all parcels of land in a tax increment district. As a result, some portions of a district may include non-blighted land that has no barriers to development. Furthermore, since 1979, cities have been permitted to establish non-contiguous districts. Thus, it is possible for cities to draw district boundaries that include developable, non-blighted sites (which may not meet the "but for" test) that are geographically separate from the blighted sites.

It is difficult in many cases to determine definitively whether a district meets the "but for" test. However, from interviews with city officials it was apparent that:

- More than one-third of the cities we visited created at least one tax increment district to capture taxes from developments that would have occurred without TIF.

The extent of this "capturing" in these cities varies widely. In some cases, most of the district met the "but for" test, but the city chose to add one or two parcels to the district that it knew would develop without TIF. In other cases, the entire district consisted of a development that would have occurred without TIF. Listed below are examples of cities that placed developments not requiring TIF assistance in a tax increment district as a means of generating revenues:

- *Shakopee.* The city knew that four downtown businesses were planning renovations (without TIF) and created a non-contiguous district to capture increments from the four businesses. While some of the increments financed a parking lot next to one of the businesses, most of the increment is now available for more general downtown uses.
- *Dodge Center.* The city modified one district to capture increments from a bank built without public assistance and used the increments for general downtown improvements. Dodge Center also created a district to capture taxes from a business known to be planning an expansion and intends to use the increments for airport renovation.
- *Glencoe.* A 16-unit housing development occurred without TIF assistance; the city created a district at the site, captured the taxes, and used them to subsidize a grocery store. The city also captured three businesses' taxes in this manner for later use as development subsidies.
- *Bloomington.* The city's current practice is to create a new tax increment district in the large Airport South project area each time a new building permit is issued. Several of these developments occurred on prime land without TIF assistance. Bloomington has not decided how to use the increments it gains, although the city expects to eventually use the funds for public improvements in the project area and for subsidies to the

proposed mega-mall at the previous site of the Metropolitan Stadium. Elsewhere in the city, Bloomington established a district to capture taxes from an office development that received no TIF subsidy. The tax increments paid for a traffic bridge and a pedestrian bridge.

- *New Prague.* A bank located at a downtown site without TIF assistance, and the city captured the increments by placing the bank site in a tax increment district. The increments will fund street or alley improvements in the downtown area.
- *Savage.* The city has a large district south of Highway 101. Savage drew its tax increment boundaries to include one area north of Highway 101, where the city knew of plans for construction of a grain elevator. The elevator received no TIF assistance.
- *Eden Prairie.* The first five districts created by the city helped finance a ring road system, and it is probably true that the ring road made these developments possible in the area. However, the city created two additional districts to generate revenues for early retirement of the road's bonds. These developments (and the road) would have occurred without creation of the latter two districts.
- *Proctor.* An outdoor advertising firm moved from Duluth to Proctor without TIF assistance. The city created a district to capture these taxes for use in a road and bridge project.
- *Hibbing.* In addition to including parcels in the downtown district that the city considered blighted, Hibbing placed several sites in the district on which development was occurring.
- *Blaine.* The city created two economic development districts at the same time: one district included several parcels on which development was occurring (but not yet on the tax rolls), and the other district included sites where there was no development. Blaine used revenues from the developing district to subsidize development in the undeveloped district.
- *North Branch.* When a law firm bought and rehabilitated a downtown building, the city placed the site in a tax increment district to capture the increased taxes. Similarly, the city placed a housing development in a district to capture taxes. Tax increment financing induced neither development, although some minor TIF expenditures occurred at the sites.
- *Marshall.* A housing project developed without TIF assistance. The city placed the site in a district, captured the taxes, and the funds will help build a new city park one mile away.

- *Princeton.* In Princeton's industrial park district, the city included the site of a newly-constructed building (financed with a UDAG, not with TIF). In Princeton's 1978 downtown district, the city drew TIF boundaries to capture increments from an apartment complex completed shortly before the district's creation.
- *Mountain Iron.* Developments in the city's first tax increment district occurred primarily because of a state grant, not because of tax increments. The city created and modified the district to capture taxes from these new businesses, which will finance future business inducements or public improvements outside the boundaries of the current district.
- *Mendota Heights.* Included in the city's tax increment district was a pre-existing business park. While the park was in an airport restriction zone, this served as no real barrier to the park's development. The city used some TIF funds to upgrade a road in the business park at the county's request, but the road was not a prerequisite to further development of the business park. The businesses attracted to the park received no TIF subsidies, and the city will use the increments for assessment write-downs outside the existing business park.

All of the above examples (except for one of the Princeton districts) occurred in districts established since 1979, the year the Tax Increment Financing Act took effect. The laws prior to 1979 required no formal "but for" finding. Still, the practice of capturing development that would occur anyway had the same effects on taxing jurisdictions before 1979 that it has now. What follows are several examples from our sample of tax increment "capturing" in districts established prior to the 1979 legislative changes:

- *Annandale.* The city's 1978 tax increment plan refers to the opportunity to capture taxes from recently-completed developments. Much of the city's captured assessed value comes from developments not related to tax increment expenditures.
- *Virginia.* The city created a district to capture increments from a Section 8 housing project under construction at the time (it required no TIF). Virginia uses these funds for redevelopment of residential areas. In another TIF district, the city included several privately developing properties in the district boundaries to create a funding source for a city recreation complex.
- *Cottonwood.* Most of the city's captured assessed value comes from a bank that privately constructed a new building shortly after Cottonwood created its tax increment district. City officials knew of the bank's plans at the time the site was placed in the district.

These cases represent the clearest examples we found of developments that would have occurred without tax increment financing. There are other

cases in which the "but for" findings were more subtly questionable. For example, some city officials established districts on land they felt was very likely to develop, even though no development agreements were in hand. Other cities used inducements other than TIF to develop large portions of tax increment districts. An example of the latter is St. Paul's scattered site housing district, which includes 18 sites. The city induced development at 15 of the 18 sites using subsidies other than TIF; one of the other three sites required only minor TIF assistance.

In light of the examples given, it is clear that a key issue regarding the "but for" test is: To what "developments" does the test apply? Many cities do not apply the test to the initial developments that generate revenue. Instead, these cities interpret the "but for" test as shown in the following two examples:

- "But for the use of tax increments from this development that would have occurred anyway, our city could not have replaced downtown sidewalks."
- "But for the use of tax increments from this development that would have occurred anyway, our city would not have revenues to use for later business inducements."

The Legislature needs to consider whether the "but for" test should apply to: (1) the initial development generating the tax increment, 2) developments funded with earlier developments' tax increments, or 3) general public improvements financed with tax increments. The latter two interpretations raise important policy questions and may enable cities to circumvent state levy or bonding limits. If a city captures taxes from a development that will occur anyway (using the increments for later business inducements or public improvements), other public jurisdictions (particularly the county and the state) fail to receive tax dollars they otherwise would have received. By permitting this "capturing" of new development, the state may encourage unproductive competition among cities. Cities that capture "non-induced" developments in tax increment districts will benefit (by having an unbudgeted source of funds for later projects), while those cities that show restraint in their use of TIF will be less able to offer inducements to prospective businesses.

The capturing of tax increments for general public improvements is of somewhat greater concern than the capturing of increments for future development inducements. Clearly, the promise of land write-downs, demolition, adjacent street improvements, and other activities at the development site can induce development. But the relationship between development activity and general improvements such as the following seems more tenuous:

- Replacement of downtown sidewalks.
- Replacement of downtown lighting.
- Routine street paving projects.
- Replacement of storm sewers in a large part of a city.

- Improvement of existing city parks.

In a time of tight budgets, it may always be possible for a city to claim that "but for" TIF these improvements would not occur. Nevertheless, many cities budget for such activities and assess for them where possible. Tax increment financing is a convenient means of obtaining county and state support for general public improvements that city taxpayers and benefitted property owners would otherwise have to finance entirely.

4. GEOGRAPHIC PERSPECTIVES ON THE "BUT FOR" TEST

As discussed earlier, the "but for" test is subject to many interpretations (see Figure 2.3). One of the most important areas of interpretation is the geographic area to which the "but for" test applies. The following sentences illustrate several possible interpretations of the "but for" test:

- "But for TIF, this development would not have occurred at this site in the tax increment district."
- "But for TIF, this development would not have occurred in this city."
- "But for TIF, this development would not have occurred in this county."
- "But for TIF, this development would not have occurred in this state."

Clearly, fewer developments would meet the latter two interpretations than the first two interpretations. The latter two interpretations represent the perspectives of the county and state, two jurisdictions with strong financial interests in TIF. In other words, it would be more difficult to meet the "but for" test from the state's perspective or the county's perspective than from the city's perspective.

It is important to consider whether TIF results in developments that represent net gains to broad geographic areas such as counties or the state as a whole. To determine whether TIF produces net gains in employment or in tax base from these perspectives, one must consider the types of development subsidized in TIF districts. The appendix presents a district-by-district discussion of the types of developments subsidized in districts we visited. Overall:

- Most TIF developments involve retail, office, or other commercial development.

Typically, the markets for the kinds of commercial development usually subsidized by TIF are competitive on a local or regional basis within a state. For example, if a new subsidized retail store is not built to meet local demand, either people will purchase goods at existing stores or a new unsubsidized store might be built elsewhere locally. From the state's

perspective, using TIF to subsidize additional retail and commercial development is much less likely to result in net employment gains than using TIF or other subsidies to attract footloose firms in the manufacturing or certain service sectors that compete in national or international markets.

Some TIF-financed developments do appear to represent net benefits from the state's perspective. One such example is low/moderate income housing projects, which cities are finding increasingly difficult to induce. Although the occupants of low/moderate income projects would live elsewhere if the housing projects were not available, it is doubtful that many cities could provide adequate housing for these people without public subsidies. A second example of developments that represent net benefits from the state's perspective is certain types of industrial projects. Specifically, districts that induce new firms of this type to Minnesota or that prevent Minnesota firms from leaving Minnesota represent a net employment and tax gain for the state. Some examples from our sample include:

- *Duluth*. The Port Authority used TIF to induce a Canadian cement company to locate a major plant on the Duluth harbor. Recently, the city announced TIF plans for a paper mill that will permanently employ 600 people.
- *Northfield*. The city's two most recent tax increment districts helped induce two industrial locations by firms that were considering locations out of state.
- *Shakopee*. The city used TIF to attract a distribution center for K-Mart that serves nine states.
- *New Brighton*. AT & T will build a regional distribution center with TIF assistance for site work.
- *Marshall*. The city's major employer considered moving its ice cream production plant to South Dakota, but the city will use TIF to help build a new plant in Marshall.

Not all industrial developments represent net gains from a state perspective since some moves by these businesses involve no consideration of out-of-state sites. However, industrial developments are more likely to result in more jobs within the state than the sorts of retail and commercial developments that are more typically assisted by TIF.

Overall, while TIF developments may satisfy the "but for" test from a city perspective, it appears that most developments probably would not meet the test from the state's perspective. Given that the minority of TIF projects result in net state gains in employment, it is important to ask whether TIF projects target state funds to those areas most in need of redevelopment, low/moderate income housing, and economic development. Specifically, one should ask:

- Do the redevelopment projects funded with TIF target the state's most blighted sites?

- Do the housing projects funded by TIF meet the greatest needs at a minimum public cost?
- Do the economic development projects funded by TIF result in maximum net job creation at a minimum public cost?

The next section of this chapter examines the first issue: the extent to which Minnesota's statutory criteria for redevelopment districts target the state's most blighted areas.

D. THE BLIGHT CRITERIA FOR REDEVELOPMENT DISTRICTS

The most common type of tax increment district established by Minnesota cities is the redevelopment district. In the cities we visited, 58 percent of the districts established pursuant to the 1979 Tax Increment Financing Law are redevelopment districts. In 1979, the Legislature gave redevelopment districts maximum lifespans of 25 years, and the Legislature required cities to make blight findings for parcels in redevelopment districts. Figure 1.2 lists the current blight criteria in the tax increment statutes. For those districts which cannot meet the blight criteria (except for those that provide low/moderate income housing), the Legislature imposed a much stricter time limitation. State law limits these "economic development districts" to ten years from the date of the district's creation or eight years from the time the city receives its first tax increments (whichever is less).

During our study, we visited many of the redevelopment districts deemed blighted by cities in our sample. We also examined all redevelopment plans for these cities that were on file with the state. In addition, we requested documentation of the blight findings from most of the cities we visited. From our review of the ways in which cities implement the statutory criteria, we conclude that the Legislature needs to address the major policy issues and technical issues discussed below.

1. GERRYMANDERING

Prior to August 1979, all tax increment districts consisted of parcels of property that were coterminous (identical boundaries) with a development project area. Further, tax increment districts prior to 1979 were contiguous, containing adjacent parcels rather than scattered sites.⁶ Cities often included large numbers of parcels, including entire downtowns, in their tax increment districts. The 1979 Tax Increment Financing Act permitted cities to establish districts that were 1) smaller in size than the project area they were a part of, and 2) non-contiguous (consisting of scattered sites within the project area). In part, the Legislature wanted

⁶One pre-1979 district we are aware of was neither coterminous nor contiguous (Robbinsdale Scattered Site Tax Increment District).

cities to freeze the assessed value of as few properties as necessary into tax increment districts. Also, the ability to establish non-contiguous districts enabled cities to focus on the portions of a project area most needing redevelopment.

However, as discussed in the previous section, cities often draw district boundaries to include properties that will develop without TIF assistance. These may be prime properties or parcels for which building permits have already been issued. Such privately developed parcels become "revenue generators" for other business inducements or for public improvements.

We found that:

- It is possible for a redevelopment district to generate large amounts of tax increments without correcting the blight problems cited by the city when setting up the district.

Several examples illustrate this point:

- *Glencoe*. There are no intentions of using TIF to redevelop the area deemed blighted in the city's most recent redevelopment district. The blighted downtown properties merely helped the city meet the statutory blight criteria. The blighted properties are not geographically close to the parcels that will generate tax increments (a motel and restaurant developed). Glencoe plans to use the tax increments for business inducements in a developing area at the edge of town.
- *Dodge Center*. One of the city's districts has three non-contiguous sites. One site (an expanding factory) will generate tax increments. Another site (an airport) will receive the TIF subsidy. The city has no redevelopment plans for the third area, the one deemed blighted by the city.
- *Mendota Heights*. So far, there has been little redevelopment of the major areas deemed blighted by the city. The city did use TIF for a feasibility study to explore the possibility of connecting certain blighted properties to city services (the nature of the blight on these properties was the lack of city utility services). If the city chooses to provide services to these homes, the work will not be completed for several years. The city's top spending priorities in the first four years of the district have been fire station construction and assessment write-downs for vacant industrial land. The district generated \$234,000 in tax increments in 1985.
- *Brooklyn Park*. The city plans to spend all of the tax increments in its most recent district to upgrade two existing roads. Several of the parcels deemed blighted by the city are along one of the two roads; none of the parcels are along the second. In addition, many of the blighted parcels are not close to either road and will likely not benefit from road improvements.

- *Chaska*. The city created its most recent district primarily to finance flood protection improvements. Chaska met the blight criteria primarily through a building inspector's rating of houses in the district. While the future improvements may remove these houses from a floodplain, the houses will likely still meet the city's blight test when the flood project is built.

These examples point out that, under current law, it is not necessary to address blight problems in order to qualify as a redevelopment district. The ability to establish non-contiguous districts and to include non-blighted land in redevelopment districts facilitates this problem.

2. THE DEFINITION OF BLIGHT

In 1979, the Legislature placed "objective" blight criteria for redevelopment districts in state law (in particular, note the first three criteria in Figure 1.2) However:

- State law permits extremely flexible city interpretations of the blight criteria. Using the least restrictive interpretations of blight that we encountered in our study, most property in the state could qualify as "blighted."

For example, Hutchinson determined that 166 of 184 downtown buildings were blighted because they did not meet current housing, fire, or building codes. Several other cities in our sample cited code violations as evidence of blight. Given the frequency with which such codes change, these results could probably be expected in most Minnesota cities.

A more commonly used interpretation of blight is "inappropriate" or "incompatible" land use.⁷ In some cases, this includes land uses that are out of conformance due to zoning changes enacted since the structure was built. In other cases, it may mean that the city has a preference for more intensive land use than currently exists.

For example, Golden Valley city officials consider greenhouses to be an inappropriate land use for their suburb. Greenhouses are land-intensive and generate few property taxes. The city is using TIF to acquire and relocate a greenhouse (out of the city) to make room for a high-rise office/residential development.

In Golden Valley's redevelopment district adjacent to the future Interstate 394, most of the blighted properties qualified on the basis of problems such as the following: lack of landscaped setbacks, too much parking in front of buildings, and outside storage of equipment. In general, Golden Valley's objective is to replace current structures on this prime land with more intensive uses.

⁷Typically, cities use "inappropriate use" or "incompatible use" as evidence of blight when employing the second blight criterion listed in Figure 1.2. With this criterion, 30 percent of the parcels may be deemed blighted in this manner.

Other cities use TIF to implement similar local planning preferences. Some cities consider car dealerships and lumberyards to be inappropriate downtown land uses and have used TIF to relocate these businesses elsewhere in the city. Some cities believe that certain types of businesses are so unattractive (e.g., asphalt plants) that they do not want such businesses anywhere within the city.

We think the Legislature should reassess the blight criteria currently in statute. Specifically:

- Some of the blight definitions are unclear or subject to a variety of interpretations.

For example, state law does not define the key phrase "requiring substantial renovation" that appears in two of the criteria. Also, cities document the physical deterioration of buildings in different ways, ranging from building inspector surveys to "windshield surveys"⁸ to code violations.

In addition:

- There is a need to reconsider the extent to which conditions such as "non-conforming land uses," and "inappropriate land uses" constitute blight.

Reasonable arguments can be made for the inclusion of these notions of blight in the second redevelopment criterion. However, considering how these notions are sometimes used by cities, their inclusion may be an impediment to effective targeting of TIF use to the most blighted areas of the state.

3. POOR SOILS AS EVIDENCE OF BLIGHT

The third criterion listed in Figure 1.2 permits raw land to qualify as a redevelopment district because of unusual terrain or soil deficiencies. The statutes attempt to apply an economic test to determine whether raw land should qualify as a redevelopment district due to soil problems. The statutes require that 80 percent of the land has a fair market value which, when added to the cost of preparing that land for development (excluding the costs of streets and utilities), is greater than its anticipated fair market value after soil problems have been corrected.

We found many cities using the "poor soils" criterion. Coon Rapids used the criterion to qualify its six most recent redevelopment districts. Other cities we visited that use this criterion include Roseville, Fridley, New Brighton, Savage, Winona, Mankato, Mountain Iron, Marshall, Hutchinson, Blaine, and New Prague.

⁸Some cities use "windshield surveys," which are structure ratings done from a vehicle.

Cities have used the third criterion to qualify districts with a wide range of soil problems. These districts include ones with relatively minor soil problems, as well as districts requiring very costly soil corrections to prepare them for development.

We think there needs to be a reexamination of the third criterion for several reasons. First, the economic test does not provide an effective way to determine when soil problems are so costly that a city should be permitted to establish a 25-year redevelopment district instead of the shorter economic development district. Some districts qualifying under the third criterion have soil problems that are minor. The problems are comparable to soil problems encountered in some economic development districts we examined and some private development.

Second, it may not be economical to use TIF to correct major soil problems in some cases. In areas where developable land that requires lower soil preparation and infrastructure costs is plentiful, it does not make sense for the state to encourage costly soil preparation by cities. According to Metropolitan Council staff, there is an abundance of developable industrial land in the Twin Cities metropolitan area.⁹ In some instances in the metropolitan area, major soil corrections have been also accompanied by major infrastructure costs (such as streets and utilities). In those cases, it may have been preferable to permit development to occur on area sites that are less costly to develop.¹⁰

4. TECHNICAL ISSUES

In addition to the policy issues raised in the preceding sections, we think the Legislature should consider two technical issues related to the TIF blight criteria. First, we found that:

- City documentation of the blight finding is sometimes poor.

State law requires cities establishing tax increment districts to 1) make a finding as to the type of district created, and 2) "set forth in writing the reasons and supporting facts for each determination."¹¹ While cities always make the blight finding when establishing redevelopment districts, some cities provide no supporting facts in the tax increment

⁹There is some discussion of this issue in *Industrial Parks In The Twin Cities Metropolitan Area, 1960-1983*, published by the Metropolitan Council in March 1984.

¹⁰In addition, in the Twin Cities area, the fiscal disparities law partially compensates communities with physical barriers to development. The fiscal disparities law "redistributes" new commercial/industrial tax base among metropolitan taxing jurisdictions. The effect is that cities experiencing new growth share tax base with cities experiencing less growth.

¹¹Minn. Stat. §273.74, Subd. 3.

plan or elsewhere. Thus, it is sometimes difficult for outside observers to know which properties a city deems blighted and what problems these properties have. The Legislature should consider ways of assuring better documentation of blight by cities.

A second technical issue is that:

- Measurement of blight on a parcel basis sometimes permits large areas of undeveloped land to be part of redevelopment districts.

Under either of the first two blight criteria, at least 70 percent of the parcels in a redevelopment district must be occupied by buildings, streets, utilities, or other improvements. No more than 30 percent of the parcels can be raw, undeveloped land. However, if the undeveloped parcels are large relative to the other parcels in the district, more than 30 percent of the district's acreage could consist of undeveloped land. For example, the city of Chaska has a redevelopment district that consists of 40 percent vacant industrial land. The vacant land, however, occupies less than 20 of the district's 833 parcels.

Other anomalies can also result. In Bloomington, a 40-acre farm qualified as a redevelopment district (the Kelly Tax Increment District) in 1985. The district is a single parcel with a partially-burned farmhouse. Because of the deficient structure, Bloomington deemed the parcel blighted and in need of redevelopment. Clearly, however, clearance of the farmhouse provides no serious barrier to development of this large site. The site will be part of Bloomington's mega-mall development near the old Metropolitan Stadium site.

Generally, the use of TIF for predominantly raw land has been reserved for economic development districts which have a shorter life than redevelopment districts. As a result, the Legislature may wish to consider whether a district with a large amount of raw land should be able to qualify as a redevelopment district.

E. ACHIEVEMENT OF PUBLIC OBJECTIVES

As noted earlier in the chapter, cities create tax increment districts for a variety of reasons. Cities often establish single districts to achieve multiple objectives. In addition to city objectives, the state also has public objectives in tax increment districts. The most obvious three objectives are redevelopment of blighted areas, creation of low and moderate income housing, and economic development. While an in-depth evaluation of the achievements of tax increment districts was beyond the scope of our study, the following discussion highlights some general findings and issues.

1. REDEVELOPMENT DISTRICTS

We found that redevelopment districts have often helped municipalities enact local planning preferences and they have often provided tangible local benefits. While these benefits sometimes come at sizable costs, it is important to consider the variety of redevelopment benefits experienced in cities.

Among the most noteworthy examples of redevelopment are those that result in historic preservation. Winona has used TIF for several such projects: restoration and re-use of a hotel, a warehouse, and a depot. Prior to creation of the tax increment districts, these Winona landmarks sat vacant.

We saw other cases in which TIF provided a timely tool to address a small town's unforeseen problems. For example, a downtown fire in Aurora destroyed the region's only drug store; TIF helped to relocate the store downtown.

Sometimes TIF has turned junkyards into productive land. A former New Brighton junk storage area now contains 127,000 square feet of office/warehouse space.

