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# Analysis of Recent Uses of Tax Increment Financing

## CHAPTER 3

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The Legislature made significant changes to the tax increment financing law in the late 1980s and in 1990. Legislative debate about further changes in 1995 once again elevated interest in the use of TIF, but statewide information on specific city uses of tax increment financing was not readily available. As a result, we visited cities and counties to evaluate their use of TIF.

We asked the following questions:

- **How have cities and other development authorities been using tax increment financing in recent years? What are the current trends in financing for TIF projects?**
- **To what extent have legislative restrictions limited the ability of cities and other development authorities to pursue development projects?**

To obtain detailed information on the use of tax increment financing in Minnesota, we selected a non-random sample of 43 cities and 3 counties currently using TIF. In our sample, we included cities with a large number of post-1990 TIF districts, cities with large amounts of total captured tax capacity and with a variety of tax increment districts, and a combination of large and small cities from various parts of the state.<sup>1</sup> Finally, we included active users of TIF before 1990 who have not certified any new districts since 1990.

For each of the cities and counties in our sample, we reviewed the TIF plans and 1994 annual disclosure, financial, and bonded indebtedness reports. After this review, we traveled to the cities and counties to discuss the districts with local officials, including city or county administrators, finance directors, and community or economic development directors.<sup>2</sup> As time permitted, we visited tax increment sites. Following the site visits, we verified district information by telephone and we asked city officials to review summaries of their districts for accuracy.

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**This evaluation looked at how a sample of cities are using TIF.**

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<sup>1</sup> We relied on data reported by county auditors to the Department of Revenue in the TIF Supplement to develop the sample. As discussed in Chapter 2, the TIF Supplement contained some errors in identifying the type of district which affected our sample selection. For example, we selected some cities thinking that they had post-1990 economic development districts. When we examined the TIF plans, however, we found that some of these districts were actually redevelopment districts.

<sup>2</sup> We conducted telephone interviews with city officials from East Grand Forks, International Falls, and North Branch.

The cities and counties visited for this study represent about 13 percent of the local jurisdictions using tax increment financing. The TIF districts in the sample captured \$122 million in tax capacity in 1995, representing 60 percent of the total captured tax capacity in Minnesota for 1995. Table 3.1 shows the captured tax capacity of cities and development authorities we visited; Table 3.2 shows the types of districts for each city and development authority visited. Appendix A lists the cities and counties we visited. A separate document, *Description of Selected Tax Increment Financing Districts*, contains a summary of over 400 tax increment districts in those cities and counties.

**Table 3.1: Captured Tax Capacity in Cities Visited, 1995**

	Number of Districts	Total City Tax Capacity	Total Captured Tax Capacity	Percent of City Tax Capacity That Is Captured
<b>METRO AREA</b>				
Bloomington	13	\$127,643,351	\$14,858,999	11.6%
Brooklyn Park	11	36,359,513	3,986,377	11.0
Burnsville	4	58,738,039	1,693,005	2.9
Chaska	8	12,268,049	4,160,480	33.9
Dakota County <sup>1</sup>	9	--	1,505,929	--
Eagan	3	59,299,204	593,573	1.0
Edina	6	84,055,819	5,162,771	6.1
Farmington	11	3,683,003	283,950	7.7
Fridley	10	27,545,541	2,642,692	9.6
Hopkins	13	15,510,773	1,021,176	6.6
Maple Grove	7	33,008,438	2,232,946	6.8
Minneapolis	52	317,158,321	40,424,769	12.8
Oakdale	13	11,662,563	1,001,348	8.6
Plymouth	16	71,428,665	4,673,782	6.5
Richfield	7	20,495,008	2,219,234	10.8
Roseville	15	42,803,926	4,793,226	11.2
St. Paul	9	158,302,112	10,388,009	6.6
Shakopee	6	14,785,689	1,730,528	11.7
Vadnais Heights	24	10,230,240	1,355,779	13.3
White Bear Lake	25	14,959,687	1,368,798	9.2
Woodbury	7	24,938,450	1,495,910	6.0
<b>METRO AREA TOTALS</b>	<b>269</b>	<b>\$1,144,876,391<sup>2</sup></b>	<b>\$106,087,352<sup>2</sup></b>	<b>9.3%<sup>2</sup></b>
<b>NON METRO AREAS</b>				
Albert Lea	11	\$7,399,062	\$441,595	6.0%
Alexandria	11	5,904,696	171,362	2.9
Becker	2	31,385,629	1,181,727	3.8
Branch	1	1,478,799	242,266	16.4
Buffalo	7	4,419,120	1,198,997	27.1
Cloquet	3	6,428,161	547,014	8.5
Crow Wing County <sup>3</sup>	2	855,196	498,804	58.3
Detroit Lakes	14	4,605,903	353,762	7.7
Dodge Center	9	871,800	192,172	22.0
Dundas	2	335,170	128,618	38.4
East Grand Forks	6	3,359,545	126,191	3.8
Elk River	9	9,895,736	571,376	5.8
Fairmont	16	4,601,327	209,462	4.6
Glencoe	10	2,141,810	330,385	15.4

**Table 3.1: Captured Tax Capacity in Cities Visited, 1995, continued**

	Number of Districts	Total City Tax Capacity	Total Captured Tax Capacity	Percent of City Tax Capacity That Is Captured
NON METRO AREAS, cont.				
Hibbing	6	5,833,873	158,654	2.7
International Falls	3	5,585,707	2,032,433	36.4
Little Falls	13	2,924,227	342,214	11.7
Mankato	21	19,306,756	1,530,820	7.9
Marshall	11	7,640,413	1,280,943	16.8
Morrison County <sup>4</sup>	3	--	21,894	--
Nisswa	8	2,540,285	96,515	3.8
Red Wing	8	32,214,609	919,222	2.9
Renville	7	321,307	12,345	3.8
St. Cloud	17	31,683,297	2,747,850	8.7
Winona	10	11,372,494	640,574	5.6
NON METRO TOTALS	210	\$203,104,922 <sup>5</sup>	\$15,955,301 <sup>5</sup>	7.9% <sup>5</sup>
STATEWIDE TOTALS	479	\$1,347,981,313	\$122,042,653	9.1%

Source: Office of the Legislative Auditor determined the number of districts. The tax capacity data are from the Minnesota Department of Revenue Abstract of Tax Lists.

<sup>1</sup>The Dakota County Housing and Redevelopment Authority (HRA) has tax increment districts in ten communities.

<sup>2</sup>Metropolitan area totals exclude Dakota County HRA tax increment activity.

<sup>3</sup>Both of Crow Wing County HRA's tax increment districts are in Irondale Township. Tax capacity data includes Irondale Township only.

<sup>4</sup>The Morrison County Rural Development Finance Authority (RDFA) has tax increment districts in two townships and one city.

<sup>5</sup>Non-metropolitan area totals exclude Morrison County RDFA tax increment activity.

## ANALYSIS OF SAMPLE CITIES AND COUNTIES

In this section we examine how cities and development authorities have been using tax increment financing in recent years. In particular, the section looks at the types of activities and projects in districts certified after April 30, 1990, compares the nature of tax increment spending between pre-1990 and post-1990 districts, examines trends in pooling and financing, and reviews the financial status of districts.

### Supported Activities and Projects

Cities and development authorities have created 346 tax increment districts since enactment of the 1990 legislative amendments. To determine how cities and counties are using TIF, we reviewed the 172 post-1990 districts in the cities and counties we visited. In this section, we discuss the types of development activities

**Table 3.2: Types of Tax Increment Districts in Cities Visited**

City	Pre-1979	Pre-1990 TIF Activity				Post-1990 TIF Activity				Total
		Redevelopment	Economic Development	Housing	Sets Condition	Redevelopment	Economic Development	Housing	Sets Condition	
Bloomington	1	6	2	3	0	0	0	0	0	13
Buena Vista Park	0	1	4	0	0	0	0	0	0	11
Burnsville	0	2	1	0	0	0	0	1	1	4
Chaska	0	1	3	1	0	0	0	0	0	4
Dakota County	0	1	0	4	0	0	0	0	0	4
Eden Prairie	0	0	1	1	0	0	0	0	0	2
Edina	2	3	2	0	0	0	0	0	0	5
Farmington	1	0	1	0	0	0	0	0	0	2
Fridley	1	5	1	0	0	0	0	1	1	11
Hopkins	0	4	0	0	0	0	0	0	0	4
Maple Grove	0	1	2	1	0	0	1	0	0	5
Minneapolis	24*	15	1	5	0	0	0	0	0	45
Oakdale	0	0	4	0	0	0	0	0	0	4
Plymouth	0	0	13	0	0	0	0	0	0	13
Richtonfield	1	1	1	0	0	0	0	0	0	3
Rosendale	0	10*	1	1	0	0	0	0	0	12
SL Paul	1	0*	0	0	0	0	0	0	0	1
Shakopee	2	2	2	0	0	0	0	0	0	6
Vadnais Heights	0	8	8	0	0	0	0	0	0	16
White Bear Lake	0	5	5	3	0	0	0	0	0	13
Woodbury	0	1	5	1	0	0	0	0	0	7
<b>METRO TOTALS</b>	<b>39</b>	<b>76</b>	<b>57</b>	<b>20</b>	<b>2</b>	<b>27</b>	<b>10</b>	<b>13</b>	<b>269</b>	

**Table 3.2: Types of Tax Increment Districts in Cities Visited, continued**

City	Pre-1979					Post-1980 TIF Activity					Total
	Pre-1979	Redevelopment	Economic Development	Housing	Sales Condition	Redevelopment	Economic Development	Housing	Sales Condition		
Albert Lea	0	2	4	1	0	0	4	0	0	0	11
Alexandria	0	2	3	0	0	0	1	1	0	0	11
Becker	0	1	0	0	0	0	1	0	0	0	2
Branch	0	0	0	0	0	0	0	0	1	1	1
Burlington	1	0	4	0	0	0	1	0	1	0	7
Cloquet	0	0	1	0	0	0	2	0	0	0	3
Crow Wing County	0	0	1	0	0	0	0	1	0	0	2
Detroit Lakes	0	5	3	0	0	2	4	0	0	0	14
Dodge Center	0	2	0	1	0	1	3	2	0	0	9
Dundas	0	0	0	0	0	0	0	0	0	0	0
East Grand Forks	0	2	1	0	0	3	0	0	0	0	3
Elk River	0	2	2	1	0	1	2	1	0	0	6
Farmington	0	2	1	0	0	0	2	0	0	0	3
Glenwood	1	2	1	2	0	0	1	0	0	0	16
Hibbing	0	2	0	0	0	2	1	1	0	0	10
International Falls	0	1	0	0	0	0	0	1	0	0	1
Little Falls	0	1	5	0	0	1	4	0	0	0	10
Marquette	2	4	8	2 <sup>a</sup>	0	2	4	1	0	0	19
Marshall	0	7	1	2	0	3	0	0	0	0	21
Marathon County	0	0	0	0	0	1	0	0	1	0	11
Mississippi	0	0	1	0	0	0	2	0	0	0	3
Red Wing	2	0	0	0	0	3	3	1	0	0	6
Remus	0	0	0	0	0	3	4	0	0	0	7
St. Cloud	1	5	2	1	0	1	7	0	0	0	17
Winona	1	4	1	0	0	0	0	0	0	0	10
WINNEMETON	0	57	38	10	0	38	47	9	3	0	210
<b>TOTALS</b>	<b>47</b>	<b>133</b>	<b>95</b>	<b>30</b>	<b>2</b>	<b>63</b>	<b>74</b>	<b>19</b>	<b>16</b>	<b>0</b>	<b>479</b>

Source: Office of the Legislative Auditor.

<sup>a</sup>Two pre-1979 districts have hazardous substance subdistricts that were certified in 1984.

<sup>b</sup>One district has a hazardous substance subdistrict.

<sup>c</sup>One district qualifies as both a redevelopment and housing district and one district has a hazardous substance subdistrict.

<sup>d</sup>One of these districts is a renovation and renewal district.

<sup>e</sup>One of these districts is certified as both a housing and a redevelopment district.

supported by TIF -- manufacturing, retail, office, and housing.<sup>3</sup> We were not able to categorize every district, and some districts served more than one purpose. Of those districts we could categorize, we found that:

- **About two-fifths of the post-1990 districts were created to assist new or existing manufacturing businesses, while office developments, retail facilities, and housing projects each accounted for one-fifth of the districts.**

## Manufacturing

About two-fifths of the post-1990 TIF districts created by cities and counties in our sample assisted manufacturing companies with land acquisition, site preparation, or other public improvements. Most of these districts were economic development districts (76 percent), but some cities used soils condition and redevelopment districts, if the district qualified, to assist manufacturing companies.

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### Most TIF-assisted manufacturing companies were local businesses that wanted to expand.

We estimate that the majority (about three-fourths) of the manufacturing companies receiving TIF assistance were local businesses that wanted to expand. City officials told us that these businesses had outgrown their existing location and were considering options for expanding, including relocating to other Minnesota cities or to other states. Some city officials told us about companies in their cities that received offers of financial assistance to move to Wisconsin, Iowa, and other states. We have not attempted to verify those claims. However, a recent article claimed that at least 31 industrial parks have been constructed in three Wisconsin border counties (Polk, St. Croix, and Pierce) in the last 30 years. The manufacturing tax bases of those counties' have increased by 28 to 43 percent between 1994 and 1995.<sup>4</sup> City officials felt that unless their cities provided assistance, companies would leave and the cities would lose both jobs and tax base. Cities created the following TIF districts to assist existing manufacturing companies:

- *Bloomington (Seagate)*: The city created this economic development district to facilitate the expansion of Seagate Technologies, an international manufacturer of disk drives, in the city. Tax increments will assist with public improvements (including storm and sanitary sewers and a water main), parking lot improvements, landscaping, and soil corrections. The expansion will create 150 administrative jobs and 350 production jobs.
- *Elk River (Tescom)*: A local manufacturer of regulators, valves, and control devices was looking at expansion options. Elk River created an economic development district in 1993, provided a land write-down on a

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<sup>3</sup> Manufacturing includes printing companies, computer software, agricultural/value added processing, and food production. Offices include banks, medical buildings, and other professional office buildings, along with wholesale distribution and mail order processors and distributors. Retail includes hotels and motels, and service and repair centers.

<sup>4</sup> Cassano, Dennis, "Officials in Wisconsin, Minnesota See Need to Coordinate Development" *Star Tribune*, November 12, 1995, p. D1. One city official showed us a letter to a local company from a St. Croix County developer, highlighting Wisconsin's lower tax rates and workers compensation costs and inviting the company to relocate there.

vacant site adjacent to the company's existing facility in the industrial park, and assisted with site preparation and soil testing.

- *Glencoe (Seneca)*: Seneca Corporation, owner and operator of an old Green Giant facility in Glencoe with 165 full-time jobs and nearly 2,000 seasonal jobs, threatened to build a new cold storage facility in another city. Glencoe created an economic development district in 1994 to assist with site preparation, utility extensions, and construction of footings, foundations, and a parking lot.
- *Nisswa (D & H Docks)*: A local manufacturer of boat docks constructed a new manufacturing facility in this 1993 economic development district. The city used TIF to reimburse the developer for land acquisition and site improvements.
- *St. Cloud (Woodcraft)*: A wooden cabinet door company was considering moving to Kentucky. The city created an economic development district in 1991 to assist the company with land acquisition for expansion of its manufacturing facility. The city amended the tax increment financing plan in 1994 to provide TIF assistance for site preparation (including tree removal, excavation, landscaping, and paving) for another expansion.

While city officials are primarily concerned with retaining existing businesses, about one-fourth of manufacturing companies receiving TIF assistance were new companies or were new to the city. City officials told us that many companies shop around to try to get the best deal. As a result, cities use TIF to compete with one another for new businesses. Cities with industrial parks sometimes offer free land and public improvements, such as utilities and street extensions. Cities created the following TIF districts to help companies establish new manufacturing facilities:

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**Cities also use TIF to compete with one another for businesses.**

- *Little Falls (Monarch Plastics)*: This 1995 economic development district in the city's industrial park assisted a new company with construction of a facility for reprocessing plastic waste into usable products. The city assisted with land acquisition, site improvements, and parking.
- *Becker (Liberty Paper)*: The company wanted to construct a cardboard recycling facility near a power plant in order to use steam in its production process. It had explored sites in Wisconsin and Mankato. Becker created an economic development district in 1993 to acquire property, purchase recycling equipment, extend utilities, improve streets, install sidewalks, construct a railroad spur and crossings, and construct a new city water tower to provide water pressure for fire fighting requirements. Mankato also established a TIF district for this facility, but its plans fell through when the company decided to accept Becker's offer.
- *Renville (Egg Production Facility)*: A joint venture of three regionally owned farmer cooperatives asked the city for assistance with construction

of 16 laying barns, one processing building to wash, pack, and prepare egg products for shipment, and a conveyor. Renville created two economic development districts (in 1994 and 1995) to provide a land write-down, extend utilities to the site, and provide site improvements, including grading, foundation work, and parking.