Several cities have used tax increment financing to redevelop entire blocks of a downtown area. Examples of this include Minneapolis, St. Paul, Duluth, Princeton, and Buffalo.

Many cities receive significant social benefits from TIF developments. In Rushford, there is considerable city pride in the redevelopment of old portions of downtown and in the newly-constructed bowling alley.

Redevelopment brings energy savings to some cities. Aurora, Zumbrota, and Glencoe all replaced existing street lights with sodium vapor lights. Many TIF projects replace energy-inefficient buildings with more efficient buildings.

In a few instances, cities have already paid off bonds and terminated districts in which redevelopment has occurred. In Buffalo, a 40-unit condominium replaced some dilapidated homes; the city decertified the district just four years after its creation. In Northfield, two single family homes are on the tax rolls several years after they replaced an old warehouse. Mankato decertified a 1975 district in 1982 after soil corrections induced the development of a distribution center.

While there is considerable business activity in many redevelopment districts we visited, some districts (or parts of districts) have not produced the intended benefits. For example, Chanhassen established a district in 1977 primarily to redevelop its downtown area. However, redevelopment of the central business district has not occurred. Redevelopment of the old Androy Hotel was a major goal when Hibbing created a redevelopment district in 1979. The city is still trying to redevelop the site today.

As noted in the previous section of this chapter, some cities have not targeted the blighted parcels in redevelopment districts for improvement. Further, in those cities using code violations as evidence of blight, it is unlikely that these problems will ever be fully eliminated. Thus, it is possible for the conditions that permitted the district to meet the blight criteria to persist years into the district's life--perhaps indefinitely.

In several cities, redevelopment of blighted areas has occurred, but not as a result of TIF. For example, all redevelopment in certain Shakopee, New Prague, and Fridley districts occurred privately, without TIF expenditures.

In some redevelopment districts, TIF provides greater benefits outside the district boundaries than inside the district boundaries. This is the case in Proctor (where construction of a new bridge will provide limited benefits to those properties now in the tax increment district) and Mountain Iron (where the city corrected soil and access problems in the district with state funds, not TIF funds).

Finally, we note that redevelopment of one site may contribute to blight elsewhere. Most of the redevelopment districts we saw were attracting retail and office developments. But office and retail tenants attracted to new buildings create vacant spaces elsewhere. In the Twin Cities metropolitan area, new office buildings tend to have low vacancy rates, often attracting tenants from older offices. In Hibbing, an auto dealership left a vacant downtown building behind to locate in a tax increment district. In Hutchinson, a new shopping mall (which received a minor TIF subsidy) threatened the viability of the city's downtown, causing Hutchinson to spend tax increments to improve downtown parking. In Buffalo, a TIF-subsidized grocery store studied personal checks received from customers and found that the new store is attracting more shoppers from Minnesota towns outside of Buffalo. Thus, the growth of retail businesses at one location may come at the expense of businesses elsewhere. In some developments, it is worth asking whether blight was simultaneously being eliminated in one place and created in another.

2. HOUSING DISTRICTS

Most of the housing districts we examined received housing subsidies from the federal or state government. Because of this, a portion of the home buyers or renters in most tax increment housing districts were subject to income guidelines established by federal or state authorities. Tax increment law requires that a portion of the units developed in housing districts be intended for occupancy by persons with low or moderate incomes.¹²

¹²The Tax Increment Financing Act does not indicate what portion of units should be available for low/moderate income housing. That is left up to various federal and other state statutes.

In the 20 housing districts we visited, about 1,300 units of new housing have been built as a result of TIF, and plans for these districts call for the construction of 1,800 more units. In addition, some large housing developments have occurred in some redevelopment and pre-1979 districts, such as a 200-unit complex for elderly citizens in a 1978 Golden Valley district.

We also found that TIF did not stimulate the housing developed in three of the 20 housing districts we reviewed. Instead, in each instance, a city captured tax increments from a housing development financed by means other than TIF. Two of the cities used the increments exclusively for projects unrelated to the housing development. Specifically:

- *Glencoe.* A Farmers' Home Administration housing development occurred without TIF assistance. The city placed the development in a housing district to capture taxes from the complex. The city subsidized a new grocery store with the increments.
- *Marshall.* A Farmers' Home Administration housing development occurred without TIF assistance. The city captured increments from the development for use in the construction of a city park about one mile from the housing project.
- *North Branch.* A Farmers' Home Administration housing development occurred without TIF assistance, although the city later spent over \$1,000 to gravel an adjacent road. The city placed the site in a district primarily to capture increments for a storm sewer project that later will provide sewers for the housing project and a large developing area of the city.

A fourth city, Winsted, also captured increments from a low and moderate income housing project; there were no TIF expenditures. There is still some chance that the city will use the tax increments in later years to subsidize low or moderate income housing, but Winsted currently expects future housing development to be market-rate. In other words, TIF has provided no low or moderate income housing in the district so far, and it may not do so in the future.

In each of these four cases, the districts do not appear to meet the qualifications required of housing tax increment districts. Had these districts not been declared housing districts, they would have either had to meet the blight criteria imposed on redevelopment districts or accept the shorter lifespans imposed on economic development districts.

3. ECONOMIC DEVELOPMENT DISTRICTS

As we noted in the section on the "but for" test, most of the developments in tax increment districts are commercial or office developments. Developments of this type generally do not have a significant net effect on the state's level of employment. While TIF may induce these developments to locate in particular locations, it is doubtful that TIF can significantly increase the overall demand for office and retail space in the state.

One of the three types of tax increment districts established by the Legislature in 1979 has the explicit goal of fostering "economic development." However, the tax increment statutes for these economic development districts view economic development from the city's perspective. A district which results in increased city employment or an enhancement of a city's tax base is eligible for designation as an economic development district, according to state law. Thus, a city can establish an economic development district to promote business development which creates new jobs within the city even if it eliminates jobs elsewhere and generates little, if any, net job growth for the state.

To examine whether economic development districts produce net employment gains for jurisdictions that are geographically larger than the city (such as the county and state), we examined the types of developments financed in economic development districts. Figure 2.4 summarizes the types of developments in the economic development districts we reviewed. Overall:

- Most of the projects in economic development districts were office, retail, or other commercial developments that probably did not generate net job growth for the state.

FIGURE 2.4

ECONOMIC DEVELOPMENT DISTRICTS IN THE STUDY SAMPLE

<u>CITY</u>	<u>TAX INCREMENT DISTRICT</u>	<u>PRIMARY TIF-SUBSIDIZED DEVELOPMENTS</u>
Brooklyn Park	TID 1 and 2	Mainly office and warehouse. Some manufacturing.
Princeton	TID 2	Federal flight service station.
Eden Prairie	TIDs 1-7	One million square feet of office space. Also: commercial, 350+ housing units.
Shakopee	Canterbury Downs	Racetrack.
Fridley	TID 4	Retail mall (no significant TIF expenditures to date).
	TID 5	Office, commercial.
Chanhassen	TID 2	Computer manufacturer, lumberyard, print shop.
Savage	TID 1	Motel, office.
	TID 4	Market-rate housing.

<u>CITY</u>	<u>TAX INCREMENT DISTRICT</u>	<u>PRIMARY TIF-SUBSIDIZED DEVELOPMENTS</u>
Lakeville	McStop TID Air Lake TID Fleet Farm TID	Restaurant, motels. Distribution center. Retail store.
Northfield	Computer Controlled Machines TID Cardinal Glass TID	Manufacturing. Manufacturing.
Faribault	Heselton TID	Bus rehabilitation company, manu- facturing company.
Albert Lea	North Bridge TID	Retail mall.
Mankato	Willard Street TID Chesley TID HyVee TID Inn Towne TID Union School TID Tow TID South Broad Street TID	Market-rate housing. Truck sales/service company. Grocery, retail. Low/moderate income housing. Office. Distribution center. Office, temporary shelter.
Hibbing	Wood Industrial Park	Chopsticks factory.
Aurora	TID 2	No development.
North Branch	TID 1	Retail mini-mall.
Blaine	TID 1 and 2	Car dealership, manufacturing.
Bloomington	Normandale TID Appletree Square TID Opus TID Bor-Son TID Muir TID VTC TID Homart TID	Office/hotel, Office. Office. Office. Hotel. Computer chip manufacturing. Office/hotel.
St. Paul	Iris Park/Hammond Building TID Waldorf TID	Office. Paper mill.
Minneapolis	Centre Village TID International Market Square TID	Hotel, condominiums, office, bank, ramp Interior design merchandising
Duluth	Miller Hill Mall TID	Retail.

Source: Program Evaluation Division interviews.

The federal government would have located its flight service station elsewhere in Minnesota had it not chosen Princeton. Similarly, a horse-racing track would have been built in another Minnesota city had Shakopee not been selected. Lakeville built a fast food restaurant along Interstate 35 with TIF, capturing tourist dollars that previously went to other southern Twin Cities suburbs. Savage and Mankato built market-rate housing, which clearly would have gone elsewhere in the area had it not been for TIF.

The list includes some businesses that probably did contribute to the state's economic development, notably manufacturing and industrial developments. In Bloomington, tax increment financing, state loans, and state grants are inducing development by a computer chip manufacturer. In Northfield's two districts, firms considering moves to other states opened manufacturing plants. In Faribault, a bus rehabilitation company that does nationwide business constructed a new facility in a tax increment district. And in Hibbing, a chopsticks factory is the city's first tenant of a new industrial park. It is more likely that these districts will result in net employment gains (or the avoidance of employment losses) from a state perspective. Industrial developments also occurred in Brooklyn Park, Chanhassen, Blaine, Eden Prairie, and St. Paul tax increment districts, although some of these developments occurred without TIF assistance.

F. COMPLIANCE WITH STATE LAWS

Our study of tax increment financing was a program evaluation, not a compliance audit. Our purpose for visiting cities was to gain insight into policy issues, not to comprehensively audit cities' TIF finances or their compliance with state law. Nevertheless, during the course of this study, it became apparent that:

- Compliance with TIF statutes may be an important policy issue, and there is evidence that laws are not always strictly observed.

Oversight of tax increment financing practice rests primarily with county auditors, the Office of the State Auditor, and private audit firms. County auditors have the power to certify and decertify tax increment districts. In recent years, the Minnesota Department of Revenue periodically provided county auditors with its interpretations of state TIF statutes, particularly those that affect computations of tax increments. The Office of the State Auditor conducts financial and compliance audits of 10 to 15 cities each year. Private accounting firms audit the rest of Minnesota's cities. In general, TIF audits tend to focus on the accuracy of financial information. Few audits focus on legal compliance issues or assessed value determinations for TIF districts.

We think that some compliance issues need attention. In part, this is due to the statutes' failure to clearly assign responsibility for enforcement. In addition, while county auditors have the authority to certify and decertify districts, it is questionable whether the auditors have enough

knowledge of individual districts and TIF expenditures to enforce TIF provisions.

Perhaps the most important compliance issue relates to the so-called "knock-down provision" of tax increment financing. In 1979, the Legislature mandated that cities may not gather increment on a parcel in a tax increment district for more than five years if "no demolition, rehabilitation or renovation of property or other site preparation" occurred during that time.¹³ In 1982, the Legislature amended the provision, placing a four-year time limit on undeveloped parcels. The provision is designed to prevent cities from capturing inflationary increases in assessed values and from keeping assessed values off county and school district tax rolls.

We found that:

- At least five cities in our sample have districts that should be subject to the knock-down provision but the provision is not being enforced. Some county auditors question whether they have the authority to enforce the provision.

The five cities (and the certification dates of their districts) are:

- Zumbrota (September, 1979)
- Hibbing (November, 1979)
- Winona (October, 1980)
- Rushford (October, 1980)
- Hutchinson (May, 1980)¹⁴

Some county auditors we talked with wondered whether they had authority to intervene in a "legal matter" such as this. Some felt they might not have the clout to enforce such a provision, particularly if it endangered a city's debt obligations. Some county auditors were not familiar with the provision. In one county that has several large 1981 districts, the county auditor has discussed the knockdown plans with the city involved and plans to enforce the provision in 1986.

We think the "knock-down provision" is important, especially since many cities with large districts are now approaching either the four-year limit or the five-year limit, depending on when their district was certified. The following cities in our sample have districts that will reach the limit in 1986: Duluth, Savage, New Brighton, Faribault, Fridley, Winsted, Mendota Heights, Minneapolis, and St. Paul. Duluth is particularly noteworthy; the city has two extremely large tax increment districts (created

¹³Minn. Stat. §273.75, Subd. 6.

¹⁴Hutchinson combined three existing districts (two pre-1979 districts, one economic development district) to form this redevelopment district. City officials told us that they consider their district to be subject to pre-1979 laws. However, Minn. Stat. §273.74, Subd. 4 and Minn. Stat. §273.78 indicate that at least the portions of the district added after August 1, 1979 should be subject to the 1979 laws.

in 1981 and 1983), but redevelopment projects have thus far affected relatively small portions of the districts.

There may also be a need for the Legislature to clarify when the "knock-down provision" becomes effective. For example, Chaska recently created an 833-parcel district, and the city intends to construct flood prevention improvements. Does flood protection constitute "rehabilitation or renovation," which would exempt the affected parcels from the "knockdown provision? The statutes may need clarification.

Another compliance issue that merits attention is the accuracy of original assessed value (OAV) determinations. Proper calculation of the OAV is necessary to assure proper state aid payments and to assure the accurate collection of tax increments by cities. The method of OAV calculation is complicated and has changed over the years. We think there may be problems in the way some OAVs have been computed. For example, a Mankato district (Washington Park) reports a \$0 original assessed value, resulting in a 1985 captured assessed value of \$357,000. Even though the site previously was tax-exempt (it was a vacant hospital), state law requires all tax-exempt properties to be assessed by county auditors on a regular basis and at the time of transfer to private ownership.¹⁵ For districts established after August 1, 1979, counties must use these assessed values when computing the original assessed value of tax-exempt properties. Even the assessed values of streets and alleys must be incorporated into original assessed value determinations. Our review of TIF data and plans led us to believe that other cities may have improperly computed original assessed values. Correcting such problems may threaten the financial viability of some districts.

There are other compliance issues that may deserve attention, and these are noted in Figure 2.5. However, the key issue for the Legislature to consider is whether current statutes provide adequate authority to ensure local compliance with state requirements.

G. PROJECT AREA EXPENDITURES AND TAX INCREMENT POOLING

The 1979 revisions to TIF statutes differentiated between the terms "tax increment district" and "project area." The revisions permitted cities to establish non-contiguous districts within a project area. In addition, cities could establish more than one tax increment district within a single project area. However, the 1979 law allowed cities to spend tax increments only in the district in which they were generated.

¹⁵Minn. Stat. §273.76, Subd. 1 defines the method of determining original assessed value on parcels which transfer from tax-exempt to taxable status. If the county has determined the assessed value of a tax-exempt parcel within one year before the date of transfer, this value should be used as the OAV. If there has been no assessment in the year prior to transfer, the county must make a new assessment.

FIGURE 2.5
POSSIBLE TAX INCREMENT FINANCING COMPLIANCE ISSUES

- (1) The "knock-down provision" (discussed in Chapter 2). Minnesota Statutes 273.75, Subdivision 6 provides that tax increments may not be collected on parcels that have had no development within four years of district certification. We found several districts where the provision has not been enforced.
- (2) Original assessed value (OAV) determinations (discussed in Chapter 2). Minnesota Statutes 273.76, Subdivision 1 and 273.18 establish methods for OAV computation. We found some districts in which the OAV on tax-exempt properties was incorrectly calculated.
- (3) Blight criteria and documentation for redevelopment districts. Minnesota Statutes 273.73, Subdivision 10 outlines the requirements for redevelopment districts, and 273.74, Subdivision 3 outlines the requirements for municipal approval of districts. We found the following problems:
 - Many cities lack documentation of the blight criteria or a description of which criterion was used to qualify the district. In some cases, cities apparently did not make new findings when enlarging the district.
 - Three cities in our sample used more than one criterion to qualify a district.
 - There were some problems in cities' documentation of the "poor soils" blight criterion. Some cities included utility or road costs in the costs of land preparation (the law prohibits this). Two cities qualified districts after finding that the value of land following soil preparations would be less than the value of land before soil preparations, a finding that does not meet the state blight requirements.
- (4) Types of tax increment expenditures. While Chapter 273 contains some restrictions on the use of tax increments or TIF bond proceeds, most of the expenditure restrictions are in development laws, such as the HRA law and port authority law. The legality of some expenditures may require some statutory interpretation. Examples of questionable expenditures that we found include: payment of parking fund debts (Winona); subsidization of free downtown parking (Duluth); using TIF to make business loans (Duluth, Chanhassen, Shakopee, Hutchinson).
- (5) Filing of TIF plans, annual disclosures. As discussed in Chapter 2 of the report, many cities do not file plans or disclosures, as required by Minnesota Statutes 273.74, Subdivisions 2 and 5.
- (6) Maximum district duration without expenditures. Minnesota Statutes 273.75, Subdivision 1 requires that no tax increment be paid to a district unless within three years of district creation the city issues bonds, acquires district property, or causes public improvement construction in the district. We found two districts (created in 1981 and 1982) for which no bonds have been issued and no substantive TIF expenditures have been made.

The Legislature amended state law in 1982 to permit the expenditure of tax increments anywhere within the project area, either inside or outside of tax increment district boundaries. As a result, the 1982 changes authorized what is commonly called "pooling": using tax increments from more than one district to finance a development in the project area. Of the 38 cities we visited that have more than one district, 18 of those cities either employ pooling currently or are exploring the possibility of future pooling.

One way in which cities facilitate pooling is creation of a "master project area."¹⁶ This entails creation of a single project area that encompasses all tax increment districts in the city. As noted earlier in this chapter, some cities have created extremely large project areas in which tax increments may be spent. The entire city of Mendota Heights is in a project area (the city has one district). The entire urbanized portion of Hibbing is in a project area (the city has three districts). All of Robbinsdale is in two project areas (three tax increment districts).

Given the increasing popularity of large project areas and the increasing use of pooling, we think the Legislature needs to consider five issues. Specifically:

- To what extent should the sites that receive TIF assistance be related to the sites that generated the tax increments?
- Should cities be permitted to pool increments from different types of tax increment districts?
- Should there be limits on project area size?
- Is Minneapolis' 1984 refunding of its TIF general obligation bond issues a type of pooling, and does this refunding raise any unique policy issues?
- Are legislative restrictions on "excess tax increments" adversely affected by pooling and project area expansions?

We discuss these issues in the following five sections.

1. "LINKAGE" BETWEEN PROJECT AREA SITES

We encountered several cities in which the pooling of tax increments made possible a public improvement beneficial to more than one district in a project area. Perhaps the best examples are the highway projects in three cities: Brooklyn Park, Roseville, and Eden Prairie. In each case, the highway improvements funded with pooled increments improved the attractiveness of the districts that contributed increments to the pool.

¹⁶The term "master project area" is not a term found in statute.

However, there also may be cases in which the developments receiving pooled increments have little relationship to the districts generating the revenue. For example, Bloomington has not decided how it will use millions of dollars in pooled tax increments generated by office building, hotel and manufacturing developments in the Airport South project area. Bloomington may use the pool for project area storm sewers (not necessarily related to the large developments now generating increments) or it may use the pooled increments for subsidies to the proposed mega-mall.

The issue of using tax increments to finance developments unrelated to the revenue-generating TIF districts is not unique to those cities that pool increments from several districts. To date, the largest expenditure in Mendota Heights' single redevelopment district was for fire station construction, not blight elimination. Glencoe spent funds generated by its housing district to subsidize a grocery store. Tax increments generated by Minneapolis' International Market Square district will be used to provide credit enhancement not only for this district but for several other Minneapolis developments that are in neither the tax increment district nor the project area.

In our view, the problem with not having clear links between the sources of tax increments and the recipients of tax increments is that TIF may be viewed as "free money." Rather than returning tax increment districts to the tax rolls, cities may be tempted to continue funding new "needs" with TIF funds. Tax increment financing may become a convenient financing mechanism that lacks the accountability of budget processes.

2. POOLING BETWEEN DIFFERENT TYPES OF DISTRICTS

We found several cities pooling (or planning to pool) revenues among different types of tax increment districts: Bloomington; Glencoe, Brooklyn Park, and North Branch. Several other cities that do not presently pool have districts of varying types within a single project area. In addition, Minneapolis' refunding of its TIF bonds permits the increments from one type of district to, in effect, pay the debt service of other types of districts.

The issue of pooling between different types of districts is worth considering. For example, given that redevelopment districts must meet blight criteria to be certified, is it right to permit the pooling of redevelopment districts with economic development districts? In effect, such pooling may circumvent the blight criteria by permitting the combination of revenues from blighted and non-blighted parcels. The ability to use redevelopment tax increments in economic development districts may also place the goals of these districts in conflict. While economic development is a worthy objective, some cities may be tempted to spend redevelopment funds for job creation before fully addressing blighted properties in the redevelopment district.

3. THE SIZE OF PROJECT AREAS

In past years, the Legislature has revised tax increment law to encourage cities to have tax increment districts as small as possible. The Legislature made the redevelopment blight criteria somewhat more restrictive, enacted the "knock-down provision," and permitted the establishment of non-contiguous districts.

While the Legislature has tried to restrict the size of the tax increment districts (those parcels that generate the tax increments), there have been no restrictions on project areas (those parcels on which tax increments may be spent). As a result, many cities have established extremely large project areas.

In some cases, cities enlarge project areas to permit the expenditure of financial surpluses in existing tax increment districts. For example, Glencoe had a surplus in its 1975 district. In 1985, the city created a project area that encompasses this district, two other districts, and a large portion of the city. This will provide new flexibility for the expenditure of surplus tax increments. Similarly, Brooklyn Park recently enlarged its single project area to include a 1985 district. The new district will be financed largely with surplus increments from two existing districts.

The Legislature may wish to consider restrictions on project area size and the modification of existing project areas. Such limitations might ensure greater "linkage" between the parcels that generate tax increments and the parcels that receive tax increment subsidies. This may be important if the Legislature sees a need to (1) assure that tax increment district needs receive higher spending priority than project area needs, or (2) prevent the use of tax increments as "free money," available for a variety of city expenditures.

4. BOND REFUNDING

The primary ongoing expense of a typical tax increment district is debt service on general obligation bonds. Needless to say, cities prefer the lowest possible interest rates on bonds in order to minimize the debt service burden. Consequently, many Minnesota cities have refinanced outstanding bonds to obtain lower interest rates.

The 1984 Legislature authorized another type of bond refunding, one that generally is not necessarily designed to help cities obtain lower interest rates. The 1984 law permits a city to issue revenue bonds to refund the principal and interest of outstanding general obligation bonds.¹⁷ Cities may employ this type of refunding if at least one series of the general obligation bonds was originally issued to finance a development district established under Minn. Stat. §472A. Revenue bonds are backed entirely by the tax increments of new development; general obligation

¹⁷Minn. Stat. §472A.06.

bonds are backed by the full faith and credit of the city in addition to tax increments. Because revenue bonds are not backed by the city's taxing power, new revenue bond issues generally carry a higher interest rate at any given time than new general obligation bond issues.