The following examples illustrate how cities have used TIF to attract companies from other Minnesota cities:

- *Buffalo (Whirltronics)*: A manufacturer of lawn mower blades previously located in Brooklyn Park was looking at a number of Minnesota communities for an expansion site. Buffalo created an economic development district in 1991 in its industrial park and constructed a manufacturing facility that it leases to Whirltronics.
- *Detroit Lakes (D. L. Printing)*: D.L. Printing, a subsidiary of the Fargo Forum, wanted to expand from its existing site in Hawley. Detroit Lakes created an economic development district in 1992 to assist with site acquisition and improvements for a new printing plant for the regional newspaper. City officials think that the company would have located in Fargo without TIF assistance.
- *Farmington (Minnesota Pipe)*: This 1994 economic development district helped a Lakeville pipe distributor relocate to Farmington's industrial park. The city sold the company a lot in the industrial park for \$1 and assisted with site preparation.
- *Red Wing (Advertising Unlimited)*: A manufacturer of executive gifts was previously located in Maplewood. Red Wing's Port Authority created an economic development district in 1992, provided a land write-down, assisted with site improvements, and abated street assessments and utility connection fees for construction of a new manufacturing facility. The company recently acquired a Connecticut company and plans to consolidate operations in Red Wing in 1996.

In the following example, a city used TIF to attract a Canadian company:

- *Red Wing (Industrial Hardwood Products)*: A Canadian manufacturer of wood flooring for truck trailers was considering locations in Minnesota, Wisconsin and Iowa. The Port Authority established a redevelopment district in 1992 on the site of a vacant industrial building, acquired the site, made substantial improvements to the building, and rented part of the building to Industrial Hardwood Products.

### **Office Buildings**

About one-fifth of the TIF districts created since April 1990 assisted office developments, ranging from large office and warehouse facilities to small professional office buildings. These projects were located primarily in economic development

and redevelopment districts, but several were in soils condition districts.<sup>5</sup> The following TIF districts were created to assist office buildings:

- *Brooklyn Park (CSM)*: The city established this economic development district in 1993 to help develop the Boone Avenue Business Center, a 168,000 square foot multi-tenant office, showroom, and warehouse facility. Tax increment financing assisted the developer with land acquisition costs.
- *Fairmont (S.R.S. Partnership)*: The city created a redevelopment district in 1994 to demolish an old school house and some abandoned homes. A developer constructed a professional office building on the site.
- *Oakdale (Oakdale Crossing Business Park)*: This 1993 economic development district consists of 82 acres of vacant land near I-694 and I-494. A developer will construct an office/warehouse park in four phases. Tax increments will reimburse the developer for land acquisition and installation of streets and utilities. The park's first tenant, Spartan Promotional Group, Inc., constructed a 25,000 square foot office/warehouse complex.
- *Plymouth (P.O.S.)*: The city created this soils condition district in 1994 to assist a computer software peripherals and training company with construction of an office building. TIF will assist with soil correction costs including removal of topsoil and installation of a storm sewer and drain tiling system.
- *Red Wing (Durkee Atwood)*: Previously, the district contained an old factory in substandard condition. The property owner gave the site to the Port Authority. The city created a redevelopment district in 1992 and used TIF to remove asbestos and demolish the building. A developer bought the site for \$25,000 and constructed an office building.

## Housing

About one-fifth of the TIF districts created since April 1990 have been for housing. About half of these districts were housing districts providing low- and moderate-income housing and the remainder were redevelopment and soils condition districts for market-rate housing. TIF assistance for projects in housing districts often includes financial assistance for land acquisition and site improvements. Several jurisdictions in our sample used TIF to provide interest rate reduction loan programs to make housing units affordable. In some housing districts, development authorities used TIF in combination with other forms of financing such as Minnesota Housing Finance Agency resources, including housing tax credits. However, city officials also told us that federal housing finance assistance had declined considerably. In their opinion, housing developments usually do not pro-

<sup>5</sup> The Legislature restricted the use of economic development districts in 1990. At least 85 percent of the buildings and facilities (based on square footage) must be used for manufacturing, warehousing, and other related activities. We found that TIF supported many office/warehouse developments in post-1990 economic development districts, but we did not determine if warehouse space was at least 85 percent of the total project.

vide sufficient financial incentives to attract many developers, so TIF is necessary to make projects economically feasible. We also found some low-density housing districts that required the use of pooled tax increments from other districts to meet financial obligations.

The following are examples of TIF-assisted housing projects in post-1990 districts:

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**TIF supported both affordable and market-rate housing projects.**

- *Dakota County HRA (Apple Valley Family Housing)*: The HRA created this housing district in 1991 to provide assistance to two projects. Tax increments provide an interest rate reduction loan to a 39-unit multi-family rental housing project. A 50-unit senior rental housing facility, which the HRA constructed, owns, and operates, received TIF assistance for land acquisition, public improvements, and soil tests and surveys.
- *Roseville (College Properties)*: This 1993 redevelopment district contained a run-down hotel and bar. The city used TIF to provide a land write-down for a multi-use housing project, including a 57-unit motel, 90 assisted-living units, and 140 independent-living units for seniors. A future project includes a 36-bed residential facility for Alzheimer's patients.
- *Richfield (Richfield Rediscovered Housing Program)*: This program includes four redevelopment districts created in 1991 and 1993 in which the city purchases substandard single-family homes at their appraised value, demolishes them, and sells the parcels to developers for construction of market-rate homes. The city has identified 70 houses to participate in the program. City officials hope that the replacement of blighted homes will encourage new families to move into the city and existing homeowners to maintain their properties.
- *Farmington (Soils Condition District)*: A developer approached the city for assistance to construct up to 426 single-family homes and 132 multi-family townhome units. The city created this 173-acre district in 1994 to finance soil correction of lowlands. Plans include adding three feet of soil to raise the ground level, upgrading city water and sewer lines, and constructing a waterway to control flooding and provide drainage.

### **Retail**

For the most part, 1990 statutory restrictions have limited economic development districts to assisting manufacturing and related activities, as defined in the TIF Act. However, cities have continued to use redevelopment districts and soils condition districts to assist retail developments. Retail developments accounted for about one-fifth of the post-1990 TIF projects in our sample.

City officials told us that they often use TIF to redevelop blighted buildings in their commercial districts. Many small city officials told us that TIF is crucial to maintaining the vitality of their downtowns, and that, without it, businesses would build on vacant lots or other locations where it is less costly to build. In the fol-

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**Most recent  
retail projects  
were in areas  
needing  
redevelopment.**

lowing examples, cities created retail-related redevelopment districts to renovate existing buildings or replace vacant or blighted buildings with new ones:

- *Alexandria (Woodsmen Distributing)*: The city created this redevelopment district in 1995 to demolish a substandard house, five cabins, and two garages (some of the structures were fire-damaged), allowing for construction of a retail store and service center for a local distributor of all terrain vehicles. The city will provide TIF assistance for land acquisition, demolition, site preparation, and public improvements.
- *Chaska (FMG)*: This 1991 redevelopment district contained a fire-damaged cosmetic and soap outlet store. The city used TIF to acquire the property, demolish the building, and prepare the site for construction of a retail music store.
- *Farmington (City Center)*: The city created this redevelopment district in 1991 to develop abandoned railroad property and clean up an old city dump. The city used TIF to acquire the railroad property, prepare sites, improve streets, purchase and demolish an existing manufacturing facility, and construct a parking lot for the Farmington City Center, a complex of shops including a grocery store, medical office, and other retail shops.
- *Minneapolis (Ninth Street and Hennepin Avenue)*: This 1995 redevelopment district consists of three parcels. The Minneapolis Community Development Agency acquired the old Hirschfields building, made interior and exterior improvements, and leased it to Hey City Stage, a theater production company. The city plans to acquire two additional buildings and renovate them for development of a restaurant.
- *St. Cloud (Lincoln/Target)*: This 1993 redevelopment district previously contained a printing company that moved to the industrial park, an abandoned city maintenance garage, and abandoned railroad property. The city used TIF to pay for site acquisition, demolition, and clean up of contaminated soils. It leased the site to Target, which helped pay for soil clean-up and constructed a retail store.

Some cities have used soils condition districts to provide TIF assistance to large retail developments, as the following examples show:

- *Branch (Tanger Factory Outlet Center)*: This 1992 soils condition district consists of 20 acres of vacant land. The city created the district to assist with development of a 140,000 square foot retail outlet center. The city used TIF to finance water system, drainage and street improvements, and soil correction costs.
- *Brooklyn Park (Wal-Mart)*: The city created this district in 1992 to assist with construction of a 116,000 square foot Wal-Mart store. Topsoil was removed to provide a stable foundation for construction.

**Some cities  
relied on soil  
conditions to  
justify  
TIF-assisted  
retail projects.**

- *Buffalo (Target)*: An undeveloped 16-acre site had unstable soils. The city created this district in 1992 to reimburse a developer for soil correction costs. An 86,500 square foot retail facility has been constructed on the site.

### Soils Condition Districts

Cities have used soils condition districts to assist all types of development activities including manufacturing, offices, retail, and housing projects. White Bear Lake accounted for 6 of the 17 post-1990 soils condition districts in our sample cities. According to city officials, White Bear Lake has soft and unstable soils in many parts of the city. As a result, White Bear Lake has removed or replaced topsoil to provide a secure foundation for construction. Other cities have cited similar conditions to justify creation of soils condition districts. In 1995, the Legislature restricted the use of soils condition districts to contamination and pollution clean-up, so conditions such as unusual terrain and unstable soils will no longer qualify for creation of soils condition districts. However, if bedrock conditions are present and other conditions are met, tax increments from economic development districts can be used to pay for site preparation and public improvements.<sup>6</sup>

## Project Area and District Configurations

Before enactment of the TIF Act of 1979, most cities' tax increment districts were coterminous with their project areas. As a result, many pre-1979 tax increment districts were very large and captured sizable amounts of tax capacity.<sup>7</sup> The TIF Act permitted cities to establish tax increment districts that were smaller than the project areas of which they were a part.

Our sample included a number of pre-1979 districts that contain most or all of a city's central business district.<sup>8</sup> These include: St. Paul with 1,062 parcels; Buffalo with 492 parcels; Hopkins with 299 parcels in its 6 North Sector districts; Red Wing with 168 parcels in 2 downtown districts; Mankato, 102 parcels; Farmington, 71 parcels; Glencoe, 61 parcels; and St. Cloud, 46 parcels.

Other large pre-1979 districts include Edina's Southeast district (2,013 parcels which consists primarily of condominium and townhouse developments), Richfield's Lyndale/Hub/Nicollet district (806 parcels), and Minneapolis' pre-1979 districts (which range up to 1,424 parcels).

The TIF Act of 1979 included provisions designed to contain the size of TIF districts, such as blight criteria, the "knock-down provision," and the opportunity to

<sup>6</sup> *Minn. Laws* (1995) Ch. 264, Art. 5, Sections 13 and 24.

<sup>7</sup> Data presented in Chapter 2 confirm that existing pre-1979 districts contain more parcels and capture a greater share of tax capacity than TIF districts certified after August 1, 1979.

<sup>8</sup> The number of parcels listed is the current number of parcels in the district as reported by county auditors to the Department of Revenue for taxes payable in 1995. The number of parcels is an imperfect indicator of district size because there is no uniform parcel size. A parcel may be one city lot, a city block, or large tracts of undeveloped land. It may also be individual units in a townhome or condominium development.

create project areas and tax increment districts of different sizes (described in Chapter 1). Our analysis of districts certified after 1979 found that some cities have created small districts, containing only the area directly benefited by the project. However, we also found that some cities continued to create large tax increment districts during the 1980s. Table 3.3 lists the largest districts created between 1979 and April 30, 1990 in the cities we visited.

**Table 3.3: Large Tax Increment Districts Established Between 1979 and 1990 in Sample Cities and Counties**

<u>City</u>	<u>District</u>	<u>Parcels</u>
St. Paul	New Housing/Blighted Lands TID	722
	Neighborhood Business Development TID	598
	Energy Park TID	246
	River Front TID	201
Dakota County	Multiple Cities TID 2	684
	North Robert Street and Smith Avenue TID	135
St. Cloud	SCSU TID	670
Maple Grove	Eagle Ridge Apartments HRA TID	448
Burnsville	Billy Goat Sienna TID	305
	Development District Number One	290
Chaska	Flood Control TID	213
Brooklyn Park	85th Avenue Improvements TID	122
Winona	River Front TID	117
Roseville	Villa Park TID	116

Source: Minnesota Department of Revenue, Property Tax Division, TIF Supplement.

In Chapter 2, we noted that the parcel size of tax increment districts has declined from an average of 146 parcels for pre-1979 districts to 8 parcels for post-1990 districts. Still, some cities created post-1990 districts containing a large number of parcels: Inver Grove Heights (economic development district with 367 parcels); Ramsey (economic development district with 260 parcels); Mahtomedi (redevelopment district with 118 parcels); Mille Lacs County (redevelopment district with 107 parcels); Itasca County (redevelopment district with 103 parcels); and Albany (redevelopment district with 103 parcels).

We also examined the size of cities' project areas. While the tax increment district contains the properties from which revenues will be collected, the project area consists of those properties on which tax increments can be spent. The TIF Act places some limitations on expanding the size of a TIF district, but there are no restrictions on increasing the size of project areas. In our sample, we found that:

- **Some cities have very large project areas that encompass entire cities or large portions of them.**

For example, 9 of 46 jurisdictions in our sample had project areas that are the same as the city or county boundaries. These jurisdictions are Crow Wing County and the cities of Becker, Burnsville, Elk River, Hibbing, Little Falls, Nisswa, and Roseville. Some cities have recently expanded their project areas. For example, Burnsville amended its project area in February 1995, making it the same as the city limits. Similarly, Crow Wing County expanded its project area to be coterminous with the county boundaries in 1995.

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**Many cities have created large project areas to pool tax increments.**

Other cities have very large project areas that include most, if not all, land within the city limits. For example, Albert Lea's project area contains nearly two-thirds of the city. Shakopee's project area includes most of the developed area within the city. Most of the developed portion of International Falls is also in a project area. In addition, several cities use one project area that contains all tax increment districts. When a city certifies a new district, the project area is expanded to include that district and the TIF plans for all prior districts are amended to reflect the new expanded project area. The following cities structured their districts and project areas in this manner: Brooklyn Park, Marshall, Fairmont, Plymouth, Vadnais Heights, and White Bear Lake.

Many cities and development authorities have created large project areas to pool tax increments between two or more districts or to spend tax increments outside the boundaries of the district. We found that:

- **Of the cities and counties in our sample with more than one tax increment district, two-thirds have pooled tax increment revenues between districts or have project area configurations that will permit pooling.**

For example, Vadnais Heights has pooled the tax increments from several districts to finance construction of a water tower and bridge over an interstate highway and related road improvements. Glencoe uses pooled tax increments from one of its successful districts to support an industrial park development that has not been self-supporting. While Burnsville does not pool increments among its pre-1990 districts, in 1995 it combined three project areas into one that was coterminous with the city boundaries. The city also authorized \$25 million in increased tax increment spending for future commercial and industrial projects located throughout the city. Roseville pools all of its pre-1990 tax increment districts, and has used tax increments to finance an outdoor ice oval, an indoor ice arena, and other public projects.

We did not see evidence of pooling with post-1990 districts, primarily because over half of the existing post-1990 districts were certified in 1992 and 1993, following a slowdown in activity after the 1990 legislative restrictions became effective. Many post-1990 districts are just starting to generate tax increment revenues needed to finance projects in the original TIF plan. In addition, legislative restrictions on pooling and spending of tax increments from post-1990 districts were

**It is too early to evaluate 1990 legislative restrictions on TIF spending.**

intended to limit pooling from these districts.<sup>9</sup> However, it is still too early to determine the full impact of these restrictions on post-1990 districts.

## Expenditure Trends

We gathered information on tax increment expenditures from TIF plans filed with the Minnesota Department of Revenue. These plans are supposed to contain a list of development activities along with estimates of project costs. We also reviewed 1994 annual financial reports that contain amounts budgeted and actually spent on: acquisition of land and buildings, site improvements and preparation costs, installation of public utilities and other public improvements, and administrative costs.<sup>10</sup> Because these categories are broad, a more detailed analysis is not possible. A separate document, *Description of Selected Tax Increment Financing Districts*, provides a description of tax increment projects, including expenditures when available, for the TIF districts in the cities and counties we visited.

### General Trends

Based on analysis of information from the cities and counties in our sample, we found:

- **The majority of both pre- and post-1990 districts use tax increments to provide land write-downs to developers.**
- **Public improvements financed with tax increments from post-1990 districts focused more on individual projects than pre-1990 districts.**

We compared tax increment expenditures for "pre-1990" districts (or districts for which certification was requested on or before April 30, 1990, including pre-1979 districts) and post-1990 districts (or districts certified after April 30, 1990). Cities used tax increments to provide land write-downs in over half of the pre-1990 districts. In addition, cities and development authorities used tax increments to finance a wide variety of public and site improvements. Figures 3.1 and 3.2 summarize the types of improvements financed with TIF from both pre-1990 and post-1990 districts in the cities we visited.

Figure 3.1 shows that many cities used tax increments from pre-1990 districts to extend city services to newly developing parts of cities, extend public utilities to development sites, improve existing local streets and roads, construct parking lots or ramps, make general downtown improvements, improve drainage and ponding, and correct poor soil conditions. The use of tax increments to finance major

<sup>9</sup> For TIF districts certified after April 30, 1990 and before June 30, 1995, no more than 25 percent of the tax increments may be pooled. For districts certified after June 30, 1995, no more than 20 percent of the tax increments generated may be pooled. However, redevelopment districts remain at 25 percent. In addition, tax increments from districts certified after April 30, 1990 must be spent on activities for which bonds have been issued or binding legal commitments have been made within five years after the district's approval. Tax increments received after the five-year period must be used to pay these obligations and decertify the district.