The main attraction of the refunding authorized by the 1984 Legislature is flexibility. For example, some cities are unable to pool tax increments or spend tax increments outside of district boundaries due to restrictive general obligation bond covenants. With the 1984 changes, a city can replace general obligation bonds having restrictive bond covenants with new revenue bond covenants, enabling the city to pool tax increments for the revenue bond's debt service. Thus, a financially-troubled district may have its share of the city's debt service paid by tax increments from any of the refunded districts (thereby permitting the troubled district to use its increments for new project expenditures rather than debt service). In effect, this 1984 law permits cities to use tax increments from a successful district to subsidize expenditures in another tax increment district (and perhaps in another project area) to a certain extent. This type of refunding is, therefore, a type of tax increment pooling that is in some ways similar to the pooling employed by cities with large project areas.

To our knowledge, Minneapolis is the only Minnesota city that has used the 1984 refunding provision so far. In 1984, Minneapolis had 20 tax increment districts for which general obligation bonds had been issued. Some of these districts generated tax increments in excess of their debt service requirements. Two districts generated increments that were insufficient to meet debt service, requiring the city to make up the shortfall through city fund transfers or city tax levies. The bond covenants for many of Minneapolis' districts required tax increments to pay off bonds in the district of origin prior to being used for other expenditures. As a result, Minneapolis could not accomplish what many other cities accomplish through modification of project area boundaries and pooling.

Minneapolis issued a single \$141 million revenue bond to replace an existing \$173 million in general obligation bonds. The tax increments from any or all of the refunded Minneapolis districts can be dedicated to debt service on the revenue bond. In effect, Minneapolis is able to pool increments for the payment of debt service. Tax increments from one district may, in effect, pay for the debt service of another district, even though the districts may be in different project areas.

In addition to permitting tax increments to be pooled for the payment of debt service, proponents of refunding claim several advantages to Minneapolis and other taxing jurisdictions. First, by combining 31 general obligation bonds into a single revenue bond, the city may have enhanced its credit rating. If tax increments are insufficient to meet debt service on the revenue bonds, the city is no longer legally obligated (as it was previously) to levy taxes for debt repayment. Second, those districts that (in effect) have debt service paid by other districts may have more money available for project expenditures than they otherwise would. Third, Minneapolis will use the new funding source to terminate some districts earlier than otherwise would be possible, including the termination of all refunded districts by the year 2003. It is also possible that the refund-

ing might cause a financially viable district (such as downtown's City Center district) to remain in existence longer than it would without refunding since "excess increments" may now be used to fund the debt service of other districts.¹⁸ Fourth, by an agreement negotiated prior to refunding, Minneapolis plans to return a portion of its annual increments to the school district, the county, and the city. Between 1986 and 1990, Minneapolis estimates that at least \$14 million will be rebated to these jurisdictions as a result of refunding. Fifth, the city says that refunding will lessen the amount of bonding needed for future projects. Most cities issue bonds large enough to meet debt service in the early years of a district, when tax increments may be much less than the required debt payments. However, Minneapolis hopes to avoid having to bond for these early expenses by utilizing a "Development Account" that was partially capitalized by the bond refunding. Sixth, the Development Account is a new funding source for future development costs, both inside and outside of tax increment districts. The city will use the Development Account to make loans to some tax increment districts created since the refunding (such as the Conservatory Tax Increment District) and to make loans to some areas not in districts (such as a former tax increment district, Mississippi Courts). Through January 1986, Minneapolis had made about \$7 million in Development Account loans. The city is considering using this account for future neighborhood revitalization projects.

While bond refunding is a unique approach to tax increment pooling, the general policy issues related to refunding are similar to those in cities that have established broad project areas. The primary issue is whether the area generating tax increments should be logically linked to the area receiving the increments. For example, Minneapolis elected officials have the option of using a housing development's tax increments to terminate that district or to pay debt service for a commercial redevelopment district elsewhere in the city. The issue is one of accountability and process. Should funds generated by one development be available to finance unrelated developments? What role should the county, school board, and state have in these decisions? While the city of Minneapolis has established useful guidelines for expenditures from its refunding pool, it remains to be seen whether these guidelines will provide sufficient protection to the other affected taxing jurisdictions. Minneapolis' plans for early district terminations and for rebates to taxing jurisdictions are commendable, but those plans will ultimately be affected by future decisions made at the city level. Further, despite the state's substantial TIF subsidy to Minneapolis districts (in the form of increased state aids), there currently are no plans to provide tax increment rebates to the state.

¹⁸Strictly speaking, City Center's tax increment surplus does not constitute "excess increments" since the Legislature did not define and restrict excess increments until after this district was established. However, City Center does generate more increments than are needed to pay its original debt service and project costs.

5. EXCESS TAX INCREMENTS

As indicated earlier in this chapter, most Minnesota tax increment districts generate sufficient tax increments to meet debt service on bonds. City officials are proud of districts that are financially viable, particularly those districts which are scheduled for decertification prior to the bond term or the statutory life of the district. Districts have been decertified in several cities we visited, but many cities are accumulating substantial tax increment reserves.

The 1979 Tax Increment Financing Act included provisions for "excess increments." Excess increments are tax increments above the amount needed to pay the costs authorized in the TIF plan, including debt service costs. The law provides that excess increments be placed in an escrow account, used to prepay outstanding bonds, or returned to the city, county, and school district in proportion to these jurisdictions' mill rates. This restriction is intended to encourage early retirement of districts or a minimization of district impacts on taxing jurisdictions.

Restrictions on excess increments apply only to districts certified after August 1, 1979. Given that the provision has existed for less than seven years, which is less than the term of most bonds, it is difficult to fully evaluate the extent to which this provision has met legislative intent. However, it is possible to conclude that:

- Tax increment pooling and the establishment of broad project areas weaken the legislative restrictions on excess increments.

Minnesota cities can modify project area boundaries and TIF plans to facilitate the expenditure of excess increments. These modifications may delay the implementation of excess increment restrictions by creating new project costs that are eligible for tax increment subsidies.

While pooling and broad project areas weaken the excess increment restriction, it should be noted that the restriction may not have been particularly strong to begin with. Some cities include long lists of potential costs in their TIF plans, making it difficult for these cities to run out of eligible TIF activities. Other cities describe future project activities in vague terms (such as the generic term "public improvements"), leaving the city with considerable latitude for future expenditures. Unless the TIF plans of cities are specific and realistic, it may be difficult to implement legislative restrictions on excess increments.

H. THE COST OF PUBLIC IMPROVEMENTS

While land acquisition and write-downs are perhaps the most common TIF expenditures, many cities use TIF funds to finance significant public improvements: bridges, streets, interchanges, soil corrections, parks, water wells, public utilities, and others. Figure 2.2 provides examples of cities that have made these improvements.

As noted earlier, some cities consider TIF developments to be prudent so long as the tax increments generated are sufficient to cover the cost of TIF expenditures. In the view of some cities, this situation means that tax increment developments "pay for themselves."

We think that cities cannot determine the appropriate level of TIF expenditures simply by looking at the amount of tax increments a district will generate. Given the size of some public improvement projects financed with TIF, it is worth asking: Are the public improvements financed by TIF necessary, and, if so, at what cost?

As noted in the section of this chapter addressing the "but for" test, some public improvements do little to induce development. For example, while cities may find TIF a convenient means of financing general improvements such as the routine replacement of street lights and sidewalks, in many cases these improvements probably are not strong business inducements. Most cities choose to finance these improvements through the city budget process, not with TIF.

Two other issues merit consideration:

- Particularly in the Twin Cities metropolitan area, should TIF finance development at difficult sites when easier-to-develop sites are available elsewhere?
- Should TIF pay for public improvements that could be assessed?

The first issue is primarily a metropolitan issue due to the high demand for Twin Cities business locations and the relatively good supply of available land in the metropolitan area. Despite the overall availability of land, cities sometimes find it in their interest to make their land more attractive with TIF-financed public improvements. Mendota Heights is developing an industrial area with a high elevation; bringing city services to this elevation is extremely expensive. Thus, Mendota Heights uses TIF to write down special assessments at these sites. Chaska plans to use TIF to finance \$200,000 to \$400,000 in improvements to a future industrial area at the extreme north end of the city. This end of the city is at a high elevation and requires an additional pumping station and utilities. Lakeville spent \$1.3 million to build a water tower, a well, and sewer lines for a fast food/motel development one and one-half miles from existing city services. The development now attracts Interstate 35 travellers that previously stopped a few miles to the north.

Some areas in the Twin Cities metropolitan area have public infrastructure (such as interchanges and sewers) that are underutilized. While it is not possible to force development to occur at sites that developers are not interested in, it is important to consider whether public subsidies for expensive infrastructure and soil corrections make sense when developable sites exist elsewhere in the metropolitan area.

The issue is not solely a metropolitan issue. Mankato built a dike and pumping station so that a fast food restaurant and motel could locate in what previously was a floodplain. Proctor will spend \$1.5 million in tax

increments to build a new bridge on an Interstate 35 frontage road, perhaps opening up some new industrial land in the city. While developments such as these may generate sufficient tax increments to finance these projects, a comparison of costs and benefits should also be an important consideration.

A second issue is whether TIF should finance public improvements that could be assessed to benefitting property owners. Some public improvements (for example, roads and utilities) confer very direct benefits on property owners. Other improvements (such as water towers) confer more general benefits among many property owners. Many cities prefer to assess directly-benefitted properties to reflect the benefits received.

However, in some cases, the availability of TIF provides a convenient substitute for special assessments. In Annandale, the city plans to spend \$715,000 for a well, a storage tank, and water mains for an industrial park. TIF will finance 70 percent of the cost, and the rest will come from water receipts. Although the project will offer substantial benefits to current and future occupants of the industrial park, the city chose not to assess the benefitted properties. In contrast, Eden Prairie financed about 15 percent of the cost of its \$18 million ring road system with special assessments. We found that city special assessment practices vary widely, but there are several cities that financed public improvements in TIF districts without assessments. The use of large TIF special assessment write-downs by some cities creates incentives for other cities to do the same. In our view, the appropriate level of subsidy for a public improvement seems to be something best determined by a careful consideration of each project's costs and benefits, not by the competing business inducements offered by other cities.

I. EXPENDITURES FOR GOVERNMENT BUILDINGS AND PUBLIC PARKS

1. GOVERNMENT BUILDINGS

The 1982 Legislature amended the tax increment financing statutes to limit the use of TIF for municipal buildings. The law states:

No revenues derived from tax increment shall be used for the construction or renovation of a municipally owned building used primarily and regularly for conducting the business of the municipality; this provision shall not prohibit the use of revenues derived from tax increments for the construction or renovation of a parking structure, a commons area used as a public park or a facility used for social, recreational or conference purposes and not primarily for conducting the business of the municipality.¹⁹

¹⁹Minn. Stat. §273.75, Subd. 4.

In our visits to cities, we learned of several cities that have used or are planning to use TIF for municipally-owned or municipally-leased buildings or facilities. These include:

- *Lakeville.* A business expanded onto the site of the city's old fire station. Tax increments from the business are financing part of the cost of the city's new fire station. This development clearly preceded the legislative change.
- *Mendota Heights.* The city established this district in 1981 with plans to use TIF for a fire station. Because Mendota Heights created the district before the 1982 changes went into effect, this district was not subject to the new restrictions. However, the city had not issued bonds at the time of the legislative change (bonds were issued in 1983, and the station was completed in 1985). Elsewhere in Mendota Heights, the city used TIF to write down special assessment costs for a new building owned by the Minnesota Department of Transportation.
- *Coon Rapids.* Prior to enactment of the legislative restrictions, the city created a district with plans for construction of a fire station. Four years after the legislation went into effect, Coon Rapids still has not built the station, and no bonds have been issued. The city still is considering building the station.
- *Dodge Center.* The city plans to use tax increments to upgrade a municipal airport (including a new runway and new lighting). Dodge Center created the district after the legislative restrictions went into effect.
- *Princeton.* The city used \$300,000 in tax increments to help construct a federal flight service station. The city owns the building. The federal government pays \$1 per year to lease the building.
- *St. Paul.* Prior to 1983, St. Paul owned its civic center. In 1983, the city sold the center to private interests and entered into a long-term lease agreement. Tax increments from St. Paul's pre-1979 downtown district will finance 72 percent of the lease payments over the term of the lease (\$123 million). Another ten percent of the lease payments will be funded by interest earnings on TIF funds.
- *Fridley.* In a district established in 1979, Fridley built a garage for police vehicles. The city financed land acquisition and construction with TIF, completing the building in 1985.

Given these examples, we think the Legislature needs to consider three issues related to government building subsidies:

- Should the restrictions on TIF subsidies for municipal buildings be extended to buildings leased or owned by other units of government?

- In addition to the restrictions on municipally-owned buildings, should TIF restrictions apply to buildings leased by municipalities?
- Should the 1982 restrictions apply to cities that have not yet issued bonds for municipal buildings (such as Coon Rapids)? Such cities have no existing debt service requirements that would be jeopardized by these restrictions.

2. PUBLIC PARKS

Six of the 44 cities we visited have used TIF to finance public park improvements, an expenditure allowed by current statutes. The TIF statutes probably permit park expenditures because parks can contribute to the redevelopment and economic viability of developing areas. However, the following TIF expenditures for parks seem questionable:

- *Marshall*. The city captured taxes from a housing district that was occurring without TIF. The city is using these increments to speed up construction of a new city park (not in the tax increment district), which is about a mile from the housing project.
- *St. Paul*. Since Town Square Park was built in 1980 as part of a TIF-financed retail/office development, the city has partially funded its maintenance and operations with tax increments. The 1986 tax increment expense for this purpose will be about \$100,000. St. Paul established another tax increment district (Park Nursery) to finance land acquisition, write-down, and relocation benefits for the purpose of constructing a large housing project. The city is using tax increments from the housing project to make major improvements to an adjacent park. City officials say the new additions primarily serve the larger neighborhood, not the new housing project.
- *Virginia*. The city's sole use of tax increments in one district is completion of a large recreation complex that meets city-wide needs. The city captured taxes from developments that were already occurring in order to finance the improvements.
- *Annandale*. The city used tax increments to purchase park equipment and install lights on a softball field.

These expenditures seem to be the type that most cities finance with city funds or other established sources for park funding. While there may be cases where park development contributes to a city's redevelopment, the above cases appear to be routine expenditures that might best be funded without TIF.

J. TRUNK HIGHWAY IMPROVEMENTS

During the course of our study, we learned of four cities that have made major improvements to state trunk highways using TIF funds. Brooklyn Park, Plymouth, and Minnetonka used tax increment financing to construct new interchanges. Eden Prairie constructed a ring road system encircling several state highways. The total cost of these four projects is about \$32 million. In addition, Shakopee recently reached a tentative agreement with the Minnesota Department of Transportation (MnDOT) in which MnDOT will help finance a bridge project (supplementing federal funds) if the city spends \$1.9 million in tax increments to re-route Highway 101 around the downtown. These projects represent departures from the state's typical practice of financing trunk highway improvements with user fees from vehicle operators.

We think it is important to consider the implications of TIF-financed highway projects. Highway improvements financed by TIF may save the state some highway dollars if those improvements would otherwise have been financed from the trunk highway fund. However, the state bears the following financial risks for TIF improvements: (a) in all cases, the state will reimburse the school district for state education aids lost due to TIF; (b) additions to the state highway system bring with them additional maintenance responsibilities for state crews; (c) if the development could have utilized existing highway access at another site, the state may be saving no highway dollars; and (d) if the improvement could have been funded with federal dollars, the state may not be saving highway dollars.

Counties may also be at financial risk because of TIF-financed highway improvements. Clearly, counties benefit from some highway improvements even though county funds do not ordinarily finance state highways. We see nothing wrong with having a county's share of a new development's taxes devoted to a highway project provided the county considers itself a beneficiary of the improvement. If a business development could occur elsewhere in the county without the TIF-financed highway improvement, TIF deprives the county of taxes it otherwise would receive.

While recognizing the possible financial risks of TIF to the state and counties, we think tax increment financing may be a useful tool for completing highway improvements in developing areas. The highway project selection criteria of MnDOT and the Metropolitan Council sometimes fail to acknowledge the needs of newly-developing areas.²⁰ Thus, it is sometimes difficult to construct adequate highway access to a new area until after the development occurs.

²⁰MnDOT's project selection criteria for highway improvements do not include "economic development" criteria to facilitate new areas of growth. Projects selected by MnDOT and federal projects approved by regional agencies tend to favor improvements to existing infrastructure rather than construction of new infrastructure.

OPTIONS FOR THE FUTURE

Chapter 3

This chapter discusses various alternatives for addressing the concerns raised in Chapter 2. First, based on our findings, we identify the problems needing legislative attention. Second, we discuss the impact that pending Congressional restrictions on the issuance of tax-exempt bonds may have on tax increment financing. Finally, we outline two different legislative approaches to current problems, discuss the advantages and disadvantages of each, and recommend certain legislative actions.

A. ISSUES NEEDING ATTENTION

Tax increment financing has been used productively by many cities in Minnesota to induce commercial and retail development of blighted areas and to help stimulate the construction of housing for low and moderate income persons. In addition, some cities have used TIF to promote the expansion of manufacturing businesses. Not all uses of tax increment financing have been successful in reducing blight, stimulating needed housing construction, or increasing employment in the state. At times, TIF has been used in ways that are inconsistent with the basic intent behind TIF. Among the major problems identified in Chapter 2 are:

- In some instances, cities have established tax increment districts that intentionally *capture* taxes from development that is already occurring rather than *induce* new development. This practice prevents other taxing jurisdictions from collecting taxes they would otherwise receive.
- The statutory restrictions on the types of expenditures that can be financed with tax increments do not prevent a city from using tax increments to pay for general public improvements that are normally financed by special assessments or a city's own funds.
- The "but for" test, which many view as sufficient evidence of the need for a tax increment district, is interpreted by cities in many different ways. The test does not ensure that the public benefits of a project exceed the public costs.

- Increasingly, cities are pooling tax increments among districts or establishing large project areas in which tax increments can be spent. These practices enable a city to spend excess tax increments from an existing district rather than decertifying the district. This weakens the statutory restrictions on the use of excess increments that apply to districts established after August 1, 1979. Furthermore, pooling and the creation of large project areas may encourage cities with pre-1979 districts to use tax increments for new expenditures rather than to retire the districts before August 1, 2009.
- Existing statutes do not require that the tax increments generated within a redevelopment district must be used to correct the blighted conditions that permit the district to be established. As a result, some cities have established redevelopment districts that have done little or nothing to improve the blighted conditions cited as reasons for establishing the districts. Some cities: 1) have established a redevelopment district on the basis of blighted conditions existing on certain parcels within the city, 2) are generating tax increments from other parcels where private development is occurring anyway, and 3) are spending the increments on projects unrelated to the blighted conditions. The permitted use of noncontiguous districts, the lack of an effective "but for" clause, and the fact that not all parcels in a district must be blighted permit tax increment financing to be used in these ways.
- The existing blight criteria that a redevelopment district must meet have been generously interpreted by some cities. As a result, the criteria have not provided a good mechanism for the state to target public subsidies to those areas most in need of redevelopment.
- Several cities have established housing districts to capture tax increments from a housing project being undertaken without assistance from tax increment financing and have not used the increments to induce the construction of low/moderate income housing.
- Some compliance problems exist because there is little state oversight of tax increment financing and because it is not clear who has the responsibility to ensure that cities and counties comply with key provisions of the statutes relating to tax increment financing.

In addition, there is the question of whether tax increment financing results in an excess public investment in development activities. To the extent that cities use tax increment financing to induce retail and commercial development, TIF may only succeed in shifting where that development occurs within the state. This is particularly true in the Twin Cities metropolitan area. A subsidized development that brings more jobs and tax base to one city may ultimately result in fewer jobs and decreased tax base elsewhere in the metropolitan area. Because the direct

effects of tax increment financing (more jobs and tax base in the city using TIF) are easier to see and measure than its indirect effects (fewer jobs and decreased tax base elsewhere in the area), TIF may appear to be creating jobs and increasing the state's tax base when it is not.

There is reason to be concerned about this problem. As observed in Chapter 2, cities have used redevelopment districts primarily, though not exclusively, to induce retail and commercial development. To the extent that TIF's primary effect is simply to shift the location of jobs and tax base, it is important to ask whether TIF targets the redevelopment of those areas that need it the most. Tax increment financing cannot provide maximum redevelopment benefits if it is just as likely to shift jobs and tax base to non-blighted portions of our cities as it is to shift jobs and tax base to blighted portions. The lack of adequate criteria defining blight and the lack of a requirement that tax increments generated within redevelopment districts be used to address blighted conditions are impediments to a reasonable targeting of the use of tax increment financing. It is also worth considering whether local incentives are an impediment to effective targeting. For example, small suburbs may have a greater ability than large central cities to shift the costs of public redevelopment activity to taxpayers outside the municipality.¹ This may be inconsistent with the goal of encouraging TIF use in those areas most in need of redevelopment.

The purpose of economic development districts can also be called into question. According to law, a municipality can create an economic development district consisting of any parcel or parcels of property as long as the district meets one of three criteria: (1) it will discourage commerce, industry or manufacturing from moving to another state, or (2) it will increase employment in the municipality, or (3) it will preserve or enhance the municipality's tax base. The majority of the economic development districts in our sample probably could not have qualified under the first criterion. Most of the districts involved retail, commercial, and other development that would qualify under the second and third criteria. The effect of using tax increment financing for these latter types of development may only be to determine where development occurs, not to cause any significant increase in jobs or tax base within the state. As a result, the use of economic development districts involving retail and commercial development that does not create jobs for the state and does not take place in blighted areas can be questioned. While there clearly is a role for TIF in attracting new businesses to Minnesota and keeping existing businesses in the state, it is worth asking whether the state should encourage (and financially support) districts that do not result in statewide benefits.

¹The smaller a municipality's mill rate as a percentage of the total mill rate and the smaller a municipality's tax base as a percentage of both the county's tax base and the school district's tax base, the greater the percentage of tax increment financing costs that may be shifted to taxpayers outside the municipality.

B. PENDING FEDERAL CHANGES

Most cities using tax increment financing in Minnesota have issued tax-exempt bonds to finance development expenditures. Pending legislation at the federal level, however, would greatly restrict the use of tax-exempt bonds, including those commonly used to finance tax increment districts in Minnesota. The pending legislation affecting tax-exempt bonds is contained in the major tax reform bill passed by the United States House of Representatives in December 1985. Some observers do not expect final United States Senate action on the bill to occur until the summer of 1986. Whether the tax reform bill will become law is uncertain at this time. Its ultimate effect on tax-exempt bonds is also uncertain. However, the probability remains that tax-exempt bonding will be restricted. In any event, cities and states will find it necessary to comply with the provisions of the House bill until Congress and the President take final action.

The House bill would remove the federal tax exemption on bond interest if either: 1) 5 percent or \$5,000,000, whichever is less, of the bond proceeds is used to make loans to persons other than governmental units, or 2) 10 percent or \$10,000,000, whichever is less, of the bond proceeds is used directly or indirectly in any trade or business carried on by any person other than a governmental unit. Since most tax increment bonds are used to finance costs that benefit private development, they would lose their federal tax exemption under this provision of the bill. Only tax increment bonds that finance traditional public activities such as highway and road construction or sewage systems might retain their exemption.

However, the House bill provides some exceptions to this provision. Certain housing bonds, small issue and exempt facility industrial development bonds, certain bonds for nonprofit organizations, and "qualified redevelopment bonds" would retain the federal tax exemption even though they do not meet the 5 percent loan and 10 percent use tests described above. Qualified redevelopment bonds would be the only category under which existing tax increment financing bonds could retain the federal tax exemption.