<sup>10</sup> Issues related to TIF reporting are discussed later in this chapter.

### Figure 3.1: Public and Site Improvements Financed with Tax Increments from Pre-1990 Districts in Sample Cities

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

Albert Lea	Burnsville	Chaska	Farmington
Hibbing	Little Falls	Mankato	Maple Grove
Marshall	St. Cloud	Shakopee	Winona
Woodbury			

#### Improvement of existing local streets and roads (including curb and gutter):

Albert Lea	Bloomington	Brooklyn Park	Buffalo
Chaska	Cloquet	Eagan	Edina
Elk River	Fairmont	Fridley	Glencoe
Hopkins	International Falls	Little Falls	Maple Grove
Marshall	Plymouth	Richfield	Roseville
St. Cloud	St. Paul	Shakopee	Vadnais Heights
White Bear Lake			

#### Construction of major new highway improvements (including freeway interchanges, bridges, ring roads):

Bloomington	Brooklyn Park	Edina	Plymouth
Roseville	Shakopee	Vadnais Heights	Winona
Woodbury			

#### General downtown improvements (such as sidewalks, lighting, street furniture):

Buffalo	Chaska	Dodge Center	Farmington
Glencoe	Hibbing	Hopkins	Red Wing
Shakopee	Vadnais Heights	White Bear Lake	Winona

#### Extension of utilities to site (storm or sanitary sewer, water):

Albert Lea	Becker	Bloomington	Buffalo
Burnsville	Cloquet	Crow Wing County	Detroit Lakes
Dundas	Eagan	Elk River	Fridley
Glencoe	Hibbing	Little Falls	Mankato
Maple Grove	Marshall	Nisswa	Oakdale
Richfield	Roseville	St. Cloud	St. Paul
Shakopee	Vadnais Heights	Winona	Woodbury

#### Skyways:

Minneapolis	St. Cloud	St. Paul
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#### Public parks/recreation:

Buffalo	Burnsville	Chaska	Edina
Elk River	Mankato	Maple Grove	Marshall
Nisswa	Roseville	St. Cloud	St. Paul
Vadnais Heights	Winona		

#### Government-owned or leased buildings:

Dodge Center (airport)  
 Hibbing  
 Roseville (post office)  
 St. Paul (civic center, Minnesota Department of Revenue Building)

#### Construction of lift station, water wells, water towers:

Buffalo	Chaska	Crow Wing County	Dodge Center
Elk River	International Falls	Little Falls	Shakopee
Vadnais Heights	Winona		

#### Wastewater treatment plants, pre-treatment plants:

Albert Lea	Detroit Lakes	Dodge Center	Marshall
Shakopee (planned)			

**Figure 3.1: Public and Site Improvements Financed with Tax Increments from Pre-1990 Districts in Sample Cities, continued**

**Drainage and ponding:**

Albert Lea	Bloomington	Buffalo	Chaska
Edina	Fairmont	Fridley	Little Falls
Mankato	Maple Grove	Marshall	Oakdale
Roseville	St. Cloud	St. Paul	Shakopee
Vadnais Heights	White Bear Lake	Woodbury	

**Soil corrections (including grading and excavation):**

Albert Lea	Brooklyn Park	Burnsville	Cloquet
Detroit Lakes	Dundas	Fairmont	Fridley
Glencoe	Hopkins	Mankato	Maple Grove
Marshall	Red Wing	Richfield	Roseville
St. Cloud	St. Paul	Shakopee	Vadnais Heights
White Bear Lake	Winona		

**Burying utilities/power lines:**

Little Falls	Shakopee
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**Parking ramps and lots:**

Albert Lea	Bloomington	Buffalo	Burnsville
Detroit Lakes	Dodge Center	Edina	Elk River
Farmington	Fridley	Hibbing	Hopkins
Little Falls	Mankato	Nisswa	Red Wing
Richfield	Roseville	St. Cloud	St. Paul
White Bear Lake	Winona		

**Landscaping:**

Buffalo	Burnsville	Elk River	Mankato
Maple Grove	Nisswa	St. Cloud	St. Paul

**Foundations and footings:**

Cloquet	Little Falls	Nisswa
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Source: Office of the Legislative Auditor.

public improvement projects is discussed later in this section. In addition to the public and site improvement expenditures shown in Figure 3.1, at least seven cities in our sample used tax increments to capitalize economic development funds or business loan programs,<sup>11</sup> six cities and one county used tax increments to provide interest rate reduction programs for housing projects,<sup>12</sup> and two cities used tax increments to fund reserve accounts for various purposes.<sup>13</sup>

Among cities in our sample with post-1990 districts, the use of TIF to provide land write-downs continued to predominate; cities provided land write-downs in 62 percent of these districts. However, Figure 3.2 shows that public and site improvements funded with tax increments from post-1990 districts have focused on specific projects, at least so far. Most cities used increments to finance soil correc-

<sup>11</sup> Buffalo, Fridley, Hopkins, Marshall, Red Wing, White Bear Lake, and Woodbury. Crow Wing County adopted a 1994 amendment authorizing development of a business loan program, but the program is not yet operational.

<sup>12</sup> Dakota County and the cities of Eagan, Edina, Mankato, Marshall, St. Paul, and White Bear Lake.

<sup>13</sup> Minneapolis and Roseville.

### Figure 3.2: Public and Site Improvements Financed with Tax Increments from Post-1990 Districts in Sample Cities

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

Maple Grove                      Oakdale

**Improvement of existing local streets and roads (including curb and gutter):**

Eagan                                  Farmington                                  Fridley                                  White Bear Lake

**Construction of major new highway improvements (including freeway interchanges, bridges, ring roads):**

None

**General downtown improvements (such as sidewalks, lighting, street furniture, etc.):**

Farmington                                  Red Wing

**Extension of utilities to site (storm or sanitary sewer, water):**

Albert Lea	Alexandria	Becker	Bloomington
Branch	Cloquet	Dodge Center	Elk River
Farmington	Fridley	Glencoe	Little Falls
Maple Grove	Morrison County	Nisswa	Oakdale
Red Wing	Renville	St. Cloud	

**Skyways:**

None

**Public parks/recreation:**

None

**Government-owned or leased buildings:**

Hibbing (Family Resource Center)

**Construction of lift station, water wells, water towers:**

Becker (water tower)  
East Grand Forks (water treatment plant)

**Wastewater treatment plants, pre-treatment plants:**

Crow Wing County (septic tanks)

**Drainage and ponding:**

Dodge Center	Farmington	Fridley	Hopkins
Marshall	Oakdale	Plymouth	Vadnais Heights

**Soil corrections (including grading and excavation):**

Albert Lea	Alexandria	Bloomington	Branch
Buffalo	Burnsville	Cloquet	Dakota County
Dodge Center	Elk River	Farmington	Little Falls
Marshall	Minneapolis	Oakdale	Plymouth
Red Wing	Renville	Roseville	St. Cloud
Vadnais Heights	White Bear Lake		

**Burying utilities/power lines:**

None

**Parking ramps and lots:**

Albert Lea	Bloomington	Farmington	Glencoe
Hibbing	Little Falls	Morrison County	Nisswa
Renville			

### Figure 3.2: Public and Site Improvements Financed with Tax Increments from Post-1990 Districts in Sample Cities, continued

#### Landscaping:

Bloomington  
Nisswa  
White Bear Lake

Elk River  
Renville

Farmington  
St. Cloud

Morrison County  
Vadnais Heights

#### Foundations and footings:

Cloquet  
Renville

Dodge Center

Glencoe

Little Falls

Source: Office of the Legislative Auditor.

tions (including grading, excavation, and removing contaminated soils), utility extensions, drainage and ponding improvements, parking ramp and lot construction, and landscaping. Only two cities in our sample used tax increments to extend city services to large, newly developing parts of cities, and no cities used post-1990 increments to construct major new highway improvements or for public parks and recreation projects.

The TIF Act limits the use of TIF for government buildings. Tax increments may not be used to finance buildings used primarily to conduct municipal, county, school district, state, or federal government business. Some cities in our sample have used tax increments to support development projects that **lease** space to government agencies. These projects include:

#### TIF has financed development projects that lease space to government agencies.

- *Roseville*. In 1989 the city used tax increments to help renovate a building which the developer then leased to the U.S. Postal Service for a post office. The State Lottery Office leases space in a building (that also houses a computer company) that received TIF assistance.
- *St. Paul (Riverfront)*: Between 1988 and 1990, the city used tax increments to acquire and demolish old buildings on the Amhoist manufacturing plant site and extend a street to assist with construction of a privately-owned office building that is currently leased to the Minnesota Department of Revenue.
- *St. Paul (Neighborhood Business Development)*: As part of assisting with the construction of a multi-tenant office building, the city used tax increments to help demolish an old bakery building and construct a parking lot. The Attorney General's Office and the Office of the State Auditor currently occupy leased space in this building.
- *Hibbing (Family Resource Center)*: The city used tax increments from a 1991 redevelopment district to renovate a building, which it owns and

leases to a variety of other government agencies, including the school district and county.<sup>14</sup>

In some situations, the original intended use of a building receiving TIF support may not involve leasing space to a government agency. For instance, a developer could construct or renovate a building with TIF assistance without knowing who the building's future tenants will be. Or, a developer could receive TIF assistance to help construct a building that is intended to be leased to a government agency.

### **Public Improvements and Community Projects**

We examined the extent to which cities in our sample use tax increments to finance general public improvements that normally could be financed from sources other than tax increment financing. Examples include park and recreation improvements, community centers, bridges, road improvements and streetscaping, water towers, and wastewater treatment plants.

Some legislators expressed concern about cities using tax increments for public improvements and community projects that are not related to the original TIF plan or to the TIF objectives of building the tax base, producing jobs, eliminating blight, and providing affordable housing. Instead of repaying bonds and decertifying districts, cities use tax increment revenues to finance public improvement projects that primarily benefit the cities. Normally, cities would finance these public improvements with increased tax levies, special assessments, bond issues, and user fees. By using tax increments, cities do not have to ask the taxpayers directly for the money (through a bond referendum or increased taxes) or justify why the improvements are needed. In effect, the state, counties, school districts, and other taxing jurisdictions are subsidizing city improvements.

City officials, on the other hand, consider TIF one of the few remaining financing tools for public improvements, especially given the reduced availability of federal funds for projects such as wastewater treatment plants and highway improvements. Officials told us that the public improvement projects funded with tax increments are necessary to stimulate economic development. They also pointed out that, when feasible, they have funded public improvements using a variety of sources, including TIF. For example, Marshall used tax increments from three TIF districts to finance about two-fifths of its wastewater treatment plant. Increased user fees and assessments financed the remainder of the plant. In another case, city officials said that a financial analysis revealed that special assessments alone would not be sufficient to finance construction of a freeway interchange, so tax increment financing provided an additional source of revenue.

Based on our analysis of cities in our sample, we found that:

- **Many cities and development authorities have amended existing pre-1990 tax increment plans in order to spend tax increments for**

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<sup>14</sup> City officials told us that the original intent of the TIF district was to renovate the building for use by a private company. When that proposal fell through, it converted the building to its current use as a Family Resource Center.

**general public improvements and community projects that were not part of the original tax increment plan. So far, such projects are not evident in post-1990 districts.**

Our evaluation found that cities are not using tax increments from post-1990 districts to finance public improvements beyond those contained in the original TIF plan. As noted earlier, many post-1990 districts are just starting to generate the tax increments needed to finance projects in the original TIF plan. Nevertheless, under current law, no more than 20 or 25 percent of the tax increments from post-1990 districts may be pooled. In addition, the use of tax increments from post-1990 districts is limited to activities for which bonds have been issued or other binding legal commitments have been made within five years after approval of the district.

Amendments to TIF plans authorizing increased tax increment spending to finance public improvement projects occurred primarily in pre-1990 districts. For example:

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**Many cities have used tax increments from pre-1990 districts to finance general public improvements.**

- *Cloquet.* Tax increments from an economic development district (scheduled to be decertified in 1996) will partially finance the resurfacing of Cloquet Avenue and replacement of curbs, sidewalks, storm and sanitary sewers, and water mains.
- *Shakopee.* Projects funded with pooled tax increments have included: downtown street and streetscape improvements, a highway bypass, a highway bridge and junction, and storm drainage improvements. In August 1995, the city approved a plan for additional tax increment spending for construction of a community center, park improvements, the city's contribution to the Chaska sanitary sewer interceptor, and downtown alley reconstruction.
- *Mankato and St. Cloud.* Both cities used TIF to help construct civic centers.
- *Maple Grove.* The city modified the Wedgewood Commerce Center redevelopment district plan in 1992 and 1995 to authorize increased tax increment spending for a combination of development and public improvement projects. The public improvements included road improvements, development of a freeway interchange at I-94 and Weaver Lake Road, and pedestrian trail and bridge improvements, including a freeway overpass.
- *Buffalo.* Tax increments from the city's pre-1979 downtown district have or will be used to reroute a county highway, expand the park system along Buffalo Lake and construct a rest area, improve drainage and storm sewers, install a looped water main, construct a bike and pedestrian path, improve downtown streetscaping, and develop a pedestrian-oriented marina.

- *Elk River.* The city has used increments from its water tower economic development districts to acquire eight acres of land to expand a city park, 160 acres to establish Woodland Trails Park, and 5.5 acres of railroad corridor for additions to the city trail system.
- *Roseville.* The city has used pooled increments to finance construction of an outdoor ice oval, an indoor ice arena, a gymnasium for an elementary school, a bridge over County Road B2, and traffic improvements at County Road B and Fairview Avenue. The city also used tax increments to contribute to siting and parking improvements for a Ramsey County library.
- *International Falls.* Plan amendments in 1992 authorized the city to use tax increments from the Boise Cascade economic development district to pay for a water tower, looped water main, settling basin, water main replacement, highway improvements, and other public improvements.
- *Marshall.* In 1992, the city authorized the use of tax increments from three districts to repay bonds for expansion of the city's wastewater treatment plant. Increments from the Minnesota Corn Processors, Schwan's, and Heartland Foods redevelopment districts financed approximately two-fifths of the total plant expansion costs.
- *Glencoe.* In 1993, the city used pooled tax increments from its pre-1979 downtown district and three other districts to finance reconstruction of all downtown streets (including street resurfacing and replacement of curbs and gutters, storm and sanitary sewers, and water mains).

Some cities also create tax increment districts to provide public services or increase the existing capacity of public services, with the expectation that this will stimulate development. Some people argue that these projects represent examples of how tax increment financing is intended to be used -- to provide funding for public improvements that are necessary to stimulate development, create jobs, and increase the tax base. Others argue that cities should finance these projects through methods other than TIF. Most of these projects were in pre-1990 districts, as the following examples illustrate:

- *Elk River.* In the early 1980s, the city identified a severe deficiency in the storage capacity of its existing water system which limited the city's future development. In 1985 and 1986, the city created two economic development districts to finance construction of a water tower and related water system improvements. These public improvements enabled extensive commercial and residential development to occur within the TIF districts.
- *Dundas.* The city does not have a central sewer system. It created a TIF redevelopment district in 1989 to assist with development of a Kmart store and it planned to use tax increments not pledged to debt service to finance construction of a central sanitary sewer system. This has not occurred

because the city of Northfield has agreed to allow Dundas to hook in to its central sewer system.

- *Plymouth.* All of Plymouth's 13 pre-1990 districts were created to finance construction of major roads and freeway interchanges. City officials told us that the lack of adequate freeway access hampered the city's economic development.
- *Woodbury.* A 1986 traffic study determined that the city needed two freeway interchanges and local road improvements. The city created three TIF districts in April 1990 to help finance construction of one freeway interchange and other road improvements. In 1994, Woodbury issued bonds for the interchange project, which was completed in the fall of 1995.

We also found a few examples of public improvement projects in post-1990 districts, although the public improvements in these examples were intended to benefit particular development projects:

- *Becker.* In 1993, the city used TIF to finance construction of a new city water tower and a number of public improvements related to construction of a cardboard recycling facility.
- *East Grand Forks.* The city used tax increments from a 1991 redevelopment district to partially finance improvements to the city's water treatment plant and water distribution system. These improvements facilitated expansion of an American Crystal Sugar plant.

The use of large project areas, pooling, and the ability to amend TIF plans to increase spending enables cities to use tax increments to finance public improvements and community projects that were not part of the original TIF plan. Rather than returning tax increment districts to the tax rolls once the bonds are retired, cities may be tempted to identify additional "needs" that require the contribution of TIF funding. In this manner, tax increment financing may become a convenient financing mechanism that allows cities to "borrow" development revenues from other taxing jurisdictions.

## Financial Status of Tax Increment Districts

While we did not conduct a financial audit, we reviewed the financial status of over 400 TIF districts in our sample cities. We found that:

- **The majority of districts are financially stable and generate sufficient tax increment revenues to pay for project costs. Only a few cities have needed to levy general taxes to make up for revenue shortfalls.**

If a city or development authority issues general obligation tax increment financing bonds and a district does not generate the necessary tax increments, then the city has several options. It can rely on general property tax revenues to support

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**Cities may be tempted to identify additional "needs" that require the contribution of TIF funding.**

the district or it can use pooled increments from other successful tax increment districts to make debt service payments. We found several cities relying on general tax levies to support unsuccessful districts.