These exceptions would nevertheless be subject to various statewide volume caps under the House bill. It has been estimated that the Minnesota caps for each category of bonds would be approximately: \$311 million for various types of housing bonds, \$104 million for nonprofit bonds, \$278 million for industrial revenue bonds and student loan bonds, and \$33 million for qualified redevelopment bonds. These caps, except perhaps the one for nonprofit organization bonds, represent significant reductions from estimated usage within Minnesota for 1985. As Table 3.1 shows, an estimated \$800 million in housing bonds and \$621 million in industrial revenue bonds were issued in 1985. The \$33 million cap on qualified redevelopment bonds compares to an estimated \$200 million in tax increment financing bonds that were issued in Minnesota during last year.²

²The estimates of 1985 usage and of Minnesota volume caps were provided by the law firm of Holmes and Graven. In addition, Holmes and Graven provided us with their analysis of the effect of the House bill on tax-exempt financing.

TABLE 3.1

EFFECT ON MINNESOTA OF THE HOUSE WAYS AND MEANS
BILL'S CAP ON NON-GOVERNMENTAL BONDS

<u>Type of Bond</u>	<u>Statewide Cap (In Millions)^a</u>	<u>Estimated 1985 Usage (In Millions)</u>
Housing		
-Multi-family	\$103.75	\$ 600.00
-Single family	103.75	200.00
-State discretion	<u>103.75</u>	<u>-0-</u>
	311.25	800.00
Non-profit Organizations	103.75 ^b	Unknown
Qualified Redevelopment Districts (TIF)	33.20	200.00
Other	278.05	621.00
-Small issue industrial development bonds		
-Exempt facility indus- trial development bonds		
-Student loan bonds		
	<u> </u>	<u> </u>
TOTALS	\$726.25	\$1,621.00

Source: Holmes and Graven.

^aAssumes a Minnesota population of 4.15 million.

^bThis amount cannot be reallocated by the Governor or Legislature to other categories of bonds.

In order to obtain federal tax-exempt status as a qualified redevelopment bond, a tax increment financing bond must meet a number of requirements. These include: 1) all of the net bond proceeds must be used for redevelopment purposes in a designated blighted area, 2) tax increments must be exclusively reserved for debt service on the bonds, 3) a redevelopment plan must be adopted prior to bond issuance, 4) property in the blighted area must not be subject to additional assessments or fees not charged to owners of similar property outside the area, and 5) certain types of property including retail food and beverage establishments, automobile sales and service facilities, recreation and entertainment establishments, and perhaps any new market rate housing cannot be located in a redevelopment area whether or not they are financed by tax increments. In addi-

tion, a designated blighted area must be at least one quarter square mile in area but cannot contain more than 10 percent of the municipality's total assessed value.

The primary effects of the House bill on the issuance of tax-exempt bonds for tax increment financing in Minnesota would likely to be as follows:

- The amount of *tax-exempt* bonds issued in Minnesota for tax increment districts would be restricted to about one-sixth of the current estimated usage.
- The use of tax-exempt bonds would be largely restricted to redevelopment districts. Other types of tax increment districts could not use *tax-exempt* bonds unless the bonds were for general public improvement projects such as the construction of roads or sewage systems.
- Redevelopment districts for which tax-exempt bonds are issued would have to meet a number of federal requirements that are more restrictive than current Minnesota law.

The House bill would not necessarily result in a reduction in tax increment financing activity in Minnesota or in a reduction in the issuance of tax increment bonds. Instead of tax-exempt bonds, municipalities and other authorities could issue *taxable* bonds to finance tax increment financing activities. Because taxable bonds would require a higher interest rate to be paid to bondholders, a higher annual tax increment would be necessary in order to meet bond payments.

However, the difference in interest rates between a taxable bond and a tax-exempt bond is not as large as one might suspect. According to bond underwriters and bond counsel with whom we talked, the difference is between 1.5 and 2.0 percentage points, perhaps up to 2.5 percentage points for Iron Range communities. The spread for a large city like Minneapolis, which is located in the part of the state that currently has the strongest economy, is at the lower end of the range--about 1.5 percentage points, perhaps as low as 1.25 points. For smaller municipalities and those affected by weaker economic conditions, the spread in interest rates would be higher.

The impact of the House bill on the spread is uncertain, according to the experts we contacted. It seems possible that the spread could increase because the bill would restrict the supply of tax-exempt bonds. However, other provisions of the tax reform bill may lower the value to financial institutions of holding tax-exempt bonds by changing the way in which those institutions are taxed. The effect of those provisions might be to lower the spread.

Table 3.2 shows the increase in annual payments necessary to pay the debt service on a taxable bond under current market conditions. For an economic development district, the annual payment required to service an 8-year \$1,000,000 bond would increase from \$164,237 to \$174,015, or by 6 percent, assuming an interest rate spread of 1.5 percentage points. The

TABLE 3.2

ANNUAL DEBT SERVICE PAYMENTS FOR TAX-EXEMPT AND TAXABLE BONDS

ECONOMIC DEVELOPMENT DISTRICT (8 Years)				
<u>Interest Rate</u>		<u>Annual Payment on a \$1,000,000 Bond</u>		<u>Percent Increase In Annual Payment</u>
<u>Tax-Exempt</u>	<u>Taxable</u>	<u>Tax-Exempt</u>	<u>Taxable</u>	
6.5%	8.0%	\$164,237	\$174,015	6.0%
6.5	8.5	164,237	177,331	8.0
6.5	9.0	164,277	180,674	10.0
REDEVELOPMENT OR HOUSING DISTRICT (25 Years)				
<u>Interest Rate</u>		<u>Annual Payment on a \$1,000,000 Bond</u>		<u>Percent Increase In Annual Payment</u>
<u>Tax-Exempt</u>	<u>Taxable</u>	<u>Tax-Exempt</u>	<u>Taxable</u>	
8.5%	10.0%	\$ 97,712	\$110,168	12.7%
8.5	10.5	97,712	114,429	17.1
8.5 -	11.0	97,712	118,740	21.5

Source: Program Evaluation Division.

annual payment would increase by 10 percent if the spread were 2.5 percentage points. For a redevelopment or housing district, the annual payment on a 25-year bond would be from 12 to 21 percent higher, depending on the size of the interest rate spread.³ The annual payment on a longer term bond such as that used for a redevelopment or housing district is affected more because repayment of principal is spread over a greater number of years and interest is thus a more significant portion of the annual payment.

Besides issuing taxable bonds, there are several other ways a municipality could finance development activity in a tax increment district. These alternatives, which involve funding development activity out of current tax increment revenues rather than bonding, include:

³These examples do not reflect the need to pay capitalized interest. The percentage increase in annual payments would be higher if capitalized interest needed to be built into the bond issue.

- Under current state law, municipalities could use excess tax increments from existing districts to fund the up-front expenses for new development activity rather than retiring existing districts before their maximum legal duration. This could be accomplished by expanding existing project areas or by pooling increments among districts.
- Under current law, municipalities could also capture new development that is occurring without public assistance and use the additional taxes generated by that development to fund the up-front expenses for public development activity at other sites.
- It is conceivable that developers could finance the up-front costs of development and municipalities would repay the developers over time by rebating a share of the tax increments to developers.

The first two non-bonding options involve practices that currently exist but might become more widespread if the federal restrictions on tax-exempt bonds are passed. Concerns have been raised about these practices earlier in this report. It would not be desirable for these practices to become more widely used, particularly if they merely shift where development occurs without resulting in a net increase in jobs or tax base or a better targeting of assistance to blighted areas.

In considering changes to Minnesota's tax increment financing laws, it is important to recognize the effect that pending Congressional legislation may have on the development efforts of Minnesota's cities. Minnesota needs strong, economically viable cities that are able to address blight problems, encourage the development of low and moderate income housing, and help Minnesota retain and add jobs that would otherwise not be available to Minnesotans. The potential impact of Congressional action is, however, insufficient reason for dismissing the need for changes to Minnesota's tax increment financing laws. Clearly, problems exist with how tax increment financing has been used throughout the state. These problems need to be examined and corrected. Pending federal actions will not eliminate the need for changes to Minnesota's tax increment financing laws and may, as discussed above, increase the need to examine certain practices.

C. LEGISLATIVE OPTIONS

There are two approaches that the Legislature could consider in addressing problems with the use of tax increment financing in Minnesota. The first approach would be to strengthen the Minnesota Tax Increment Financing Act so that current problems would be less likely to occur in the future. This approach would primarily consist of placing additional restrictions on the use of tax increment financing by municipalities. The second approach could also include statutory restrictions, but would focus on more fundamental changes in the development financing process. For example, the Legislature might consider whether the process for approval

of the use of tax increment financing should be left to the discretion of city officials. Also, the Legislature could consider whether, or under what conditions, state aid should continue to pay for a portion of the costs of tax increment financing.

This section of the chapter is divided into two parts. In the first part, we discuss the first approach, recommend a number of specific changes in the Minnesota Tax Increment Financing Act to address certain problems, and suggest several alternative statutory restrictions to deal with other problems. The second part of this section discusses the advantages and disadvantages of more fundamental changes in TIF.

1. CHANGES TO MINNESOTA'S TAX INCREMENT FINANCING ACT

State law should discourage cities from including property in tax increment districts that is developing without assistance from TIF. However, existing law permits cities to capture the increased assessed value from any new private development or improvements for which a building permit was issued within the three-month period immediately preceding the approval of a tax increment financing plan. This provision has encouraged some cities to include properties that are developing without public assistance in tax increment districts. Some cities have even established districts that consist primarily or exclusively of such properties, rather than properties whose development would be induced by tax increment financing. To correct this problem, we recommend that:

- The Legislature should eliminate the statutory provision that permits a tax increment district to capture the increased assessed value from development for which building permits were issued during the three months prior to approval of the district.

While eliminating the three-month window would address part of the problem, it would not prevent a city from including within a tax increment district parcels of land that are expected to be developed or redeveloped privately within the near future. City officials often are aware of sites where development is likely to take place in the near future even though building permits have not been issued or applied for. This problem may be as significant as the three-month window but is not as easily remedied. We recommend that:

- The Legislature should consider addressing this problem indirectly by increasing the percentage of parcels that must meet the blight definitions in order for a district to qualify as a redevelopment district.

Increasing the percentage of blighted parcels could have the desired effect by limiting the extent to which a city can include non-blighted parcels in a redevelopment district. Because noncontiguous districts are permitted, city officials sometimes look for non-blighted parcels that are likely to develop privately. Including such parcels in a district enables the city to use the taxes generated by private development for expenditures within the district and its associated project area. Currently, a

city is able to establish a redevelopment district if as few as 35 percent of a district's parcels (50 percent of those with buildings) are found by the city to be substandard or needing renovation or clearance. Increasing the percentage of blighted parcels might limit the extent to which cities could intentionally capture tax increments from non-blighted parcels. Such a change would, however, only affect redevelopment districts and not economic development or housing districts.

Another option would be to clarify the intent of the "but for" clause. For example:

- The Legislature could consider requiring municipalities to make a "but for" finding for each parcel in a tax increment district.

Those parcels that are developing privately and do not need assistance from tax increment financing would not be permitted to be in the tax increment district. Of course, the effectiveness of such legislation might rest on the willingness of cities to implement its intent and, if implemented rigidly, it might affect the ability of some municipalities to undertake more risky, yet worthwhile, projects. Nevertheless, this option is worth considering. The existing "but for" clause has little or no significant effect on the properties placed in a tax increment district or the types of projects undertaken.

Another major concern that needs to be addressed is the lack of adequate targeting of redevelopment districts to blighted areas. We recommend that:

- The Legislature should examine ways to tighten the existing blight criteria for redevelopment districts. More restrictive definitions of a *structurally substandard* building and of conditions that require *substantial renovation or clearance* are needed.
- The Legislature should require that expenditures of tax increments generated by a redevelopment district be used exclusively to induce redevelopment of blighted parcels.
- The Legislature should examine whether, and under what conditions, unusual terrain or soil deficiencies should continue to be a criterion that can be used to establish a redevelopment district or whether it is more appropriately a reason to establish an economic development district.

In addition, some more technical amendments concerning the blight findings for redevelopment districts are needed. These amendments seem appropriate in light of the difficulty we experienced in obtaining documentation of the blight findings from a number of municipalities with redevelopment districts. They attempt to ensure that municipalities are complying with the legal requirements for establishing a redevelopment district. We recommend that:

- The Legislature should require a municipality to specify in its tax increment financing plan which one of the blight criteria it

is using and which parcels enable it to qualify a proposed district as a redevelopment district.

- A municipality should be required to maintain documentation on file that substantiates its finding that particular parcels meet the blight criterion used.
- The Legislature should require a municipality to document its blight findings again if it alters the size of a redevelopment district.

Another area needing attention is the increasing use of tax increments for general public improvements. These improvements--including improvements to existing parks and recreation facilities, replacement of existing infrastructure, and similar municipal functions--are usually financed with a city's own funds, special assessments, or other sources of funding such as user fees. They often have little direct impact on development activity. Tax increment financing is thus increasingly being used to provide a state and county subsidy for functions that most cities finance from other sources. In addition, some cities have used TIF to finance government buildings, and these are costs that most governmental bodies finance themselves. Current law restricts TIF expenditures only on certain types of municipal buildings. We recommend that:

- The Legislature should consider restrictions on the use of tax increment financing for various types of general public improvements normally financed from sources other than tax increment financing. Restrictions should apply to pre-1979 districts as well as districts created since the passage of the 1979 Minnesota Tax Increment Financing Act.
- The Legislature should consider the need for additional restrictions on TIF expenditures for government-owned or government-leased buildings, as discussed in Chapter 2.

Another issue raised in this report concerns the use of tax increments in housing districts for purposes other than to induce the construction of low and moderate income housing. We recommend that:

- The Legislature should require that tax increments generated by housing districts be used exclusively for the purpose of financing the development of low and moderate income housing.

We also recommend that:

- The Legislature should examine and clarify the purpose of economic development districts.

As long as the state continues to indirectly bear a major portion of the costs of a tax increment district, it seems reasonable that the purpose of an economic development district should be consistent with state goals. To the extent that economic development districts only result in shifting economic activity within the state, they serve no major state purpose.

Existing law recognizes that the purpose of economic development districts is to create and retain jobs, as well as increase the state's tax base. However, it assumes that creating jobs and increasing tax base at the local level is synonymous with creating jobs and increasing tax base at the state level. As pointed out earlier, the two are not always equivalent. One possibility the Legislature could explore would be to:

- require that the use of economic development districts be restricted to development activity that will increase or retain jobs for the state as a whole, and
- require that approval to establish an economic development district must be obtained from a state agency or entity such as the Minnesota Energy and Economic Development Authority.

There also needs to be legislative discussion of the increasing practices of tax increment pooling and establishment of large project areas. In some cases, cities employ these practices to spend tax increments for developments unrelated to the developments generating the increments. Furthermore, creating large project areas in which tax increments can be spent permits cities to extend the duration of districts to the maximum permitted by law. This conflicts with the statutory intent of Minn. Stat. §273.75, subd. 2., which requires that *excess tax increments* (tax increments that are in excess of the costs authorized by a tax increment financing plan) be used or set aside for the purpose of retiring a tax increment district early.

Prior to August 1979, tax increment districts were not required to have tax increment financing plans. Consequently, there is no requirement on excess tax increments generated in pre-1979 districts. However, cities may expand the project area in which a pre-1979 district was located in order to find ways to use tax increments that were in excess of the district's original needs. This expansion may prevent pre-1979 districts that have served their purpose from being decertified prior to the final statutory deadline of August 2009.

There are a number of possible ways of addressing these issues. One way, of course, would be to require once again that a project area be no larger than its associated tax increment district. Prior to 1979, this was generally the rule. However, in 1979, the Legislature saw the need to permit a tax increment district to be smaller than its project area so that a city did not have to place its entire project area in a tax increment district. For that reason, going back to the pre-1979 method would not be an improvement. Another possibility would be to permit multiple tax increment districts within a single, larger project area but require that tax increment generated by each district be expended only in that district and not pooled with increments among districts in the same project area. This requirement was effective for all districts established after 1979 until the so-called *technical amendments* of 1982 authorized the expenditure of tax increments anywhere within a project area, including other districts within that project area. However, this requirement could also cause cities to create larger districts in order to achieve flexibility in where tax increments are spent.

Other options that might be effective without reverting to the restrictions in effect before 1982 would be to:

- permit expenditures outside a redevelopment district only if the expenditures directly address documented blight elsewhere within the project area (with similar restrictions placed on the other types of districts);
- limit the amount of property or assessed value that a city could place in project areas;
- prohibit enlargement of project areas five years after their creation (state law already prohibits enlargement of tax increment districts after five years); and
- require that, if the tax increment financing plan is amended to include additional project costs, the original assessed value of that district be set equal to the then current assessed value (provided that the value of the district has increased).

It might be difficult to apply some of these options to existing districts and project areas. As a result, the Legislature may wish to consider other restrictions to address how existing districts are being operated. We recommend that the Legislature consider the following options:

- prohibit any further expansion of existing project areas.
- prohibit a municipality from creating a new tax increment district or expanding an old district if the captured assessed value in existing districts plus the estimated captured assessed value in the proposed district or district expansion exceed a given percentage of the municipality's total assessed value.

A final area that merits attention is the lack of sufficient state oversight of tax increment districts. As discussed in Chapter 2, there is evidence that some tax increment districts do not comply with certain key provisions of the Tax Increment Financing Act. While our study did not include a comprehensive compliance audit, it is clear that certain types of compliance problems require greater state attention.

Specifically, there needs to be better compliance with those statutes that address the computation of captured assessed value and tax increments. These statutes directly affect the level of state aid and the development subsidies which cities provide. The primary examples are statutes which describe 1) the method for computing original assessed value on tax-exempt property, 2) the "knock-down provision," and 3) the three-year limit on tax increment collection without the issuance of bonds, the acquisition of property, or the construction of public improvements.

Currently, no state agency audits or directly enforces these provisions. Also, while county auditors are generally presumed to have the primary responsibility for tax increment compliance, the tax increment financing law does not explicitly charge county auditors with this responsibility.

As a result, county auditors are sometimes unfamiliar with tax increment financing provisions or unsure of their authority to enforce these provisions.

We recommend:

- The Legislature should provide clear authority for county auditors to enforce state tax increment financing laws affecting the determination of tax increments.
- The Minnesota Department of Revenue should provide additional guidance to county auditors on those TIF provisions that directly affect tax increment calculations. The department should ask county auditors to review existing districts and correct previous errors. Furthermore, the department should consider incorporating its communications to county auditors regarding tax increment financing into a broader property tax manual for counties, facilitating future application by the 23 counties which currently have no tax increment districts.

Some compliance problems may be beyond the scope of the county auditors' authority. For example, the question of whether certain expenditures are permitted by law is a legal issue, perhaps best addressed by the Office of the State Auditor. Currently, the State Auditor's compliance manual for city audits does not require reviews of tax increment districts for legal compliance. While we happened to find only a few cases in which the legality of TIF expenses is in question, we think there is a need for some oversight of these matters and of county auditors. Consequently, we suggest that the State Auditor's Office incorporate several key matters of legal compliance relating to tax increment districts into the State Auditor's compliance manual. Alternatively, the State Auditor could conduct periodic statewide studies of tax increment financing compliance.

2. FUNDAMENTAL CHANGES IN TAX INCREMENT FINANCING

The previous section discussed possible changes in the tax increment law that might address the problems cited in this report. At a minimum, the Legislature should consider these methods of tightening state TIF law. However, one might question the extent to which new statutory restrictions will prevent future problems. It is admittedly difficult to regulate through legislation a program with as many complexities as TIF. For example, while we recommend that the Legislature should tighten the statutory definitions of blight, it is clear that no definitions can perfectly target TIF to those areas most in need. Also, bond attorneys, financial consultants, and city officials are adept at finding "creative" uses of TIF that are not expressly prohibited by law. Thus, it is doubtful that new statutory restrictions alone will fully address the problems with tax increment financing.

In addition, it may not be possible to address TIF problems unless there are fundamental changes in the incentives cities have to create districts. These incentives stem from the divergence between 1) *who funds tax*

increment districts, 2) *who benefits* from tax increment districts, and 3) *who initiates and controls* tax increment districts. On the issue of *who funds* tax increment districts, TIF rests on the notion of cost-sharing among several taxing jurisdictions. Currently, the state, county, and city bear the largest costs of tax increment financing. The state's cost is indirect (primarily through increased education aids to school districts), but the state's cost is often larger than the city's cost. On the issue of *who benefits* from TIF, it appears that cities are the primary beneficiaries of tax increment financing. Taxing jurisdictions benefit from TIF to the extent that it induces development that would not otherwise have occurred in the boundaries of these jurisdictions. For geographically large taxing jurisdictions, such as the state, TIF typically results in few net benefits. On the issue of *who initiates and controls* tax increment districts, cities have the sole authority for district creation and spending (within the parameters established by state law). The law permits school districts and counties to review and comment on TIF plans, but these jurisdictions have no authority to approve or deny city decisions. The state does not have authority to approve TIF districts nor to comment on TIF plans. In sum, there are incentives for cities to use state and county funds to leverage development. This development generally benefits cities, but the development may come at the expense of development elsewhere, perhaps yielding little or no benefit to the state or other taxing jurisdictions.

Given these incentives and the difficulty of "regulating" tax increment financing, the Legislature may wish to consider more fundamental changes in TIF. These fundamental changes could go beyond a mere tightening of tax increment financing restrictions, perhaps changing TIF incentives and the way TIF is funded. Two such changes that the Legislature could consider are:

- *Alternative 1:* Make changes in the process for approving tax increment districts, permitting those jurisdictions that finance TIF districts to jointly approve or deny district creation. This alternative would most likely be accompanied by a requirement that school districts hold the state harmless for state aid purposes; or
- *Alternative 2:* Replace tax increment financing with "redevelopment funds," financed with a combination of local and state funds.

The first alternative would directly address cities' current incentives to create tax increment districts. Counties and school districts, which now can only review and comment on TIF plans, would be given a stronger role in the tax increment district approval process. By involving counties and school districts, the Legislature might decrease the likelihood that these jurisdictions will have to finance developments from which they receive few benefits. For example, it may be in a particular city's interest to induce a development by financing a freeway interchange or major soil corrections with tax increment financing. However, if development could have located at other sites in the county that did not require these expenditures, the county stands to gain little from TIF. Alternative 1 would

give the county a direct role in approving or denying this tax increment district.

Changes in the approval process might be accompanied by changes in the source of TIF funding. Currently, the state typically funds more tax increment costs (primarily through increased education aid to school districts) than do other taxing jurisdictions, yet the state generally receives relatively small benefits from TIF projects. By requiring school districts to hold the state harmless for their tax increment districts, the Legislature could ensure that the taxing jurisdictions involved in district approval are the jurisdictions with financial stakes in TIF.⁴

The second alternative which the Legislature could consider is replacement of tax increment financing with "redevelopment funds." In 1985, a report by the Twin Cities Citizens League recommended: 1) phasing out TIF over a two and one-half year period; 2) replacing TIF with "redevelopment funds," which could be financed with city general fund transfers, city property tax levies, a new program of state aid, general obligation bonding, TIF district surpluses, and repayment of development loans to city governments. The Citizens League's primary reason for this proposal was to improve the accountability of development finance to voters; local sources of the redevelopment fund would be subject to city budget processes or voter approval. In addition, the League felt that state aid for redevelopment funds could target the state's most blighted areas. Conceivably, the Legislature could use the state aids that now indirectly finance TIF districts to assist these local redevelopment funds.

In a sense, some cities already have the equivalent of redevelopment funds. Those cities that have large project areas and have accumulated surplus reserves of tax increments can use these funds to subsidize any development in the project area. Like Alternative 2's redevelopment funds, surplus tax increments are a combination of state and local tax dollars.

For the reasons stated in the preceding paragraphs, changes in the TIF approval process (Alternative 1) and establishment of redevelopment funds (Alternative 2) both deserve legislative consideration. In addition to the potential advantages of these alternatives that we have discussed, the Legislature should consider some concerns that may be raised about each option.

One concern about changing the process for tax increment district approval is that county and school boards have little experience in development finance. Officials from these jurisdictions may not understand tax increment financing, so any change in the TIF approval process must be accompanied by some educational efforts.

⁴One way to hold the state harmless would be to change the way state law treats captured assessed value in education aid calculations. Currently, captured assessed value is not counted as part of local tax bases in aid calculations. As a result, school districts which include property that has captured assessed value generally receive more state education aid than they would if it were included in the local tax base.

Another concern about Alternative 1 is that changes in the approval process will not necessarily prevent excessive TIF subsidies. For example, a small city may wish to induce a grocery store with a large land write-down. While a new grocery store may contribute little to the economic well-being of the state as a whole, it may be in the interests of the city, county, and school district to finance the store. This would be particularly true if the store was considering locating in an adjacent county. Thus, while the county and school district may have broader perspectives than the city, their perspectives sometimes may be similar to the city's.

A third concern is that an approval process with three parties could take longer than an approval process involving only the city. Tax increment financing appeals to some cities because creation of a district can be done relatively fast. This concern might be addressed by placing statutory limits on the approval process timeline.

Finally, there may be concern over the structure of the TIF approval process. Some people have proposed granting counties or school districts veto power over city TIF decisions. However, such a system could allow narrow interests to block worthy projects. A better system might be one in which the city, county, and school district make TIF decisions jointly, based on majority vote. Wisconsin has such a system of joint review boards for TIF districts.

Some concerns can also be raised about Alternative 2. First, the redevelopment funds proposed by the Citizens League involve no county or school district financial contributions, although these jurisdictions may benefit from new development. Perhaps the most unique aspect of tax increment financing is its potential for cost-sharing among benefitting jurisdictions, and we question whether it makes sense to ask cities to bear all local costs for development finance. In contrast, Alternative 1 preserves and enhances the cost-sharing approach by enlarging the school district's financial stake in TIF.

A second issue is the practical problem of designing a state formula for allocating redevelopment funds to cities. While the Citizens League report suggests allocating aid on the basis of the age or condition of a city's buildings, we wonder whether this idea is workable. It is in the state's interest to target redevelopment expenditures to blighted areas, but it is not clear that an aid formula could do this better than legislating new restrictions to the TIF blight criteria.

A third concern is that redevelopment funds may not change the fundamental incentives that cities have to compete with each other. The Citizens League suggests that regional planning agencies should develop guidelines to prevent inter-city bidding for new development. However, it will still be in the interest of individual cities to try to lure development from other cities. Unlike Alternative 1, this alternative does not provide broader governmental jurisdictions (such as the county and school board) with a direct voice in cities' development decisions.

A final concern is whether cities will be able to bond for redevelopment projects under Alternative 2. If the bonds issued for the redevelopment

funds are subject to the state's existing municipal debt limits, this may seriously restrict the ability of cities to finance major development projects.

Overall, we encourage the Legislature to examine the merits of these more fundamental changes in tax increment financing. From the state's perspective, there may be local incentives to oversubsidize new developments, and it is important that the Legislature address these problems before they become more widespread. Neither of the alternatives discussed in this section is a panacea for the problems of tax increment financing and both have potential disadvantages. However, both deserve serious consideration from the Legislature.

APPENDIX

This appendix contains brief descriptions of nearly 200 Minnesota tax increment districts in the 44 cities we visited. The information is current as of November-December 1985, when each city reviewed its appendix summary for factual accuracy. In two cases (Minneapolis and Bloomington), only the most recent tax increment districts are summarized, due to the large number of districts in those cities. In parentheses following the name of each tax increment district (TID) is the type of tax increment district (redevelopment, economic development, housing, pre-1979) and the year of district certification. "Pre-1979" refers to those districts established prior to August 1, 1979. The summaries describe the previous use of tax increment sites, the resulting developments, the amount of tax increment bonds issued, and the specific uses of TIF.

ALBERT LEA

Red Owl TID (pre-1979, 1976). The city issued \$225,000 in bonds in 1977 to acquire and clear three parcels. Prior to creation of the TID, this site housed strip commercial structures built during the 1950s. An Albert Lea grocery store expanded its business at the site. The city expanded the district in 1982 to include the old city hall, but no renovation of this structure has occurred.

Farmstead Foods TID (redevelopment, 1984). Albert Lea issued a \$1 million tax increment bond to assist in the modernization of a hog processing plant. The slaughterhouse and smokehouse of one of the city's major employers were functionally obsolete. The company built new facilities on stockyard land. The primary uses of TIF were sewer and water extensions and soil corrections.

North Bridge Mall TID (economic development, 1984). Developers will construct 260,000 square feet of retail space next to Interstate 90 and the Albert Lea airport. This site currently houses a discount store and a grocery store (they will remain); part of the site was a slough and part was farmland. A \$1.2 million dollar TIF bond will finance a \$550,000 land write-down to compensate the developers for soil corrections. The rest of the bond will finance storm sewers,

sanitary sewers, and streets. Businesses at the mall will pay assessments of \$235,000 for the public improvements, and the city will fund a portion of the storm sewer improvements out of its general fund.

Skyline Mall TID (redevelopment, 1984). This 18-year old enclosed mall requires significant repairs to its parking lot, roof, and lighting. The city attributes the condition of the mall to the owner's lack of maintenance. A principal tenant (Montgomery Wards) left the mall, and city officials think that other tenants may leave in the future. No bonds have been issued. The city may contribute a \$400,000 write-down if the owner agrees to renovation and land acquisition for an 82,000 square foot expansion.

ANNANDALE

TID 1 (pre-1979, 1978). This 201-parcel district includes Annandale's downtown, some residential areas, an industrial park, a city park, and extensive frontage along Highway 55. The city issued a \$240,000 tax increment bond, paid off in 1984. Annandale purchased and wrote down a vacant hotel that has since been privately renovated. For three years, the city paid half of 40 merchants' special assessments for construction of new storefronts throughout downtown. Other downtown expenditures included: acquisition and demolition of two vacant buildings for parking lots; acquisition of a site for a hardware store's expansion; acquisition of a dilapidated house for construction of office space. The city also improved a city park (new equipment, new lighting). In the industrial park, the city wrote down land and existing special assessments for two sites that now house manufacturing firms. Annandale plans two major expenditures in the future. First, TIF will finance roughly half the cost of building a 9-ton road through the industrial park (total cost of the road is \$316,000). Second, TIF will finance 70 percent of a \$715,000 water well and storage tank system for the industrial park.

TID 2 (redevelopment, 1978). Prior to creation of the district, this site in a residential neighborhood contained a welding shop and junkyard. The city wrote down the land and demolished the structure; no bonds were sold. Three market-rate, single-family houses were built at the site.

AURORA

Downtown TID (pre-1979, 1978). This district covers about seven city blocks. A bank and convenience store were planning new construction without TIF assistance, and the city included these parcels in the district. The city used \$24,000 in tax increments to write down land for a new drug store to replace an old one destroyed by fire. The city also used tax increments for a parking lot and sidewalk that benefited new businesses. No bonds have been issued. The city will use \$75,000 of its tax increment reserve to replace street lights and downtown sidewalks.

TID 2 (economic development, 1984). The city created this five-acre district in 1984 hoping for development of a motel and restaurant. No businesses have located in the district, and the city will not issue bonds for infrastructure construction until it receives a developer's commitment. The site is currently vacant and not served by city utilities.

BENSON

The city's two 1975 districts include large numbers of parcels but very little of the central business district. *TID 1* is north of downtown, and *TID 2* is south of downtown. Sixty-two percent of the city's 1975-1984 building permit valuation occurred in these districts. The city has issued \$975,000 in bonds for the two districts.

TID 1 (pre-1979, 1975). While this district contains some commercial properties downtown, the primary land use is residential. The residential area was largely unplatted at the time of *TID* creation. The primary uses of *TIF* were to: construct streets in a new housing subdivision; write down and clear land for commercial uses near downtown; construct sidewalks and alleys in commercial blocks near downtown. Two new businesses located in the *TID* since 1975, one of which received *TIF* assistance. Nineteen single-family homes and 58 rental units have also been built.

TID 2 (pre-1979, 1975). Benson focused most of its *TIF* efforts on this district, which includes more commercial land uses than *TID 1*. The primary uses of *TIF* have been street construction and widening, land write-down, and utility extension to a new subdivision. New developments since 1975 include 13 single-family homes, 39 rental units, 10 retail business relocations, and one industrial relocation (a metal fabrication firm) from elsewhere in Benson.

BLAINE

TID 1 and TID 2 (economic development, 1981). Blaine created these two districts at the same time, and both consist of industrial parcels of land. The distinction between the districts is that *TID 1* contained lots on which developments were already occurring, while *TID 2* contained vacant parcels where the city wanted to induce development. The city pools increments from the districts. Blaine funded a \$250,000 reserve fund for industrial development bonds with a tax increment bond. Only one development in the district has used *IDBs* for construction, somewhat less than the city expected. The city also provided a \$200,000 write-down to a car dealership. In addition, the city plans to use \$150,000 in tax increments for a \$2.2 million reservoir that will serve most of the city.

Housing TID (housing, 1985). The district contains several contiguous residential areas. These include: (1) a new subdivision that is one-third built and will have 90 homes within five years,

(2) a vacant area on which 70 homes will be built over five years, starting in 1986, (3) about 10 older homes with large lots along a principle street, (4) vacant land on which 45 homes will soon be built. A fifth area is the only area targeted for redevelopment with tax increments. It currently has 65 homes served by aging wells and septic systems. Blaine proposes developing 140 new homes in this fifth area (\$50-70,000 price range). A \$2.7 million tax increment bond will finance utilities, streets, a public park, and a civil defense siren for the area. Assessments will repay approximately \$1 million of the bond, but city officials feel that assessments must be capped due to the incomes of residents.

TID 4 (redevelopment, 1985). The city established the district to provide assistance to a truck leasing firm that was considering this Blaine site. The site has soil problems, and the city offered to finance soil corrections with TIF. The trucking firm chose a Fridley site instead of the Blaine site, but Blaine still hopes to induce a business with its offer of TIF-funded soil work.

BLOOMINGTON

Bloomington has 17 active districts. We focused on the city's most recent districts, so details of the earliest six districts (all are "pre-1979" districts) are not included here.

CAB TID (housing, 1982). This site previously contained a vacant school administration building. Bloomington issued a \$1.4 million tax increment bond to finance acquisition and demolition of the site. TIF also financed a write-down of the development: an elderly housing/health care complex. To date, 45 housing units have been built, and 190 more will be built in the future.

Oxboro TID (redevelopment, 1984). This commercial district is east of Interstate 35 (centered at 98th Street and Lyndale Avenue). For 20 years, Bloomington has tried to establish more intense, better planned development at the site while keeping existing businesses in the area. Until establishment of this district occurred, the city was unable to achieve this. Bloomington issued \$8 million in tax increment bonds for acquisition and write-down (purchase land for \$5.9 million, sell it for \$2.4 million), public improvements (primarily streets and sewers), and relocation costs. A general obligation tax levy also supports the project (currently \$540,000 per year). Redevelopment in the district will occur over a ten year period.

Normandale TID (economic development, 1982). The city wants to construct a ring route that will keep some local traffic off of Interstate 494, Interstate 35, Cedar Avenue, and Normandale Avenue (all of these have freeway status). As a first step in construction of the ring road, Bloomington built a bridge over Normandale at 82nd Street. A developer planned office/hotel construction nearby, and the city created the district to capture increment from the project (the development received no TIF assistance). The Normandale bridge had

the lowest priority of the ring route bridges; the others have not yet been built. A \$4.1 million bond funded the ring road bridge plus a pedestrian bridge from the office complex to a nearby lake.

Homart TID (economic development, 1985). This site at the corner of Interstate 494 and France Avenue previously contained a drive-in theatre. The city plans to use TIF for \$1.6 million in road improvements at the site and \$300,000 in sanitary sewer enlargement/lift station construction. The developer will build a high-rise office and hotel complex.

The following seven districts are all in the "Airport South Development District." There is a single bond fund for the districts, and the city plans to pool increments in the future. For most of the districts so far, business developments have occurred without TIF assistance, and the city will decide in the future what uses TIF funds should be dedicated to. Except for the two redevelopment districts, all of the sites were previously vacant.

Appletree Square TID (economic development, 1982). This office building developed without TIF assistance. A \$540,000 tax increment revenue bond was issued and helped fund a traffic study for the entire Airport South area. The bond may finance storm sewer work in the future, but the city is still undecided.

Opus TID (economic development, 1984). Bloomington created the district to capture increments from a 12-story office building. Future TID developments may include a hotel and a second office building. There has been no TIF expenditure to date. Bloomington issued \$1.17 million in bonds, probably for some storm sewer and road improvements in the Airport South area.

Stadium Site TID (redevelopment, 1984). For over twenty years, this was the site of Metropolitan Stadium, home to the Twins and Vikings. Current plans call for development of a "mega-mall" at the site, including retail and entertainment uses. A \$140 million tax increment bond issue will finance project costs, primarily public parking and road improvements. Bloomington expects to use increments from some of the other Airport South districts at this site.

Bor-Son TID (economic development, 1984). The city created the district to capture an office development that was about to occur. There was no TIF assistance to the development, and no bonds were issued.

Muir TID (economic development, 1984). Bloomington created the district to capture increments from a planned hotel development. The development received no TIF assistance, although the city issued a \$1.1 million bond for later expenditures in the Airport South area (these may include sewer and road improvements, but no decisions have been made yet).

VTC TID (economic development, 1985). A computer chip manufacturer located in the district. The land previously was vacant and had no structures or soil problems. Bloomington issued \$750,000 in taxable bonds to finance site land acquisition and write-down; the bonds will be repaid with tax increments.

Kelly TID (redevelopment, 1985). This 37-acre parcel is adjacent to the stadium site and will be part of the mega-mall development. Previously, this was farmland occupied by a partially burned farmhouse. The site will probably contain parking for the mega-mall.

BROOKLYN PARK

TID 1 (economic development, 1980). Before 1980, this land was largely vacant. TIF funded all costs for construction of a \$4.5 million freeway ramp for Interstate 94 and U.S. Highway 52. A business park (primarily with office and warehouse uses) provides the tax increments created a second TID and is pooling tax increments to support the ramp project. Brooklyn Park considered the land placed in TID 2 to have a high potential for development, in part due to the freeway ramp's proximity. Three businesses have located in this TID, the largest of which is Belco Storage. The city is now planning to build a road connecting TID 1 and TID 2.

TID 3 (redevelopment, 1985). This district contains scattered sites, many of which the city deemed blighted (visual blight, non-conforming uses). Brooklyn Park plans to use tax increments from this district, in addition to a \$3 million surplus from the first two districts, to accelerate the improvement of County Road 109 (85th Avenue) and 93th Avenue. The city hopes to complete the work without issuing tax increment bonds. Among the businesses that will generate tax increments are eight that received building permits during the three months preceding TID certification.

BUFFALO

Downtown TID (pre-1979, 1979). This 405-parcel district includes Buffalo's downtown, some commercial areas along Highway 55, and some large areas of housing. The city developed the district to strengthen its downtown and to counter pressure to build shopping malls along Highway 55. The city has issued about \$2 million in bonds, primarily for downtown projects. The major downtown expenditures included: changes in street alignment; the bricking of previously-paved streets; installation of new sidewalks, street lighting, and street furniture; acquisition of a lumberyard to make room for a large grocery store and parking lot. In addition, the city wrote down (1) a downtown site with an old gas station for retail expansion and (2) a vacant restaurant site for development by a new restaurant.

CHANHASSEN

Downtown/Business Park TID (pre-1979, 1977). When the district was originally established in 1977, the focus of the plan was on downtown redevelopment. To date, the only major redevelopment downtown has been relocation of a printing business to the business park. The developers of a bowling center and retail shops remodelled the printer's building after the city purchased the building for \$3.1 million and re-sold it for \$120,000 (a tax increment bond funded the purchase). Excess tax increments financed a \$200,000 construction loan for the bowling center. Significant development (light manufacturing, service businesses, office space) has occurred west of downtown in the city's new business park. The city has spent \$1.1 million in the park for street construction, well-house construction, and utilities on land that was previously agricultural. The city is spending \$2.5 million in the business park for assessment write-downs. Businesses receive assessment subsidies equalling seven percent of the value of their buildings. For the average business, this reduces assessments 75 percent. The TID generates over \$800,000 in tax increments annually, and the city may use some increments in the future for downtown acquisition and public utilities work.

TID 2 (economic development, 1980). The city issued \$800,000 in bonds to finance development of a business park on previously vacant land. The bonds were used primarily for street and utility work; there have been no special assessments. The major tenants of this 1980 district are a computer manufacturer, a lumberyard, and a print shop. The city expects to spend an additional \$440,000 for road construction in 1986.

CHASKA

Talheim/Chaska Manor TID (housing, 1982). Prior to creation of the tax increment district, this site housed an old duplex and a small storage building. The city issued \$200,000 in bonds primarily to write down the land and provide sewer and water. Demolition and relocation were minor TIF costs. A 59-unit senior citizens housing project resulted.

Sugar Creek TID (redevelopment, 1983). Crystal Sugar vacated two office buildings in the early 1960s. A developer rehabilitated the buildings, and \$48,000 in tax increments are being used to reduce the interest-rate on the mortgage. The district is financed on a pay-as-you-go basis, and the city will not provide the write-down if the development generates insufficient tax increments.

Floodplain TID (redevelopment, 1985). This district contains 833 parcels, many of which lie in the floodplain of the Minnesota River at the southern end of Chaska. In addition, 40 percent of the district's acreage is in commercial and industrial areas that stretch to the north end of the city. Chaska hopes to finance at least \$4.5 million of a \$30 million federal flood control project with TIF. While the

project has been authorized by the federal government, federal funds for the project have not yet been appropriated. The city also plans to use \$400,000 to \$700,000 in TIF bonds for acquisition, write-down, clearance and improvements at the site of a future downtown mini-mall. The city will also provide \$200,000 to \$400,000 in TIF assistance for development of an industrial park at the north end of town. The city plans several other tax increment uses, primarily for utility and street improvements to commercial/industrial areas. TIF will finance about 40 percent of the \$700,000 in improvements planned for the city's main street (a municipal state aid street). Chaska has issued \$2.3 million in bonds for this district.

COON RAPIDS

The city has a single project area for its eight tax increment districts. The project area contains scattered parcels and primarily includes industrial areas of the city. Generally, the city finances tax increment projects internally, issuing tax increment bonds at a later date to reimburse the city. To date, \$5.5 million in bonds have been sold. Most of the office buildings built in the district have received industrial development bonds. Coon Rapids tries to limit TIF subsidies to 15 percent of land and building costs for new developments. Soil corrections receive the city's highest TIF priority.

Galway Place (housing, 1980). The city drew up plans for the district but forgot to have the district certified in 1980; there has been no subsequent certification. Consequently, this development technically is in the project area but not in a TID. A 36-unit subsidized housing project was built on previously vacant land in the center of the city. Coon Rapids internally financed \$160,000 in improvements, half of which went for equipment and landscaping to a nearby park. City officials say the development created needs for recreation space previously unforeseen in the city's comprehensive park plan. Coon Rapids also assisted the developer through a land write-down and payment of special assessments for new utilities.

Oxbowl Bend Apartments TID (housing, 1982). A non-profit developer (Volunteers of America) built a 60-unit subsidized senior housing project on previously vacant land. The \$120,000 bond issued by the city financed a land write-down and persuaded the developer to add a community room to the project.

Glacier-Industrial Park TID (redevelopment, 1982). TIF has financed \$230,000 in land write-down and soil corrections at several sites in the district. Subsidized developments to date include one office building and six office/warehouse buildings. Possible future developments include a motel and a city fire station. The city approved its TIF plan in 1982 shortly before the state law banning TIF subsidies for municipal buildings took effect. If built, the fire station would be completed in 1987, at the earliest.

Endotronics/Gaughan TID (redevelopment, 1983). This previously vacant industrial site now houses four office buildings, plus some residential and retail space. All four received TIF for soil corrections and land write-down.

Medical Building TID (redevelopment, 1983). A clinic that had been in Coon Rapids for 30 years expanded on a previously vacant site after merging with a Fridley clinic. TIF subsidized a land write-down, soil corrections, and utility extensions for the clinic and an office building.

Dart Park TID (redevelopment, 1985). Three businesses were in this business park prior to creation of the district, and two businesses located in Dart Park without tax increment assistance since the district's creation. Gage Tool constructed an office building with TIF assistance for soil corrections, and Merchandising Fixtures Incorporated moved its Twin Cities operations here with TIF assistance for soil work, utilities, and land write-down.

Reisling Park (redevelopment, 1985). A 140-unit subsidized housing project is being developed on vacant land with TIF assistance for land write-down, soil corrections, and utilities. The city feels it was able to get a higher quality project (swimming pool, sauna, exercise room, underground parking) than it would have without TIF. Tax increments will also finance the creation of a new city park near the development.

Doty Industrial Park (redevelopment, 1985). Currently, this is vacant industrial land. No developments are currently anticipated in this district. The city expects to finance soil corrections for any sites on which development occurs.

COTTONWOOD

Downtown TID (pre-1979, 1978). This district includes all of downtown plus an industrial area east of downtown. A bank began construction of a new building in 1979, and today the bank represents 60 percent of the district's captured assessed value. The bank received no tax increment assistance. The city's first expenditure of tax increment funds came in 1982, when the city leveraged a \$217,000 community development block grant for Mid-Continent Cabinets with \$40,600 of TIF funds. Mid-Continent, a major Cottonwood employer, wanted to expand, and TIF paid for all sewer and water improvements (primarily with a bond issue). The company now employs nearly 200 people. More recently, the city has used its reserve of tax increments (no additional bonds) for downtown sidewalk and street improvements. In 1984, the city replaced its downtown streetlights. In 1985, the city replaced streets and sidewalks in half of downtown, and the other half of the streets and sidewalks will be replaced in 1987. The total cost of the downtown improvements is about \$140,000. Cottonwood will consider terminating the district after completing these improvements.

DODGE CENTER

Downtown TID (redevelopment, 1979). Originally, the city planned to clear some houses to make room for a grocery store relocation, but the grocery store decided to remain at its existing location. As a result, the city amended its TID boundaries to include a parcel where a bank was planning construction of a new building and to include greater portions of the downtown streets. The bank received no TIF assistance. A \$155,000 tax increment bond financed downtown improvements to sidewalks, streetlights, curbs and gutters, trash containers, benches, and a parking lot.

Housing TID (housing, 1979). The original TIF plan was for a 38-unit, low income housing project. The city expanded the district boundaries in 1981 to include land for a 36-unit housing development for the elderly. Dodge Center issued \$110,000 in bonds to finance streets and utilities for the first project.