- *Bloomington (Oxboro TID O-1)*: Market conditions did not support the city's redevelopment plans for this district. In 1994, the city levied \$484,000 in general property taxes to support the project. Bond refunding and debt restructuring in 1995 will reduce the tax levy needed to support the district to \$250,000 per year. The city also transferred \$116,275 in pooled tax increments from its Nativity of Mary pre-1979 district to Oxboro O-1 in 1995.
- *Hibbing (Chopsticks)*: The city created this economic development district to facilitate construction of a chopsticks factory which subsequently closed. The city levies between \$120,000 and \$126,000 a year to cover debt service on bonds that were issued for development of an industrial park. The district was decertified on December 21, 1992.<sup>15</sup>
- *East Grant Forks (Burlington Northern Triangle TIDs)*: The city created two districts to redevelop rail yards and industrial property. The area has not been renovated and a grain elevator on the property burned down in 1993, reducing the district's tax capacity. The city uses about \$24,000 from a combination of lease payments and general city funds to make debt service payments.

Some cities use pooled increments from successful districts to support districts that are not able to generate enough increments to pay project costs. Examples include:

- *Glencoe (Industrial Park)*: The city created a redevelopment district in 1987 to develop an industrial park. A \$1.2 million TIF bond financed land acquisition, public improvements, and site preparation. The district has not been self-supporting; the city used tax increments from a 1983 housing district to make debt service payments. City officials told us that only three lots remain undeveloped in the industrial park and the district should be self-supporting by the end of 1995.
- *White Bear Lake (Highway 61 West and Depot TIDs)*: The city created these downtown redevelopment districts in April 1990 to remove blighted structures and provide infrastructure improvements for new residential and commercial development. TIF bonds of \$3.8 million financed demolition and relocation costs, street and sewer improvements, and other costs. The hoped for development has not yet occurred; the districts have not generated any tax increments. The city is using pooled tax increments from other TIF districts to make debt service payments.

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<sup>15</sup> This district was recertified as part of a redevelopment district in 1993 for development of an industrial park.

Finally, our sample included a number of non-performing districts using pay-as-you-go financing arrangements which require the developer to pay for development costs up-front. This type of financing arrangement can reduce a city's risk. If the project does not develop as scheduled, then the developer usually ends up absorbing the loss. Examples of districts with pay-as-you-go financing that did not develop as planned include:

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**"Pay-as-you-go" financing requires a developer to pay site acquisition or preparation costs up front.**

- *Buffalo (Polka Dot Recycling)*: The city created this economic development district to support construction of a recycling business. After some delay, the developer constructed a 12,600 square foot industrial building and then went bankrupt. The city has not made any payments for this project.
- *Mankato (National Poly Products TID 6b)*: The city budgeted \$500,000 in tax increments to reimburse the developer for construction of a 70,000 square foot industrial facility in this redevelopment district. The company decided to build in another Mankato location. The city is soliciting other proposals for the site.
- *Nisswa (Nisswa Lakes Plaza)*: Originally, the city envisioned development of a major retail mall in this redevelopment district with up to \$3.2 million in tax increment revenues used to reimburse the developer for public and site improvements. So far only a motel has been developed on the site. The city will use \$304,000 in tax increments to reimburse the motel developer for public utility and improvement costs.

## Financing Trends

Cities have a number of options available to them for financing the up-front development costs for tax increment financing projects, including: general obligation bonds of a city or development authority, revenue bonds, internal financing (such as borrowing from other city accounts), and pay-as-you-go arrangements. (See discussion in Chapter 1.)

We attempted to analyze financing trends for tax increment districts using (1) the annual financial reports filed with the Office of the State Auditor for the year ended December 31, 1994, and (2) the TIF district bonded indebtedness report filed by cities with the Department of Revenue for outstanding debt on December 31, 1994. These sources collect different types of debt information related to tax increment districts. The annual financial reports provide audited financial information on TIF bonded indebtedness. The debt reports are self-reported by cities and provide information on bonded indebtedness and outstanding principal on loans from authority funds, development agreements used in pay-as-you-go financing arrangements, and other binding financial agreements. Unfortunately, we found that:

- **The self-reported TIF debt information is not always consistent with the audited TIF bonded indebtedness data.**

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**The use of  
"pay-as-you-go"  
and internal  
city financing  
of TIF projects  
has increased.**

The Office of the State Auditor reported that cities had \$1.36 billion in outstanding TIF bonded indebtedness at the end of 1994. Cities with populations over 2,500 accounted for 95 percent of the total TIF debt; general obligation TIF bonds accounted for 72 percent of the total debt. However, cities reported a total of \$956.2 million in TIF bonded indebtedness to the Revenue Department, which was 30 percent less than the audited figures from the State Auditor's Office.

The true extent of pay-as-you-go and internal financing is difficult to measure. The city bonded indebtedness report to the Revenue Department is the only central source of information on the use of internal financing and developer agreements, but we lack confidence in that data because it is not always consistent with audited data for bonded indebtedness. Nevertheless, that report indicated that cities had \$74.6 million in outstanding principal on loans from authority funds or revenue notes at the end of 1994, plus \$119 million in outstanding principal from development agreements and \$88.3 million in outstanding principal from other binding financial obligations.

If information from our sample cities is an accurate reflection of overall trends, we conclude that the use of pay-as-you-go and internal financing has increased. Among the 172 post-1990 districts in our sample, over half used pay-as-you-go financing arrangements, one-quarter used various forms of internal financing, and less than one-fifth issued bonds to finance the preliminary project costs. We also found that amendments to TIF plans for pre-1990 districts provided for pay-as-you-go financing to fund increased spending or additional projects.

When the 1995 Legislature gave the Office of the State Auditor responsibility for enforcing TIF laws, it also consolidated the TIF financial reporting requirements in the State Auditor's Office. We think the bonded debt report should continue to summarize information on internal and pay-as-you-go financing obligations. We are hopeful that these changes will result in more reliable financial data for TIF activity in the future.

Pay-as-you-go financing can reduce a city's costs of issuing bonds and a city's risk if a project does not get implemented. Depending on how pay-as-you-go financing is structured, developers may assume most of the risk for failed projects. However, while some cities specifically identify developer costs eligible for reimbursement and require documentation of those costs (land write-down, utility extensions, etc.), others obtain little documentation of actual expenditures. In the latter cases, it may be difficult to ensure that developers are using TIF funds for activities allowed by state law.

A number of projects receiving tax increment support also received Economic Recovery Funds from the Minnesota Department of Trade and Economic Development (DTED). Appendix B lists the 32 tax increment districts in 22 of the cities and towns we visited that also received DTED Economic Recovery Funds. In addition, some development authorities also operate revolving loan funds and industrial revenue bond programs and use these programs to provide additional financial support to projects located in TIF districts.

We found that very few cities routinely collect information on the number of jobs created or wages and salaries paid by businesses and industries receiving TIF support. Therefore, we are unable to make any conclusions or projections about the number or types of jobs created or the wage levels paid related to these projects. An objective analysis of TIF's employment impacts would be difficult to conduct because of this scarcity of job information.

## Decertified Districts

County auditors decertify a tax increment financing district when the district reaches the end of its statutory duration limit. City officials may also notify the county auditor that they want to decertify a district prior to its mandated expiration. There is no central source of information on decertified districts. We asked cities and counties in our sample about decertified tax increment districts. Appendix C contains a list of 72 tax increment districts that city officials told us they have decertified or planned to decertify at the end of 1995 or in the near future. We found that:

- **Generally, cities do not decertify tax increment districts before their expiration dates.**

Over two-thirds of the decertified tax increment districts were economic development districts at the end of their duration limits or unsuccessful districts. Using the Revenue Department's TIF Supplement database, we estimate that approximately 192 economic development districts, or 38 percent of all existing economic development districts, should be decertified in the next three years.<sup>16</sup>

## The "But For" Test

The Tax Increment Financing Act requires that before a city establishes a TIF district, the governing body must find 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..."<sup>17</sup> This requirement, known as the "but for" test, is intended to restrict the use of TIF. However, its usefulness depends on how cities apply the "but for" test. We reviewed TIF plans in our sample cities and interviewed city officials to see how they determine that a development meets the "but for" test. We found that:

- **Cities interpret the "but for" requirement in a variety of ways.**

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<sup>16</sup> These numbers are based on the assumption that the duration of economic development districts will be 10 years from the date certified. The estimates are approximate because of reporting problems with district type information in the TIF Supplement.

<sup>17</sup> *Minn. Stat.* §469.175, Subd. 3 (2). In 1995, the Legislature added another condition for the "but for" test. The new condition requires the city to find that the use of TIF will increase the market value of the site over that which would occur without TIF. In applying the new condition, the city must deduct the present value of the TIF subsidies from the projected market value of the TIF development. Qualified housing districts are exempt from the new "but for" test. *Minn. Laws* (1995), Ch. 264, Art. 5, Sec. 18.)