Airport TID (redevelopment, 1983). The district contains parcels in three areas of the city. These include: (1) the city airport, (2) a manufacturing firm that was planning expansion, (3) some businesses in old buildings. The city plans to use tax increments generated by the manufacturing firm's expansion to finance the non-federal share of airport upgrading. Specifically, the city wants to pave its sod runway, provide more space for hangars, and improve airport lighting.

DULUTH

Truck Center TID (pre-1979, 1975). Prior to 1975, this site had some housing but was largely vacant. Duluth issued \$1.26 million in tax increment bonds to acquire and demolish about 30 homes. A variety of truck-related businesses consolidated their operations at this site. Because tax increments generated by the project initially came in slower than expected, Duluth levied \$91,000 in additional taxes between 1977 and 1979 to support the project.

Downtown TID (pre-1979, 1975). This district includes about 25 blocks of downtown Duluth plus portions of the Interstate 35 corridor and the waterfront. Of the \$13.8 million in district expenditures through 1984, the city has spent \$5.2 million for downtown skyways (TIF pays for the skyways, and building owners pay for the cost of hooking them up). Duluth spent \$2.4 million in TIF funds to redevelop the "Lyric Block" into a hotel (TIF funded land write-down, demolition, sidewalks, streets, a skywalk, and a public space). The city has spent \$2.4 million to provide loans to store owners for building rehabilitation. In addition, the city has used TIF to help subsidize free parking in several downtown ramps. The city has no immediate plans and has spent few TIF funds for redevelopment of several areas in the district, including the Bayfront, Harbor Square, and the East Superior-First Street areas of the district. Overall, the city issued tax increment bonds totalling \$14.1 million through 1984. Federal grants, housing bonds, and industrial revenue bonds have also played a major role in downtown redevelopment.

West Duluth/Oneota Industrial Park TID (redevelopment, 1981).

There are two major TIF projects in this district; one is completed and one is just starting. The completed project is a neighborhood shopping center. Duluth issued a \$3.1 million tax increment bond to acquire approximately two dozen parcels (most of them containing residential structures in poor condition) and to construct streets, sewers, and other utilities. The second major project in the TID is development of an existing industrial park. The city used federal funds to clear this site, but there have been no TIF expenditures to date. TIF will be used to install roads and utilities in the future. Some new businesses have already located in the park.

Waterfront and Eastern TID (redevelopment, 1983). This district contains most of the waterfront east of Duluth's Downtown TID. It includes the Duluth Auditorium, the approach to the Aerial Bridge, and many industries. The main reason for creating the district was to encourage redevelopment of a vacant brewery, for which the city issued industrial development bonds and received a federal UDAG. Developers converted the brewery into an inn, restaurant, and shops. TIF helped to ensure adequate parking at the site. The developers financed parking ramp construction, and the city is using tax increments to pay its lease on the ramp. The city hopes to redevelop more sites in the district as tourist attractions.

Miller Hill Mall TID (economic development, 1985). The district contains an enclosed mall, two large retail stores, housing, and some wetlands. A developer proposes building a 190,000 square foot addition to the mall. Site preparation, road construction, and retention ponds will be financed with a \$1.75 million tax increment bond. The TIF plan states that this district will exist for 12 years, which is two years longer than the maximum permitted by state law.

St. Louis Bay Energy and Industrial Park TID (redevelopment, 1985). An electrical utility and a paper milling company propose construction of a mill on a 92-acre site next to an idle steam electric plant. Over \$26 million in TIF bonds will finance land acquisition and the retrofitting of the electric plant. Over 600 mill-related jobs may be created by this development. The public financing for the project (including TIF) will total about \$42 million.

Rice's Point (redevelopment, 1981). This district includes the Duluth Clure Public Marine Terminal and other waterfront dock facilities. Duluth's Seaway Port Authority used TIF for acquisition and improvement of a privately-held dock, where the authority hopes to attract future development. The Port Authority used its own funds to construct utilities and a railroad loop in the district. Expected TIF activities in the future include construction of several streets and additional improvements to the dock. The primary business attracted to the district so far is St. Lawrence Cement, a Canadian-based company. No bonds have been issued.

Air Park TID (pre-1979, 1978). The Duluth Port Authority issued \$1.67 million in bonds to finance utility extensions and streets to undeveloped Port Authority land near the Duluth International airport. Twelve businesses have located office, warehouse, or service outlets here. A portion of the park has foreign trade zone designation, and part of the TID is in an enterprise zone. The Port Authority will use the district's tax increment surplus to improve additional streets.

EDEN PRAIRIE

TIDs 1, 2, 3, 4, 5, 6, 7 (economic development, 1981-1985). The sole TIF expenditure and prime reason for establishing the district is the ring road system that now surrounds the confluence of trunk highways 494, 5, and 169. According to the city, access to these routes was confusing, and access to an existing shopping center was difficult from certain directions. While development was occurring in the area at the time of TID creation, the city felt that further development would not occur without the ring road. Tax increments are generated by a variety of new office, commercial and industrial developments in the area. The developments in districts 1-5 were needed to pay for the ring road system on schedule, while TIDs 6 and 7 permitted the city to retire tax increment bonds at a faster rate than originally pledged. The total cost of the road and utilities improvements is about \$18 million, of which about 15 percent is assessed.

FARIBAULT

The city has issued two bonds to subsidize its five TIDs: \$155,000 in 1982, and \$1.2 million in 1985.

West TID (redevelopment, 1981). Four new developments have generated tax increments in this district to date. K and G Manufacturing, which manufactures parts for computers, is expanding its current building on an adjacent site. The city has used TIF for parking lot construction thus far, and TIF will be used in the future for acquisition, clearance of old structures, and street improvements. A second development is Stafford Housing, 16 market-rate housing units constructed on a site previously occupied by a substandard dwelling and a dirt alley. TIF financed clearance and alley paving. The third development is the expansion of the Crown Cork and Seal Company, a manufacturer of cans. This company was landlocked, and TIF subsidized clearance of four adjacent homes, a land write-down, and a street improvement. The fourth development occurred at a site occupied by a bus rehabilitation company that wanted to move. TIF financed clearance and grading of the site for a Faribault car dealer, who expanded his business at this site. The West TID also includes a sizable residential area, but redevelopment of this section occurred with federal community development funds.

North TID (redevelopment, 1981). The one major development in this district has been the Faribault Canning Company, which relocated a bean processing plant to Minnesota from Colorado. The primary inducement to the company was a \$250,000 Economic Recovery Grant. TIF provided a \$115,000 subsidy for pollution controls, street and access improvements, and a parking lot. In addition, TIF will pave several streets in an adjacent low-income neighborhood. In the near future, Faribault plans to use TIF to acquire land and make street and site improvements for the expansion of a major city industry, the Woolen Mills.

Old Town TID (redevelopment, 1981). This 546-parcel district contains most of Faribault's downtown. Many sources of funds facilitated Faribault's downtown redevelopment, including \$5 million in private investment and \$750,000 in CDBG funds. The city has spent approximately \$300,000 in TIF funds downtown, primarily to acquire and clear sites for parking lots. The city says that private investment downtown was contingent on provision of more parking.

Johnston Hall (redevelopment, 1985). The district includes an historic building (formerly a monastery) located next to a hospital. Faribault created the district in light of a proposal by several doctors to purchase the building and convert it into a clinic. The doctors withdrew their proposal in late 1985, and the city hopes to find a new developer for the building.

Heselton Industrial Park (economic development, 1982). Faribault established an industrial park on land that previously was agricultural and swampy land. The park is privately owned and served by utilities. TIF has assisted two businesses in the park. The city provided a bus rehabilitation company with \$225,000 for land write-down and on-site improvements. In addition, a company that makes plastic containers started a plant in the park with \$85,000 for land write-down and on-site improvements.

FRIDLEY

All of Fridley's five districts are in a single, non-contiguous project area. The city has done no pooling of increments so far. The only bonds issued to date have been for the Center City district, totalling \$3.4 million.

Center City TID (pre-1979, 1979). Fridley established this district in light of the following problems: heavy traffic in a commercial district; lack of modern, visually-attractive shopping areas; multiple landowners at potential development sites. Primarily through acquisition, clearance, and write-down, the following developments occurred in the district: construction of two office buildings, a medical clinic (city officials say it would have located elsewhere in Fridley without TIF), and the remodelling of a shopping center. A market-rate housing development occurred in the district without TIF. The city also used TIF to finance a road to the clinic, a public plaza

and fountain, parking, and utilities. In 1985, Fridley completed construction of a police garage with tax increments.

Moore Lake TID (redevelopment, 1981). Among the types of blight cited in the TIF plan were non-conforming land uses, traffic congestion, and underutilization of prime land. While several market-rate houses have been built in this area since 1981, there have been no TIF expenditures, and no TIF assistance is currently foreseen.

North Area TID (redevelopment, 1981). The primary reasons for placing this area in a district were poor soils and a high water table. To date, there have been only minor TIF expenses (less than \$50,000). However, several multi-tenant speculative commercial buildings developed here since 1981.

TID 4 (economic development, 1983). The largest area of this non-contiguous district contained the existing Skywood Mall. Fridley is considering improvements to a major intersection near the mall in the future. To date, no TIF funds have been spent in the mall area. However, since 1983, the mall has been remodelled, and a motel and an office building were constructed in the district. In a separate area of the tax increment district, Fridley used TIF to finance \$30,000 in soil corrections, attracting a Minneapolis printing business.

TID 5 (economic development, 1984). The city used TIF to finance \$50,000 in soil corrections on a previously vacant site. An office building was constructed at the site.

GLENCOE

In 1985, Glencoe created a single project area that encompasses all three districts and includes over 100 blocks of the city. The city has issued no bonds for its tax increment districts.

Downtown TID (redevelopment, 1975). The district includes about 6 blocks of downtown Glencoe. Six projects have been financed, although no bonds have been issued. First, the city acquired and cleared buildings destroyed by an explosion, and a parking lot was constructed at this site. Second, the city bought and cleared lumberyard property; the land is still vacant. Third, the city bought a site for future development that is now leased for commercial use. Fourth, the city wrote down the cost of a vacant site that now houses professional offices. Fifth, the city funded a feasibility study for the lumberyard site. Sixth, the city refurbished all downtown street poles and installed more energy-efficient lights. The district has a \$200,000 reserve, and the city may use this to attract a mini-mall to downtown.

Housing/grocery TID (housing, 1983). This district consists of non-contiguous parcels. A 16-unit Farmer's Home housing project was constructed in 1983 without TIF assistance. The city used the tax increments to subsidize a grocery store that was renovating a building

on the east end of town. The city amended the district to include a third site where two businesses located without TIF assistance.

Hardees/motel TID (redevelopment, 1985). This district consists of non-contiguous parcels. It includes two businesses that received building permits shortly before TID certification (the motel received a \$30,000 land write-down, the restaurant received no TIF assistance). Previously these two sites were farm land and a city park. Several old downtown buildings were included in the TID to satisfy the blight criteria. The city will use the tax increments to construct a street and storm sewers at an industrial site on the east edge of the city; there may be industrial land write-downs in the future, too.

GOLDEN VALLEY

Valley Square TID (pre-1979, 1978). Golden Valley created this district to establish a focal point for the city and to relieve traffic on Winnetka Avenue. In 1978, the TID included several major retail centers, government buildings, a large greenhouse, and some housing. The city has issued three bonds in this district, totalling \$3.9 million. Taxes from four major developments are repaying the bonds: Calvary Senior Housing, which provides 200 units of subsidized and cooperative housing; two office buildings and one office/warehouse building. The warehouse/office building developed without a TIF subsidy. The primary TIF expenditures have been for land write-down and reconstruction of a municipal state aid street (Rhode Island Avenue). The city plans to issue \$6 million in bonds to subsidize a 122-unit apartment building and 210,000 square feet of office space. TIF will help write down the land, acquire right-of-way, re-route a street, and install new street lighting at a site now occupied by a greenhouse. There are no immediate plans to address the problems of existing commercial areas in the district, but the city hopes to have funds for these sometime in the future.

North Wirth Parkway TID (pre-1979, 1978). Prior to 1978, this site near Highway 55 and France Avenue contained houses, small businesses, and vacant railroad buildings. The city considered the land under-utilized and felt the existing uses detracted from the adjacent regional park. Golden Valley issued bonds totalling \$2.5 million to subsidize an eight-story office building and two four-story office buildings. TIF was used for land write-down, relocation expenses, and construction of streets and utilities.

Medley Park TID (housing, 1981). A developer who had planned construction of 30 market-rate townhouses in Golden Valley was unable to complete his project, and only six units were constructed. The city established a TIF district that included the remaining parcels of this developer's land plus an adjacent site. A \$360,000 TIF bond supplemented an equal amount of federal community development funds to provide a total write-down of the site. The developer built 30 units for low/moderate income families, and 30 market-rate units are being built. TIF also funded drainage improvements, street lighting, and nature trails.

Golden Hills TID (redevelopment, 1985). This district lies north of Highway 12 (soon to be Interstate 394) near what is called "Turner's Crossroad." The primary purpose for creating the district is to redevelop the area for more intensive use in conjunction with construction of the new interstate. Problems cited by the city in this area include inadequate parking, inadequate setback and landscaping, poor soils, incompatible land uses (such as an asphalt company and an unscreened equipment leasing firm), and underutilized buildings. The city plans to issue a total of \$27 million in tax increment bonds. Costs will include \$12.2 million for land write-down, \$3.2 million for relocation, \$1.6 million to bury power lines, and \$1.3 million for demolition. The city plans to complete the redevelopment by 1989. The only major development lined up so far is a hotel/office complex.

HIBBING

Downtown TID (redevelopment, 1979). This district contains 59 non-contiguous parcels in Hibbing's downtown. The city considered many of these parcels underutilized, but at least three parcels scheduled for construction were placed in the district to generate tax increment (these included a restaurant, a grocery, and a multi-tenant business center). The city has issued \$540,000 in bonds. TIF projects to date include: acquisition and write-down of a building for the city's Elks Club; building demolition and parking lot construction at the site of the old Elks Club; conversion of a vacant gas station into a restaurant with TIF for acquisition and site improvements; conversion of a vacant store into a restaurant with TIF for utilities and a sidewalk; purchase of new downtown lighting and traffic signals. Redevelopment of the vacant Androy Hotel, one of the key reasons for establishing the district, has not occurred. Several parcels in the district have been rehabilitated since 1980 without TIF assistance.

Wood Industrial Park TID (economic development, 1984). Two non-contiguous industrial sites are in this district: the 270-acre Wood Industrial Park and the 40-acre Mitchell Red Ore Industrial Park. Both were undeveloped prior to TID creation; the Wood site is a former mining company waste storage area. The city sold \$900,000 in tax increment bonds for the Wood site to supplement over \$5 million in state, federal, and IRRRB funds. \$275,000 in TIF will write down land for a chopsticks manufacturer, the only tenant lined up so far. \$463,000 in TIF will leverage a \$1.1 million federal grant for roads and utilities. Development of infrastructure at the Mitchell Red Ore site will not begin until 1987.

Scattered Industrial Site TID (redevelopment, 1985). The district includes 12 vacant or partially-vacant buildings throughout Hibbing that are targeted by the city for more intensive use. Two developments have occurred. A car dealer used a \$70,000 TIF write-down to move his business from downtown Hibbing to a larger, vacant building in an industrial area. Second, an industrial firm (Hibbing Printed

Circuits) bought a vacant industrial building with a \$125,000 TIF write-down. The city's planned expenditures include write-downs at two additional sites and service road construction (affecting two parcels). A \$300,000 bond has been issued.

HUTCHINSON

TID 1 (redevelopment, 1980). In 1978, Hutchinson established two tax increment districts that encompassed the entire downtown area. In 1979, the city created an economic development district in an industrial park. In 1980, the city combined its three existing districts and added a fourth non-contiguous area (the site of a planned shopping mall); thus, the city now has a single TID. The first tax increment bond (\$650,000) primarily funded construction of a senior citizens' high-rise and purchase of equipment for the building's kitchen. The high-rise site previously contained dilapidated houses near downtown. The second bond (\$135,000) helped convert a vacant downtown department store into retail, office, and restaurant space. TIF funded an \$83,000 write-down and the \$10,000 installation of utilities. The city's next TIF expenditure (\$300,000) funded parking construction downtown. The tax increments for the parking came from Hutchinson's new shopping mall, which was attracting businesses from downtown. Hutchinson financed a portion of the mall's storm sewers (\$10,000) with TIF. The city's most recent TIF bond (\$150,000) may be used to rehabilitate an old hotel/retail building into apartments and retail space. In addition, Hutchinson plans to use its tax increment reserve (now at \$300,000) to finance a revolving loan fund for city businesses. The loans may help businesses install sprinklers and remodel storefronts; they may also subsidize non-profit ventures. Hutchinson also plans to use TIF to construct a \$330,000 railroad spur to its industrial park.

LAKEVILLE

Despatch Industries TID (redevelopment, 1980). A Lakeville oven manufacturer needed to expand but was surrounded by streets and railroads at its existing site. Across the street, the city had a 20-year old fire station that was too small. The city vacated the street and provided the company with the fire station (\$150,000 value) for \$1. The company paid for the land and then used \$3 million in industrial revenue bonds to increase their operating space by 50 percent. The city built a new fire station, and tax increments pay for 65 percent of the fire station bond payments (the city levies the rest).

McStop TID (economic development, 1984). This 15-acre district lies at the intersection of Interstate 35 and Dakota County Road 70. The prior use of this land was agricultural. The project, developed by the McDonald's Corporation, contains a restaurant, 130 hotel rooms, 85 motel rooms, a convenience shopping center, and a gas station/car wash. "McStop" is designed to attract travellers as they enter the

Twin Cities from the south. Sewer and water pipes were one and one-half miles from the site, so the city issued \$1.3 million in TIF bonds to build a water tower, a well, and sewer lines. Special assessments and city-wide water connection charges provided an additional \$1.4 million. The city may use future increments to redesign and add lanes to the County Road 70 bridge over I-35.

Senior housing TID (housing, 1984). Prior to completion of this development, Lakeville did not have subsidized housing for seniors. The city purchased five homes next to the central business district and sold them to a non-profit developer. TIF subsidized a \$135,000 write-down for the 24-unit complex with tax increment bonds. Federal community development funds helped construct an adjacent community center. Tax increments currently pay one-third of the TIF debt service, and a city levy pays the other two-thirds.

Meadows North TID (redevelopment, 1984). This site was adjacent to a lake and to former railroad land. Most recently, it housed an electrical contractor's business and a buried junkyard. Residential development nearly surrounded the site. The city issued a \$125,000 bond to acquire the site, excavate the junk, replace the soil, and write down outstanding special assessments. The site will contain market-rate residential housing in the future.

Air Lake TID (economic development, 1984). This 15-acre site was farmland prior to creation of the TID. The city issued a \$260,000 bond to subsidize a land write-down for the Toro Corporation. Toro consolidated smaller outlets (including one in Bloomington) into this large distribution center. Lakeville created the TID primarily to offer a competitive bid for Toro's business.

Mills Fleet Farm TID (economic development, 1985). Mills Fleet Farm will build a store on agricultural land. The company agreed to locate at the site only if the city makes improvements to an Interstate 35 frontage road. Lakeville plans to issue a \$600,000 bond in 1986 to finance part of the roadwork; special assessments will fund the remainder.

MANKATO

Downtown TID (pre-1979, 1973). Most of Mankato's downtown lies in this district. TIF has supplemented a variety of state and federal funds to help produce major changes in the downtown area. The city issued a \$315,000 bond in 1973 to acquire and clear a site for office building development. In 1978, the city issued a \$745,000 bond to finance soil improvements, utilities, and construction of a parking ramp for a new downtown hotel. In 1980, a \$2.5 million bond financed construction of a ramp next to the downtown mall. Mankato used federal urban renewal funds to spur the mall, which enclosed several existing stores and attracted several major tenants. The city also issued a \$280,000 tax increment bond to demolish a vacant department store and construct a municipal parking lot.

Honeymead TID (pre-1979, 1974). A Fridley-based company considered several Minnesota cities for relocation of company headquarters and consolidation of operations. The company had an existing Mankato plant, but the housing that surrounded the site prevented private expansion. The city used TIF to acquire and demolish 34 houses to facilitate the expansion.

Valley Park TID (pre-1979, 1977). Mankato created the district to encourage re-use of vacant buildings on Mankato State University's lower campus. To date, the primary use of TIF has been the construction of parking at two sites, financed with \$1.1 million in bonds. In addition, the city acquired one building for a housing development and demolished another. Buildings in the campus are now occupied by government offices and over 350 apartments. Mankato enlarged the district in 1983, adding nearby, older homes that often flood. The city hopes to replace storm sewers and streets in this area and develop additional housing.

Washington Park TID (redevelopment, 1980). The city issued a \$255,000 bond to acquire a vacant hospital. TIF also helped demolish part of the building, add a congregate care facility, and improve the parking lot. In addition, two houses were demolished and the residents relocated. The development contains 108 federally-subsidized housing units for the elderly.

Riverside TID (redevelopment, 1981). This 24-acre site contained vacant land in a floodplain between Highway 169 and the Minnesota River. Mankato spent \$130,000 to construct a dike and pump station along the river. A fast food restaurant and a 69-unit motel were built at the site.

Lime Valley Industrial Park (redevelopment, 1981). Originally, the city intended to acquire and prepare land for a corn wet-milling plant. This would have required \$13.9 million in tax increment bonds. The plant is no longer planned, and plans for the area have been scaled down. The city will spend \$100,000 for sewer, water, and roads in the industrial park. TIF will subsidize a write-down of the special assessments for these improvements. Problems with the site include bedrock and a high water table. The city anticipates construction of a new industrial building and grain mill at the site.

Willard Street TID (economic development, 1981). The city acquired and demolished several dilapidated houses with city funds. Mankato wanted the land for street right-of-way and for a market-rate, 10-unit housing development.

Chesley Company TID (economic development, 1981). Prior to TID creation, this site was mostly vacant. Bedrock near the land's surface presented an obstacle to development. A truck/trailer sales and service facility across the road from the site wanted to expand. The city issued a \$100,000 revenue bond to finance acquisition, structure demolition, and relocation.

HyVee TID (economic development, 1983). Most of the district was acquired and cleared with federal funds prior to the district's creation. The city used TIF to acquire and remove a railroad line and to make soil corrections for a grocery store development. Mankato also acquired and cleared land to facilitate relocation of a car dealership. The city expects to provide additional assistance to developers of a mini-mall in the district. \$680,000 in tax increment bonds have been issued to date.

Inn Towne TID (economic development, 1983). Mankato issued a \$675,000 bond to finance the redevelopment of a vacant motel. The city acquired the site, sold the building to a developer, and kept the land. The developer converted the building into 38 apartments, 20 percent of which are intended for low/moderate income persons.

Union School TID (economic development, 1984). A developer requested tax increment assistance from the city for conversion of a vacant 1919 school into office space. Mankato issued a \$210,000 bond to finance a total write-down of the land. The building now houses professional offices.

Tow Distributing TID (economic development, 1984). The site previously contained a limestone quarry and a dump. A \$180,000 tax increment bond subsidized sewer and water extensions to the site, a lift station, and sidewalk installation. A 40,000 square foot wholesale distribution facility located in this district.

South Broad Street TID (economic development, 1985). The city will use tax increments and a \$50,000 grant from the Minnesota Housing Finance Agency to finance conversion of a church into office space and housing. The facility will have 15 sleeping rooms for low income people needing temporary shelter. The city internally financed a \$10,000 loan to the developer for acquisition, and tax increments will repay the loan.

MARSHALL

Marshall's first four tax increment districts are in one project area, and the Schwan's district is in a second project area. The city has done no pooling of tax increments to date.

Minnesota Corn Processors TID (redevelopment, 1982). Much of this 90-acre site previously was a sewage lagoon. A southwest Minnesota farmers' coop conducted a feasibility study and considered several Minnesota sites for a wet-milling processing plant. They selected the Marshall site primarily because of the size of the parcel, the promise of future rail access and utilities, and the existence of an adjacent waste water treatment facility. Marshall issued a \$3.2 million bond to write down the land, provide soil improvements, construct a railroad to the site, provide utilities, and construct streets. About \$800,000 of the improvements occurred outside the TID.

Downtown TID (redevelopment, 1982). Marshall issued \$385,000 in bonds to subsidize two 30-unit, market-rate apartment buildings and a law office. The city purchased and cleared five old houses, reconstructed and widened two adjacent streets, and provided utilities, curb and gutter, and sidewalks. The city says the street improvements would have been years away without TIF; there were stronger street needs elsewhere in the city. One of the streets was a municipal state aid street.

Independence Park TID (housing, 1983). The city established this TID to capture tax increments from a 30-unit housing project that was being planned. The districts consists only of this housing site. Marshall provided no assistance to the housing project. The city will use the increments generated from the site to finance development of a city park about one mile from the TID. The "park" is currently a cornfield, but eventually it will contain an amphitheatre, a lake, a nature area, and recreation facilities. TIF will finance about 40 percent of the park's first phase of construction. Creation of the TID allowed the city to start park construction sooner than it otherwise could have.

Marshall Labs TID (redevelopment, 1984). At the time of this district's creation, the site contained several vacant buildings that had once housed an egg-processing plant. Marshall issued a TIF bond to provide a \$60,000 write-down to an industrial products/research firm from the Twin Cities.

Schwan's TID (redevelopment, 1985). The district includes two non-contiguous sites: the headquarters of Schwan's Sales Enterprises and an industrial park site containing several of Schwan's buildings. All buildings in the district have been built within the past 15 years. The city created the district to retain Schwan's ice cream production plant in Marshall and to facilitate Schwan's expansion of a cold storage facility and construction of a pail-making plant. Schwan (an employer of about 2,000 people in Marshall) was planning to vacate its ice cream production plant, and South Dakota sites were under consideration. Most of Marshall's TIF assistance will be provided at the industrial park site. The main expenses will be Schwan's relocation costs, site grading, and parking lot construction. Lesser costs will include street reconstruction and utility provision. A \$550,000 bond covers the TIF costs.

MENDOTA HEIGHTS

TID 1 (redevelopment, 1981). The entire city is in the empowering project area. The TID includes all city land subject to airport building restrictions (including a pre-existing business park), some housing areas unserved by city utilities, and scattered sites not in conformance with existing zoning. To date, the major TIF expenditure in the district has been construction of the city's new fire station (\$825,000), completed in 1985. In addition, the city provided \$400,000 in utility assessment write-downs to property owners at the

site of a future business park and to the Minnesota Department of Transportation (which built a maintenance garage here). The city is writing down assessments from 15 to 60 percent for an area that has high costs for installation of public utilities; the write-downs will be given over a 20-year period. Mendota Heights' other major expenditure to date is for 45 percent of the cost of road reconstruction on a county state aid highway through the business park. The city hopes to eventually subsidize utility extensions to some housing areas, but not until at least 1988 (this would occur in conjunction with a MnDOT construction project). Other future expenditures may include street extensions and noise-proofing subsidies in the business park. Mendota Heights has issued \$1 million in bonds, and the city had a \$600,000 TIF reserve at the end of 1985.

MINNEAPOLIS

At the end of 1985, Minneapolis had 35 active tax increment districts (20 pre-1979, 9 redevelopment, 3 economic development, 3 housing). We focused on the 12 most recent districts (those established since 1980). In December 1984, Minneapolis refinanced the general obligation bonds issued for 20 tax increment districts; the city issued a single revenue bond in their place. Chapter 2 provides a description of this refunding.

Franklin Avenue TID (redevelopment, 1981). Prior to TID creation, this scattered site district consisted primarily of old commercial structures and some residential buildings. The city issued a \$650,000 tax increment bond to supplement \$1 million in UDAG funds and \$750,000 in industrial development bonds. The city used TIF primarily to finance land acquisition, demolition, relocation, and the project's administrative expenses. Four major businesses located or expanded in the district: a grocery store, a drug store, an auto parts store, and a wholesale business. The city hoped this development would spur other development in the area, but activity has been slower than expected. Minneapolis recently agreed to acquire a site in the district for a large commercial/light industrial development.

Elliot Park TID (redevelopment, 1981). This district contains 130 parcels in a residential neighborhood just south of downtown. Prior to 1980, there had been no major rehabilitation projects in the neighborhood for 30 years. With a combination of TIF, UDAG, and CDBG funds, the city has induced several building rehabilitations and two new apartment buildings in the district. There have been no TIF bonds issued. Instead, the city has financed acquisition, relocation, and public improvements with federal funds; for several developments, these funds have been and will continue to be reimbursed by tax increments. Approximately 275 housing units built or proposed in the district are using TIF; about the same number of units built received no TIF assistance.

Centre Village TID (economic development, 1981). Most of this site was a surface parking lot prior to creation of the tax increment district. Minneapolis issued \$16.4 million in tax increment bonds for

this development, primarily to finance a 1200-space parking ramp (TIF also financed land acquisition and a skyway). The building constructed over the parking ramp includes three floors of office space, six floors of hotel rooms, and nine floors of condominiums. Prior to Minneapolis' 1984 bond refunding (which pooled the debt service of 20 districts), Centre Village's tax increments were insufficient to meet debt service on its bond. Parking fund revenues financed most of the shortfall.

Nokomis Homes TID (redevelopment, 1982). Minneapolis issued a \$1 million tax increment bond to redevelop the site of a vacant school. TIF financed demolition (\$165,000), a land write-down (\$215,000), and utility, curb, and sidewalk replacement (\$219,000). The site now contains 208 condominiums. The city will recoup its \$600,000 investment from the developer if the units cease to be cooperatives during the first 20 years of the district's life.

Symphony Place TID (housing, 1982). The city issued \$20 million in housing revenue bonds to develop 250 rental units at a site that previously contained a parking lot. The base of this structure is a parking ramp. The city agreed to pay the developer 95 percent of the development's tax increments over a 19 year period. In return, the city will receive an option on half of the ramp at the end of this period. The city may make this a municipal ramp or it may re-sell the ramp to the Symphony Place owners.

Central Avenue TID (redevelopment, 1983). When established, the district consisted of eight parcels with commercial and residential structures. The city has issued no TIF bonds in the district. Instead, Minneapolis financed \$700,000 in demolition, land write-down, and relocation with city development funds. These funds will be reimbursed by tax increments. The development under construction is 15,000 square feet of retail space and 95 rental housing units. The city used CDBG funds in the project area for streetscaping, a market study, and business loans.

110 Grant TID (housing, 1983). Prior to 1983, this one-block area was part of Minneapolis' Loring Park TID. Minneapolis cleared the site while it was part of the Loring district, so the land was vacant at the time the city created the housing district in 1983. Developers built a 320-unit rental housing structure at the site. The developer will receive up to 95 percent of the tax increments for up to 12 years in the form of an interest rate reduction loan. In effect, city officials intend for this subsidy to compensate the developer for making 20 percent of the units affordable to low/moderate income persons. Minneapolis also issued \$27 million in housing revenue bonds for the development.

International Market Square TID (economic development, 1983). The tax increment district contains the former office/manufacturing facility of the Munsingwear Corporation. The plant closed in 1982 and was vacant at the time the city created this district. TIF is not being used to provide direct subsidies for development at the site.

Instead, up to 95 percent of the district's tax increments help to provide security enhancement for the "Minneapolis Bond Fund." The city has used this fund to issue over \$35 million in bonds so far, including \$9.9 million for the Munsingwear site. No TIF bonds have been issued. The security fund (of which the Munsingwear tax increments are a small part) will be used only if any of the Minneapolis Bond Fund projects have problems meeting debt service. Rehabilitation of the Munsingwear facility resulted in an interior design merchandising center.

Conservatory TID (redevelopment, 1985). The tax increment district includes about one block of property on the downtown Nicollet Mall. The city does not anticipate the sale of TIF bonds for this site. Instead, the city's development account will loan \$2.4 million to the project for acquisition, demolition, relocation, and street restoration work; tax increments will reimburse the development account. The city anticipates development of a four to six story retail/office facility. Currently, the site contains retail and office space which the city deemed structurally deficient and economically obsolete.

Chicago Avenue Medical Building TID (redevelopment, 1985). The city plans to acquire 14 parcels (mostly residential) containing structures which the city says are blighted. TIF bonds will finance expenditures of nearly \$1 million for acquisition, relocation, and demolition. A medical office building will be constructed at the site.

Chicago/Lake TID (redevelopment, 1985). The district includes five commercial buildings and the parking lot of a large department store. A developer proposes building 160,000 square feet of retail space at the site. The primary TIF expense will be a \$5 million municipal parking ramp. In addition, the TIF bonds will finance over \$1 million in land acquisition, relocation, and demolition.

Laurel Village TID (housing, 1985). Currently, this four-block tax increment district is part of a 12-block project area. The district includes a mixture of commercial structures, apartment buildings, and parking space. A \$10 million tax increment bond issue will primarily finance land acquisition, demolition, and relocation. Housing revenue bonds will subsidize a 1200-unit housing development in the district. The city may enlarge the project area in the future to use TIF for broader streetscaping plans, particularly on Hennepin Avenue.

South Nicollet/Convention Center TID (redevelopment, 1985). This district includes nearly five blocks in downtown Minneapolis, including three and one-half blocks with Nicollet Mall frontage. The city recently issued \$44.8 million in tax increment bonds, \$30 to \$35 million of which will be used for land assembly and demolition in the tax increment district. A developer proposes building 800,000 square feet of commercial and office space; a second developer proposes a hotel in the TID. From \$10 to \$15 million of the bond issue will

finance site assembly and preparation for a planned expansion of the existing convention center, which is in the project area, but not in the TID. If Minneapolis does not receive legislative authorization to levy a city sales tax for the convention center, the city may use tax increments from the North Washington Industrial Park TID to retire up to \$10 million in bonds sold for site acquisition costs. (North Washington is a 1973 TID that is not in the downtown area.)

MOUNTAIN IRON

A single project area contains both of Mountain Iron's districts. The city has not pooled increments from the districts so far, but there are plans to do so in the future.

TID 1 (redevelopment, 1983). This site, at the intersection of highways 169 and 53, was vacant land before 1983. The city acquired the land in 1980 and constructed utilities in 1981. The primary problems with the site were soil problems and lack of frontage roads. The city used a \$400,000 Small Cities grant to construct a frontage road north of 169 and to prepare sites. All lots in the district are currently developed. To date, five businesses have located in the district. The city issued a \$360,000 TIF bond, of which \$35,000 has been spent (for TIF plan preparation and minor site improvements). Increments generated by the businesses in the district more than cover the bond's debt service. The city expects to expand the district eventually and spend its remaining bond proceeds for frontage roads and site improvements in the expansion area. This TID is in a state enterprise zone.

TID 2 (redevelopment, 1985). The district contains two non-contiguous parcels that are part of a state enterprise zone. One may be the future site of a carpet manufacturing firm, and the other site contains a new Dairy Queen. The city received a UDAG for the manufacturing plant, and a TIF bond may finance site work. The firm would employ at least 200 people. The Dairy Queen located on city recreation land. The city financed clearance of the land, and TIF financed a complete write-down of the land (\$25,000).

NEW BRIGHTON

A single project area contains all of New Brighton's districts. The city has not pooled increments but may do so in the future.

TID 1 (redevelopment, 1981). This 12-acre site previously contained one home, some vacant land, and a drainage ditch. The city says the site has considerable soil problems. New Brighton used TIF to acquire the site for \$1.75 million and write down the land to \$.25 million. In part, the write-down will compensate the developer for the soil corrections needed. The city signed an agreement in 1985 for development of a 150-room hotel at the site. The original TIF plan called for construction of a public safety building in the district,

but the city no longer intends to use its bonds for this purpose. The city will use tax increments to fund improvements to a city park within the district.

TID 2 (redevelopment, 1981). This district is part of an area that the city wants to develop as New Brighton's downtown or focal point. Currently the site has several old buildings, and the parcels are owned by many different people. In addition, peat-based soils present problems at the site for potential developers. The city would like office space at the site, but there are no development agreements to date. There have been no TIF expenditures.

TID 3 (redevelopment, 1981). While this site was highly attractive for its location adjacent to Interstate 35W, the existing land uses contributed little to the city's tax base. Sandblasting, truck storage, tree stockpiling, and junk vehicle storage were among the area's previous uses, and streets at the site were unpaved. The city issued \$1.4 million in TIF bonds to write down the land (the developers cleared the site), and New Brighton also used the bonds to establish a reserve fund for industrial development bonds. \$5.5 million in industrial development bonds subsidized construction. The resulting development was 127,000 square feet of office/warehouse space, most of which is now leased.

TID 4 (redevelopment, 1982). This site is adjacent to Interstate 694 and to tax increment districts 1 and 2. The site had soil problems, and it had a 50-year old sewer main that needed to be moved. New Brighton used TIF primarily for site excavation and soil work. A medical-clinic is now at the site (the city issued \$1.9 million in industrial development bonds for construction).

TID 5 (redevelopment, 1984). Prior to TID creation, this district contained three pieces of property: one lacked street access, one contained a vacant building, and two were tax-forfeit. A \$300,000 TIF bond primarily funded a land write-down, allowing the developers to clear the site and do some soil corrections. A tool and die company and a printer built new buildings at the site with industrial development bonds.

TID 6 (redevelopment, 1985). New Brighton will use TIF to acquire and clear 14 single family homes along one of the city's main streets. Most of the homes are 60 to 70 years old, and the city concluded they are not worth moving elsewhere. Future developments planned include 60 market-rate apartments, 18 single-family homes, and an office building. TIF bonds will fund \$1 million in demolition, soil improvements, holding pond construction, and land write-down.

TID 7 (redevelopment, 1985). This eight-acre site previously contained an old motel and vacant land, and a portion of the land was used as a dumping area. The city issued a \$550,000 bond to finance acquisition, demolition, and clean-up of the district. AT & T will build an office/warehouse structure at the site that will consolidate distribution centers from Minnesota and other states.

TID 8 (redevelopment, 1985). Prior to district creation, this area contained three vacant buildings, an equipment storage yard, a contractor's office, and construction debris. TIF will finance \$700,000 in land write-down and soil corrections at the site. Two manufacturers from the metropolitan area will build at the site.

NEW PRAGUE

Mill Pond TID (redevelopment, 1980). The city had three sites for possible Section 8 housing development, and the Minnesota Housing Finance Association selected the Mill Pond site. At the time, the site contained a rented house and some vacant land with soil problems. After MHFA's selection, New Prague established a TID, primarily to write down the land and provide soil corrections. A \$256,000 bond was also used for utilities and construction of alleys and driveways. A 44-unit project resulted.

Westgate TID (housing, 1980). Like the previous TID, MHFA selected the development proposal for a low/moderate income housing development. The developer had an option on this property near downtown. The TID previously was farmland, and the city used TIF to write down the site and to construct sewers, streets, and water mains. The resulting development is a 37-unit, federally subsidized housing project. A \$175,000 bond funded the project.

Super Valu TID (redevelopment, 1981). An existing New Prague grocery store wanted to expand. The city used TIF to finance a \$70,000 write-down on land containing a vacant chicken hatchery. The grocer constructed his new store with \$825,000 in industrial revenue bonds.

Downtown TID (redevelopment, 1983). The district previously contained three tin sheds that had been vacant for 20 years. The site is one-half block from the city's main street. A bank relocated at the site without TIF assistance, and the city established the district to capture increment from the new bank. The city's project area includes the entire downtown, and the city is planning to spend the increments for downtown sidewalk or alley improvements.

NORTHFIELD

River Park Mall (pre-1979, 1975). Prior to TID creation, this site contained a tire warehouse, a vacant business, and two houses. The primary TIF expenditure was a \$127,000 land write-down, financed with a tax increment bond. The resulting development houses six retail stores, the largest of which is a grocery store. This store was downtown before moving to the mall, but its former location was too small.

Jonathan/Hills TID (pre-1979, 1976). Northfield acquired land occupied by a beer warehouse. A \$65,000 bond financed the land

write-down and clearance. The developer built 13 market rate town-houses at the site.

Third Street Grant TID (pre-1979, 1978). The site contained a wood-frame structure considered a fire hazard by the city. A taxi service had its offices in the building. The city issued a \$45,000 bond to finance write-down and clearance of the property. The resulting development was a professional office building for four Northfield businesses.

Woodley and Winona TID (redevelopment, 1983). The city used TIF to acquire and clear a one-parcel, 1.1 acre site. The site contained one house and seven dilapidated sheds. A \$70,000 bond financed the TIF costs, which helped produce nine market-rate townhouses at the site.

Computer Controlled Machines TID (economic development, 1984). A 5-year old, rapidly growing Northfield business wanted to expand, but it lacked capital for the expansion. The company considered locations in Iowa and South Dakota. Northfield established a TID on agricultural land that was slated for industrial development. A \$150,000 tax increment bond subsidized a write-down of the land and utility installation. The company used a small business loan to finance a building eight times the size of the company's existing space.

Cardinal Glass TID (economic development, 1984). A Minneapolis-based firm that coats plate glass wanted to expand, and it considered sites in three Minnesota cities and three other states for a new production plant. A \$220,000 bond financed a land write-down and the installation of utilities and streets. The development brings over 50 new employees to the city and strengthens the city's industrial area. Northfield says that legislative change in the state's sales tax was probably the key factor in the company's decision to build in Minnesota (although state rules passed later did not qualify this project for a sales tax exemption).

NORTH BRANCH

North Branch has a single project area that contains all three of the city's tax increment districts. The city intends to spend most of the increments generated by the three districts on storm sewer construction in the southwestern part of the city, mainly to open new land for housing (the projected cost of the sewer project will be \$364,000). The city has issued no bonds for its districts to date.

TID 1 (economic development, 1984). The TID contains two non-contiguous downtown parcels on the same block. A law firm moved into a building on one parcel shortly before the district was created; the firm was remodelling the building without TIF assistance. The second parcel was vacant but being considered by a dentist as a site for an office. The increments generated by these two developments will be spent for: (1) drainage corrections in an alley behind the TID; (2)

drainage corrections in a portion of an alley east of the TID; (3) demolishing the rear of a building in another block and opening up an alley to traffic.

TID 2 (redevelopment, 1984). Developers built 14,000 square feet of retail space at this downtown site. Previously, the site contained a house. The city acquired the property and removed the house. TIF subsidized foundation work, a parking lot, and utilities. In addition to housing several businesses, the new building will house the city's library for two or three years.

TID 3 (housing, 1984). A 12-unit Farmers Home complex was built in a previously undeveloped area. TIF did not induce the development, but it did help construct an adjacent gravel road (the cost was less than \$2,000). Special assessments paid for utilities. The increments from the site will help pay for the city's future southwest storm sewer project, which will serve an area that includes the TID.

PRINCETON

Downtown TID (pre-1979, 1978). This district contains nearly six blocks of Princeton's downtown, bisected by the city's main street. There has been little redevelopment of the western half of the district; there has been substantial redevelopment of the eastern half, including the construction of two mini-malls. A partnership of existing businesses developed the first mall on a block previously occupied by old commercial buildings and a car dealership. Developers built the second mall in a block that previously contained a car dealership and an old house. A \$2 million TIF bond subsidized land write-downs (from \$6 per square foot to \$1 per square foot), relocation costs, and some minor utility and alley improvements. In addition, the malls received \$600,000 in federal UDAG assistance and \$2 million in industrial revenue bonds. Smaller downtown projects that received TIF assistance included the acquisition and clearing of land for a print shop and an American Legion building, and the purchase and rehabilitation of a vacant theatre.

Industrial park TID (economic development, 1981). The city created the district because there had been little development of an industrial park since its establishment in 1972. The industrial park's largest current employer, a cabinet manufacturer, came to the park in 1981 with UDAG assistance shortly before creation of the district. Originally, Princeton planned to use TIF for public improvements to the park, including a district heating system, an incinerator, a railroad spur, streets, and utilities. However, the city installed streets and utilities primarily with a state Small Cities grant, and the other improvements will not be done during the district's life. Instead, Princeton uses TIF to write down lot prices (from \$16,000 to \$1,000) and the city used \$300,000 in tax increments to finance construction of a federal flight service station. Princeton owns the building and leases it to the federal government for \$1 per year. The federal government considered offers from about 20

Minnesota cities during site selection for the state flight service station.

PROCTOR

TID 1 (redevelopment, 1983). This district lies next to Interstate 35. Prior to TID creation, the site contained a motel, a restaurant, a general contractor, a heavy equipment distributor, and several vacant parcels. The primary reason for creating the district was to facilitate reconstruction of a frontage road and construction of a frontage road bridge over railroad tracks. There has been no bridge on the frontage road since construction of the freeway ten years ago. The primary generator of tax increment is an outdoor advertising firm that relocated its headquarters in the district from Duluth without TIF assistance (the company received \$950,000 in industrial revenue bonds). A convenience store is currently being built in the district without TIF assistance. The city may use next year's increments for business inducements, and increments thereafter will finance the frontage road. The city will issue a tax increment bond for the road project (probably about \$1.5 million). The federal Interstate Substitution program will fund 70 percent of the cost, and the state will fund seven percent.

ROBBINSDALE

The city has two project areas. Together, the project areas encompass the entire city.

Scattered Site Housing TID (pre-1979, 1968). In 1968, Robbinsdale produced a list of 400 sites that were candidates for housing redevelopment; the city added some sites to the list during the 1970s. Most of these sites have substandard housing with declining property values, while some others have poor soils. The city acquires properties on the list when they come up for sale, and usually the sites are cleared and new houses built. The city does not freeze the assessed value of the sites until they are acquired. Thus, the TID continues to grow as new sites are acquired. Vocational-technical institute students have built many of the houses. To date, nearly 200 market-rate units of housing have been created at the sites. Robbinsdale funded the projects internally until 1979, when a \$1 million bond reimbursed the city for past projects. The bond continues to fund projects, and the city's increments exceed bond debt service by about \$100,000 annually. Some of the district's surplus tax increments fund housing redevelopments at sites not included in the TID.

"Project Four" TID (pre-1979, 1978). The district includes Robbinsdale's primary commercial area and a residential neighborhood. The city felt that many parcels were too small for development. There have been three bond issues for the TID: two general obligation bonds totalling \$840,000, and a \$690,000 revenue bond. The largest development has been construction of a bank (TIF subsidized a land write-down

at a site that previously contained old commercial and residential buildings)). In addition, one of the scattered site housing projects is now in this district, contributing over \$450,000 in captured assessed value. A garden store built a new business at the site of a lumberyard, using tax increments for land acquisition, land write-down, and storm sewer work. The district had \$1.5 million in excess increments at the end of 1984, and Robbinsdale plans to use the increments for a major office/retail development.

TID 3 (housing, 1985). The district currently contains three single-family homes and state highway right-of-way. Robbinsdale will use \$112,000 in surplus increments from the Project Four TID to finance a land write-down. The result will be a 25-unit Section 8 apartment building for handicapped persons.

ROSEVILLE

All four of Roseville's districts are in a single project area that encompasses over two-thirds of the city.

TID 1 and TID 2 (redevelopment, 1982); *TID 4* (redevelopment, 1985). Roseville recently issued \$26 million in tax increment bonds, primarily for for TID 1 and TID 2. The primary public improvement will be construction of a bridge over Interstate 35W at County Road B-2. When created in 1982, each of these two scattered site districts contained parcels north of the Rosedale Shopping Center and parcels northwest of the I-35W/Highway 36 junction. TID 1 primarily contained sites with inappropriate land uses (e.g., housing in commercial/industrial areas) and substandard structures. TID 2 primarily contained land with poor soils. In 1985, Roseville added sites to each district to accommodate new development. In addition, the city placed the TID 1 and TID 2 parcels that were not developing in a new district, TID 4. Roseville plans to make street and sewer improvements in TID 4, most of which is at the I-35/Highway 36 junction. Roseville is pooling tax increments from the first two districts to support its expenditures. Development north of Rosedale will consist of two malls. In TID 1 and TID 2, the city has agreements for several developments, including three office complexes, over 200 housing units, a hotel, and a warehouse/office building.

TID 3: Villa Park (redevelopment, 1985). Prior to TID creation, this site was vacant land with poor soils. Roseville issued a TIF bond to make \$225,000 in soil corrections. The resulting development will be 100 units of housing for senior citizens.

RUSHFORD

TID 1 (redevelopment, 1980). Rushford was a boom town at the turn of the century, and many of the buildings in town date from that era. The city established a TID to clear wood frame buildings and to

encourage downtown business development. Since 1981, an impressive number of business relocations and expansions have occurred with a combination of TIF, private, and federal community development funds. The city estimates that 10 businesses in this 125-parcel district have received direct TIF assistance, primarily financed by \$730,000 in bonds. Major projects involving TIF included: Norsquare Mall (demolition of five buildings, land write-down for two businesses, interest rate write-down for three businesses, construction of a parking lot); expansion of a grocery store (TIF paid for utilities and parking); demolition of a building and construction of parking for a restaurant; bowling alley (the city used CDBG funds for acquisition and clearance, TIF for a parking lot); acquisition of a building to facilitate the relocation of three businesses. In addition, the city financed soil corrections for a metal fabrication plant and wrote down utilities for a molding factory and an implement dealership. The city added a non-contiguous, agricultural parcel to the district in 1983; no development has occurred.

ST. PAUL

Downtown and Seventh Place TID (pre-1979, 1974). The district originally included 37 blocks of St. Paul's downtown, including 12 blocks that were already being redeveloped through the federal Urban Renewal program. A \$500,000 tax increment bond financed planning and design studies in 1974. In 1977, a \$4.6 million tax increment bond financed acquisition and sitework for a ramp at the Minnesota Science Museum plus two downtown skyways. In 1978, due to a lack of downtown redevelopment, the city changed the TID boundaries (19 blocks were taken out, four were added), and the city refinanced its earlier bonds. Most of an additional \$6.5 million bond issue financed development of Town Square, a retail/office complex with an indoor public park. Since 1981, St. Paul has loaned \$7.8 million in tax increments to the city's district heating system for new construction, and the loans will be repaid with heating system revenues. In 1982, St. Paul added one block to its district: the site of the Galtier Plaza development. A \$3.15 million special obligation tax increment note financed soil and foundation work, skyway construction, and public areas in the retail portion of the development. In 1983, St. Paul sold its civic center to private interests and entered a 25-year lease for the facility. Tax increments and TIF interest earnings will pay an estimated \$141 million in lease payments during this time (82 percent of the lease). In 1985, the city issued \$10.2 million in tax increment bonds for the World Trade Center, financing a ramp, land acquisition, and foundation work. Other uses of tax increments in St. Paul's downtown include construction of three skyway bridges (in addition to the those noted earlier), clearance of a parking ramp, and partial support of the ongoing maintenance and operations expenses of Town Square Park.

Park Nursery TID (pre-1979, 1977). The site previously housed a nursery in a residential neighborhood. The nursery was interested in leaving the site, and the city used tax increment financing to acquire

and clear the site. The resulting development was 240 condominiums for the elderly and 60 townhouses. In addition, tax increments are financing major improvements to an adjacent city park, including: creation of a buffer between the park and the development; construction of a new gymnasium and activity rooms at an existing recreation center; construction of a playing field, tennis courts, racquetball courts, and a children's playground. A \$2.1 million tax increment bond financed the district.

Energy Park TID (redevelopment, 1981). This 230-acre district contained railroad right-of-ways, gravel pits, and a stadium. The city used TIF to induce re-use of the old railroad buildings and to produce a mix of commercial, industrial, office, and residential uses. Tax increment revenue bonds will supply \$30 million for the project, approximately half of the public financing. The primary TIF use is land acquisition, with lesser amounts for grading, storm sewers, streets, and an energy plant. Major projects completed to date include a retail complex (Bandana Square) and 400 housing units.

Scattered Site TID (housing, 1981). The district includes 18 non-contiguous sites, all slated for housing development (some are completed). Only three of the sites have received TIF assistance. Two of the sites were largely vacant, while the third contained dilapidated structures. The other 15 sites are being developed with a variety of public and private funding sources. No TIF bonds have been issued, and the TID had a \$310,000 reserve at the end of 1984. The city may expand the district to include additional sites for housing development.

Hammond Building/Iris Park Place TID (economic development, 1982). St. Paul established this district as part of a broader plan to revitalize a strip commercial area (the "Midway" area). The district contains a three-story building which, in 1982, was partially vacant and partially used as a warehouse. St. Paul's HRA issued \$1.8 million in industrial development bonds for the project and provided a second mortgage for the building. The city intended to use TIF as a security enhancement (e.g., helping to pay letter of credit fees), but there has been no TIF expenditure to date. The renovated building now contains office and retail space.

Waldorf TID (economic development, 1985). This site currently contains a paper mill operated by the Waldorf Corporation. This local corporation purchased the plant in 1985 in light of speculation that an out-of-state corporation would acquire and close the facility. The city issued a \$4.8 million tax increment revenue note for the project, primarily to purchase two surplus buildings and the right to use steam heat generated at the site. In exchange for this assistance, Waldorf agreed to keep its corporate headquarters in St. Paul for 10 years and to maintain the facilities current production levels (approximately 1,000 employees).

SAVAGE

Project Area 1, TID 1 (economic development, 1981). When created, this district contained Savage's downtown area and a large residential area. Originally, the city proposed \$5.4 million in public improvements for the district. The planned activities included construction of several major sewers and streets. These public improvements have not been done. In 1985, the city removed large portions of the district that had not redeveloped (the county would have required this action in 1986). Today, the TID includes only the few parcels on which development has occurred (TIF funded the clearance of blighted parcels for a motel, a 10-unit housing development, and a future office building; the motel also received a write-down). City officials believe the TIF-funded developments have spurred some private redevelopment downtown. The city has accumulated a TIF reserve of \$250,000 that will fund improvements in the project area, probably downtown street or sewer improvements (the city funded a study of sanitary sewers with TIF).

Project Area 1, TID 2 (redevelopment, 1981). This district (about 400 acres) lies west of Savage's downtown and was primarily unserved by city utilities before creation of the district. Originally, the city planned \$30 million in public improvements for the area. To date, the city has funded \$3.75 million in road and utility improvements for a small portion of the district. Special assessments paid one-half of the cost, and TIF funded the rest. There are no immediate plans for further public improvements. It is likely that the county will remove many parcels from the district in 1986 due to lack of development. In 1986, a warehouse/manufacturing facility will locate in the district, and this is the first development on the land with new utilities. The district includes land recently designated as wetlands by the federal government, and this may hinder development. The TID also contains land included by the city in 1981 to capture anticipated development (a grain elevator was built).

Project Area 1, TID 3 (redevelopment, 1985). The district contains 17 non-contiguous lots that previously were in TID 1. The sites contain substandard houses, but the city has no immediate plans for site redevelopment.

Project Area 1, TID 4 (housing, 1985). The five parcels in this district were previously in TID 1. The city plans to acquire the parcels and provide site improvements for an elderly housing complex; no development has been secured for the site to date.

Project Area 2, TID 4 (economic development, 1983). Prior to TID creation, this site had multiple owners, large lots, soil problems, and no city utilities. The city issued a \$220,000 bond to finance a land write-down. The resulting development is 48 market-rate, single family homes.

Project Area 2, TID 5 (housing, 1983). The city converted farmland into five non-contiguous housing subdivisions. TIF and a grant

from the Minnesota Housing Finance Agency provide a three-year write-down of the mortgage interest rates on 120 homes. Interest rates will be written down to 8 1/2 percent in the first year, 9 1/2 percent in the second, 10 1/2 percent in the third, and 11 percent thereafter. Annual tax increments will support the project; there will be no tax increment bonds. Many parcels that received no TIF assistance are still in the district and have developed privately; the city plans to remove these parcels from the district. Savage will terminate this district when the write-down is completed.

SHAKOPEE

As of 1984, all of Shakopee's tax increment districts are in a single project area. This area encompasses about one-third of the city, including downtown Shakopee.

K-Mart Distribution Center TID (pre-1979, 1979). This 29-acre site houses K-Mart's regional distribution center, which serves nine states. Prior to creation of the TID, the site was primarily vacant industrial land with soil problems. The city issued a \$3.5 million bond to finance a land write-down, site development (grading, drainage improvements), widen County Road 83, and build a water well. Shakopee refinanced its bonds in 1984 and issued an additional \$2.4 million in bonds to make off-site roadway improvements near the racetrack site (a portion of which is in this TID) and the distribution center. The district is generating surplus tax increments, which Shakopee hopes to use for storm sewers and downtown improvements.

Senior High-rise TID (redevelopment, 1979). The city issued a \$365,000 tax increment bond to subsidize 66 units of Section 8 housing for seniors on land that previously had one home and two vacant parcels. The primary uses of TIF in the district were land write-down and provision of water service through a limestone bed.

Downtown TID (redevelopment, 1982). The district contains four properties, each containing a business that planned expansion prior to creation of the district. The four businesses (bank, grocery, realty firm, abstract company) all expanded without TIF assistance. No bonds have been issued. To date, tax increments have funded a planning consultant and construction of a parking lot next to the abstract company's building. Shakopee also planned to use TIF to fund interest write-downs on commercial rehabilitation loans downtown, but no write-downs have been done to date.

Racetrack TID (economic development, 1984). Shakopee issued \$4.2 million in tax increment bonds to assist development of the Canterbury Downs horse-racing track. The primary uses of TIF were land write-down and grading. Previously, this site was vacant industrial land. The city thinks tax increments may be higher than expected, in which case the excess will probably be used for storm sewers and downtown improvements.

Family Chow Mein TID (redevelopment, 1984). This one-parcel site was a gas station before being placed in a TID. developers converted the station into a Chinese restaurant without TIF assistance. Shakopee hoped to use tax increments for downtown improvements, but the restaurant is currently generating fewer taxes than the gas station did.

VIRGINIA

Finn Town TID (pre-1979, 1977). Virginia created the district to capture tax increments from a Section 8 housing project that was under construction (the Ellis-Nettle Tower). The project received no TIF assistance, and no bonds have been issued. The city uses the tax increments as they become available to redevelop the city's oldest housing area. The city has written down the acquisition of standard houses and houses on small parcels. Tax increments also paid for a sewer extension. The district generates about \$115,000 per year in tax increments.

Miner's TID (pre-1979, 1979). In the early 1970s, Virginia received a three-year commitment of federal funds for development of a large recreational complex. President Nixon impounded the funds after one-third of the complex had been completed. The city created the TID to provide a source of funds for completion of the project. Virginia included the following sites in the district: a new housing subdivision; a condominium under construction at the time of TID creation; a 7-acre site planned for industrial use. No development occurred at the industrial site. To make up for the lack of industrial development, the city amended the district in 1980, adding a parcel on which a private office building (leased to the state) was being constructed. The tax increments generated by the district may still be insufficient to cover debt service on the \$1.6 million tax increment bond.

Northland Office Center (redevelopment, 1981). The tax increment district includes most of Virginia's downtown streets, several parking lots, and the Northland Office Center. The office complex is the only recipient of TIF funds, receiving a \$436,000 write-down. Developers converted a city recreation building into office space, and the largest tenant in the building is now St. Louis County. A \$620,000 UDAG and a \$250,000 state Small Cities grant also contributed to the project.

LP Medical Park TID (redevelopment, 1984). An office building was constructed at a site that previously was a parking lot for a medical clinic. A health maintenance organization is the primary tenant. Virginia provided a \$600,000 write-down to finance the development.

Tini Mechanical TID, Environmental Energy/D.B. Western TID (redevelopment, 1984). Virginia created these two districts at the same time and for the same general purpose. Both districts are in a state enterprise zone, and tax increments from the developments finance the local contribution required for enterprise zone projects. Tini was an existing business in the tax increment district, and it

added a 3,000 foot addition to its building on vacant land without soil problems. Environmental Energy was an existing business within its tax increment district, and D.B. Western moved its business to the district from Oregon. \$15,000 in tax increments paid about 10 percent of the cost of a rail spur for Environmental Energy and D.B. Western.

Coates Hotel TID (redevelopment, 1985). A downtown hotel closed in 1975 and was standing vacant. TIF financed an \$800,000 write-down of the property, a \$377,000 industrial development bond reserve, sub-surface improvements, and utility installation. Three homes and a vacant lot were acquired for parking. The old building has been completely rehabilitated, and developers built an adjacent, three-story addition. Other funds in the project included an \$880,000 UDAG, \$2.6 million in industrial development bonds, and a \$250,000 Small Cities grant.

WILLMAR

Highland TID (pre-1979, 1979). The site contained six dilapidated residential properties, five of which had absentee landlords. The city acquired the property, and a developer built 79 Section 8 housing units in the district. A \$245,000 bond financed the city's costs for acquisition, demolition, and relocation.

Downtown TID (redevelopment, 1981). Willmar's entire downtown is in this district (approximately 25 city blocks). The city created the district to revitalize its aging downtown, which was losing business to Willmar's shopping mall on the edge of town (the mall was expanding in 1981). In addition, the downtown's 75-year-old district heating system required either replacement or removal, and either option required the city to tear up downtown streets and sidewalks. The city assessed property owners for the street, sidewalk, sewer, water, and beautification improvements done in conjunction with replacement of the heating system. TIF wrote down the \$4 per square foot assessments to as low as \$0.58 per square foot. The city built the new district heating system without TIF.

Lakeland TID (redevelopment, 1983). The two parcels in this district are also currently in the downtown TID. The city gains no financial advantage by the creation of this TID, but Willmar established the district to clarify that increments from the two parcels (not the whole downtown) will support the project costs. The two parcels contained a vacant theatre and a partially-vacant hotel. TIF financed a \$400,000 land write-down on the properties, and both redeveloped into retail/office space (they received \$1.5 million in industrial revenue bonds).

WINONA

Downtown TID (pre-1979, 1969). Winona established its district in conjunction with a federal urban renewal project. The city cleared

several properties in the early 1970s (without tax increment funds), but no development occurred until 1977. A \$660,000 tax increment bond issued in 1979 financed a land write-down (to \$1 per square foot) for a mini-mall, a bank, 118 apartments for seniors, a professional office building, and a movie theatre. In addition, TIF funded 130 new parking spaces and street and utility improvements.

Kensington TID (redevelopment, 1983). A downtown hotel closed in 1976. Thereafter, the building was vacant, hazardous, and tax-delinquent. The city used TIF to finance \$121,000 in sidewalk, street, parking, and beautification improvements at the site. In addition, \$122,000 in tax increments will pay Winona's parking meter system debt caused by the city's removal of parking meters downtown. A developer rehabilitated the building into 45 market-rate apartments (about half of which are now occupied) and ground-floor retail space. Excess increment from this district may be used to finance the 51 Walnut TID.

51 Walnut TID (redevelopment, 1984). The district includes a vacant, four-story warehouse near the Mississippi River. The warehouse is being converted into office space. All TIF expenditures will be in the project area adjacent to the district, not in the TID itself. The city used TIF to: (1) acquire a junkyard next to the warehouse and build a 62-car parking lot; (2) rebuild two adjacent streets. The Port Authority used its general fund to purchase two buildings for restoration near the warehouse; TIF will reimburse the Port Authority.

Freighthouse TID (redevelopment, 1983). A developer restored an old depot, converting half of the building into a restaurant. The remaining portion of the building is not presently occupied. The developer paid for sidewalk, curb and gutter and utilities when he rehabilitated the structure; TIF will reimburse the developer for his costs. The developer will receive up to \$45,000 in tax increments over five years, depending on the increments generated.

Choate TID (redevelopment, 1985). This vacant downtown building is on the National Register of Historic Places and housed a department store until three years ago. The city expects to use TIF to provide a land write-down and to construct public parking on part of what is now a downtown mall. Winona expects the resulting development to include two floors of retail space and two floors of residential space. No tax increment bonds have been issued.

Watlow TID (redevelopment, 1983). A Winona electronics firm wanted to expand its business. The firm said it would build an 80,000 square foot addition without TIF; it would build a 100,000 square foot addition with TIF. The city issued a \$1.05 million tax increment bond to finance three costs: (1) site costs (parking, landscaping, and fill to elevate the building), (2) water and sewer extensions, and (3) a downpayment on a 40-acre farm for conversion to industrial uses (this is in the project area, not the TID; Watlow is not located in this new industrial area). The district qualified as a redevelopment district on the basis of poor soils.

Winona Knitting Mills TID (redevelopment, 1983). This district is adjacent to the Watlow TID. Like Watlow, this land was vacant but qualified as a redevelopment district on the basis of soil problems (the problems are relatively minor in this district). The main use of TIF has been for correction of drainage problems. The city issued a \$215,000 bond for construction of a storm sewer and lift station that will benefit this site, the Watlow TID, and a 40-acre industrial site nearby. The source of tax increments for the district is a new distribution center for an existing Winona knitting mill.

Riverfront TID (redevelopment, 1980). The district contains about 400 acres of land (primarily industrial) along the Mississippi River. The port authority has purchased about 60 acres of land with TIF and CDBG funds. The land is sold at market value, without write-downs. The city has spent about \$160,000 in TIF funds for streets and utilities. Eight commercial/industrial firms have built facilities since creation of the district; one of them received direct TIF assistance (soil replacement). The city anticipates using TIF to assist a major Winona industry in 1986 with construction of a waste water pre-treatment facility and relocation of a rail yard.

WINSTED

Downtown TID (redevelopment, 1982). This district includes Winsted's entire downtown area. Winsted used TIF to redevelop a four-parcel area; no bonds were issued. Tax increments funded: (1) acquisition, write-down, and clearance of the four parcels, and (2) assumption of the mortgages on the businesses that were cleared. The resulting development is a building containing two retail stores and two professional offices. Currently, tax increments from this development cover about 40 percent of the city's annual costs for the district; Winsted's other downtown properties provide the rest of the increments needed. A large share of the city's captured assessed value came from a recent county re-valuation of all downtown properties. No additional TIF expenditures are currently planned.

Housing TID (housing, 1982). The city acquired a 40-acre parcel of farmland for housing development. Winsted used a \$500,000 community development block grant to finance streets, utilities, and park areas for Phase I of the housing development (23 single-family homes for low/moderate income families). There were no TIF expenditures for construction of Phase I, although the completed development will generate about \$10,000 per year in tax increments. Winsted intends to use these tax increments for infrastructure in future phases of the housing project, starting in 1987 at the earliest. However, seven of the Phase I lots have not yet been sold, so the city may delay additional phases. At this time, it appears likely that future phases will be market-rate.

ZUMBROTA

Downtown TID (redevelopment, 1979). The district includes a large portion of Zumbrota's downtown. The city's initial \$200,000 tax increment bond financed acquisition and write-down of properties in one downtown block (CDBG funded clearance and relocation costs). The resulting developments were a 45-unit elderly housing complex and a clothing store. The taxes generated by the housing complex have declined unexpectedly. A \$300,000 bond issue financed several other downtown projects. The city wrote down land for a 12-unit subsidized housing development, acquired land for a municipal parking lot, converted downtown street lights to sodium vapor, and facilitated a service station and a two-story retail/office building with the acquisition and relocation of five properties (two commercial, three residential). The tax increments generated by the developments are insufficient to pay for Zumbrota's annual TIF debt service. Between 1985 and 1989, Zumbrota will levy a total of \$130,000 to make up for the shortfall.

STUDIES OF THE PROGRAM EVALUATION DIVISION

Final reports and staff papers from the following studies can be obtained from the Program Evaluation Division, 122 Veterans Service Building, Saint Paul, Minnesota 55155, 612/296-4708.

1977

1. Regulation and Control of Human Service Facilities
2. Minnesota Housing Finance Agency
3. Federal Aids Coordination

1978

4. Unemployment Compensation
5. State Board of Investment: Investment Performance
6. Department of Revenue: Assessment/Sales Ratio Studies
7. Department of Personnel

1979

8. State-sponsored Chemical Dependency Programs
9. Minnesota's Agricultural Commodities Promotion Councils
10. Liquor Control
11. Department of Public Service
12. Department of Economic Security, Preliminary Report
13. Nursing Home Rates
14. Department of Personnel: Follow-up Study

1980

15. Board of Electricity
16. Twin Cities Metropolitan Transit Commission
17. Information Services Bureau
18. Department of Economic Security
19. Statewide Bicycle Registration Program
20. State Arts Board: Individual Artists Grants Program

1981

21. Department of Human Rights
22. Hospital Regulation
23. Department of Public Welfare's Regulation of Residential Facilities for the Mentally Ill
24. State Designer Selection Board
25. Corporate Income Tax Processing
26. Computer Support for Tax Processing
27. State-sponsored Chemical Dependency Programs: Follow-up Study
28. Construction Cost Overrun at the Minnesota Correctional Facility - Oak Park Heights
29. Individual Income Tax Processing and Auditing
30. State Office Space Management and Leasing

1982

- 31. Procurement Set-Asides
- 32. State Timber Sales
- 33. *Department of Education Information System
- 34. State Purchasing
- 35. Fire Safety in Residential Facilities for Disabled Persons
- 36. State Mineral Leasing

1983

- 37. Direct Property Tax Relief Programs
- 38. *Post-Secondary Vocational Education at Minnesota's Area Vocational-Technical Institutes
- 39. *Community Residential Programs for Mentally Retarded Persons
- 40. State Land Acquisition and Disposal
- 41. The State Land Exchange Program
- 42. Department of Human Rights: Follow-up Study

1984

- 43. *Minnesota Braille and Sight-Saving School and Minnesota School for the Deaf
- 44. The Administration of Minnesota's Medical Assistance Program
- 45. *Special Education
- 46. *Sheltered Employment Programs
- 47. State Human Service Block Grants

1985

- 48. Energy Assistance and Weatherization
- 49. Highway Maintenance
- 50. Metropolitan Council
- 51. Economic Development
- 52. Post Secondary Vocational Education: Follow-Up Study
- 53. County State Aid Highway System
- 54. Procurement Set-Asides: Follow-Up Study

1986

- 55. Insurance Regulation
- 56. Tax Increment Financing
 - Programs for Mentally Retarded People: The Impact of *Welsch* (in progress)
 - Programs for Mentally Ill People: The Linkage Between State Hospitals and the Community (in progress)
 - Public Employee Pensions (in progress)
 - Fish Management (in progress)

*These reports are also available through the U.S. Department of Education ERIC Clearinghouse.