Figure 3.3 shows cities' interpretations of the "but for" requirement. Cities frequently use the high cost of a proposed development to justify public assistance. Some cities analyze project costs and expected financial returns and determine that financial assistance is required for a developer to earn a reasonable profit on his investment. If a proposed project requires demolition of existing buildings or other site improvements and the developer could construct a similar facility on vacant land in another city, then city officials may determine that the request for assistance is justified based on the higher project costs.

### Figure 3.3: Interpretations of the "But For" Test

- |                               |   |
|-------------------------------|---|
| 1. <b>Cost</b>                | A city cites unusual circumstances, such as the need to remove blighted structures or the need to treat contaminated soils, making the project too expensive without public assistance.   |
| 2. <b>Location</b>            | A city recognizes that the proposed development would occur without assistance, but it uses TIF to make sure the development occurs in this city and not another, and at a location consistent with the city's development goals. |
| 3. <b>Timing</b>              | A city concedes that development could occur without assistance, but it concludes that development will occur sooner if the city provides assistance.   |
| 4. <b>Scope and Quality</b>   | A development might occur without public assistance, but it will be bigger or better with assistance.   |
| 5. <b>Ultimatums</b>          | An existing company wishes to expand and threatens to go elsewhere if it does not receive assistance.   |
| 6. <b>Public Improvements</b> | A city makes public improvements, such as developing an industrial park, improving the appearance of downtown, or improving roads to make the city more attractive to new businesses.   |

**It is difficult for a development project not to meet the "but for" test.**

Sometimes, cities use TIF to ensure that a facility's location is consistent with city development goals. Many cities are interested in redeveloping blighted parts of the city and maintaining the viability of their central business districts. They may use TIF to assist a retail development downtown when the developer might be willing to locate at another city location without TIF. Fairmont, for example, established five tax increment districts to help local banks renovate existing downtown buildings rather than building new facilities on the outskirts of town.

In some cases, city officials told us that development might have occurred without TIF assistance, but the TIF support made the development occur sooner. In other cases, a development was going to occur, but cities provided assistance to ensure that the developer constructed a larger or better quality facility. For example, Brooklyn Park officials said they provided assistance to the developer of the Boone Avenue Business Center (TID 13) because the city did not want a cheap looking structure in a prestigious business area.

Companies sometimes request financial assistance as an incentive to locate in a particular city, and that city's officials assume that if they do not offer TIF assistance, another city will. The same is true when an existing facility wishes to expand and seeks assistance. In these cases, city officials feel that if they do not provide assistance, the company will expand someplace else. Frequently, it is difficult for city officials to judge whether a company truly intends to move. City officials, however, are often unwilling to risk the loss of tax base and jobs on the chance that a company might be bluffing.

Several cities in our sample established TIF districts to fund public improvements to facilitate development. The most common example is extending sewer and water utilities (and sometimes streets) to new industrial parks. Other cities created TIF districts to construct highway interchanges, widen or extend roads, and install traffic signals. Cities have concluded that these public improvements meet the "but for" test because development would not be feasible without them.

Given the variety of interpretations available, it is difficult to imagine a development that would not meet the "but for" test in some sense. Ultimately, however, the "but for" analysis evaluates the merits of a proposed development from the city's perspective, not the county's or state's perspective. If the "but for" analysis for a proposed development were conducted from the county or state perspective, the outcomes would likely be different. From the state's perspective, using TIF to subsidize a manufacturing company that could relocate in any number of Minnesota cities is much less likely to result in a net increase in jobs than using state resources to attract a manufacturing company that competes in national or international markets.

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**"But for" analyses are based on cities' perspectives, not the state's.**

The tax increment financing law requires that the city or development authority "set forth in writing the reasons and supporting facts" for the "but for" finding. Some cities in our sample require developers to submit financial statements documenting proposed project costs and expected financial returns. One financial consultant we interviewed said that he compares a developer's figures with industry construction costs and area rental rates to determine if the developer requires financial assistance to earn a reasonable return on his investment. This type of analysis is based on projected figures of developers and judgments of city officials. For recent soils condition districts, some cities provided cost estimates from engineering consultants to document projected soil correction costs.

Some city officials had copies of letters from companies or financial institutions that said the project would not be feasible without TIF, although some of the letters were written after the city established the TIF district. In some cases, the TIF plan or the city council resolution establishing the district contained a statement of finding for the "but for" requirement, but we found that:

- **Some cities were unable to provide documentation or analysis supporting their finding that a TIF district met the "but for" requirement.**

Rather, they relied on their first-hand knowledge of the project to assure us that it would not have proceeded without TIF.

## Blight Criteria for Redevelopment Districts

The criteria in state law for determining blighted conditions have changed several times since 1979. Under current law, in order to create a redevelopment district, a city must find that parcels containing 70 percent of the area of the district must be occupied by buildings, streets, utilities, or other improvements and that more than 50 percent of the buildings must be structurally substandard to a degree requiring substantial renovation or clearance.<sup>18</sup> For districts certified after October 3, 1989, at least 90 percent of tax increments collected must be spent to eliminate the blight conditions that justified creation of the redevelopment district.

We reviewed the recent redevelopment districts in our sample cities to see how they met those requirements and asked cities officials to provide us with the supporting evidence that their recent redevelopment districts met the statutory requirements. We found that:

- **Statutory changes to the "blight" requirements have reduced the tendency of cities to create very large redevelopment districts or to use redevelopment districts for purposes other than rehabilitating blighted parts of a city.**

The TIF Act allows cities to create noncontiguous TIF districts. During the 1980s, several cities created districts that included aging parts of the city along with undeveloped areas intended for retail or industrial development. Examples include: Chaska's Flood Control district (1985), which includes the city's downtown, the river front area, and undeveloped land in the northern part of the city earmarked for industrial development; Dodge Center's Airport district (1983), which includes the airport, a manufacturing firm that was planning to expand, and some businesses containing old buildings; and Vadnais Heights' SEH/Super America district (1989), a scattered site district consisting of parcels with old houses on one side of the freeway and undeveloped land on the other.

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**Legislative restrictions have made it difficult to create large, scattered-site redevelopment districts.**

Several statutory changes have made it difficult for cities to create large, scattered-site redevelopment districts like those illustrated above. The 1989 Legislature required parcels containing 70 percent of the area, rather than 70 percent of the parcels, to be occupied. It also added a requirement that, for noncontiguous districts, *all parts* of the district (plus the district as a whole) must separately meet the law's blight requirements. Thus, the Chaska example cited above, which was able to meet the 70 percent occupancy requirement by combining a few large undeveloped parcels with many smaller inner city parcels, would not qualify as a redevelopment district under the current definition. Other scattered site districts cited above would qualify only if each of the sites met the blight criteria contained in law. As a result:

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<sup>18</sup> In 1990, the Legislature added a definition of structurally substandard to the TIF statute and created renewal and renovation districts. (See Figures 1.4 and 1.5.) According to the TIF Supplement, there were only five renewal and renovation districts created between 1990 and 1995.

- **Most post-1990 redevelopment districts were smaller than pre-90 districts, were contiguous, and were focused on individual projects.**

Project plans for post-1990 redevelopment districts usually include assistance with demolition or renovation of existing structures and site preparation for new facilities. Nevertheless, it is still possible to create unusually shaped districts. For instance, Glencoe created its Nordic Track district in 1992. The district consists of seven parcels and a stretch of Highway 22 right-of-way. Six parcels contain an empty 165,000 square foot industrial building located outside the city limits that was not served by public utilities. Another parcel contains a single-family house located in the city. The city annexed the industrial site and extended water and sewer to it.

Between 1982 and 1988, cities were permitted to establish redevelopment districts on bare land if 80 percent of the acreage contained unusual terrain or soil deficiencies that required substantial filling, grading, or other physical preparation. Using this criterion, cities created large redevelopment districts to correct excessive or unstable soil, poor drainage, and steep grading. For example, Fridley created its North Area district in 1982 to facilitate industrial and commercial development; Marshall's Minnesota Corn Processors 1982 district consisted of a 90-acre site that had contained a sewage lagoon; and Burnsville created two large districts in 1984 and 1987 to facilitate a mix of housing, office/warehouse, and industrial park developments. In 1988, the Legislature removed poor soils as a criterion for redevelopment districts and created a 12-year soils condition district in its place. In recent years, the Legislature has also tightened the criteria for soils condition districts.

We asked some cities with post-1990 redevelopment districts to provide us with copies of the documentation used to analyze the blight criteria. Some cities provided copies of inspection reports from building inspectors or engineers that found deficiencies such as cracked foundations, leaking roofs, or electricity code violations. Some cities had photographs of blighted conditions or fire-damaged buildings. Some cities' documentation consisted of a statement that city staff had determined that the structures were substandard or in disrepair.

## Reporting Requirements and Other Issues

Our study of tax increment financing was a program evaluation, not a compliance audit. Our purpose for visiting cities was to gain insight into how they were currently using tax increment financing, not to comprehensively audit cities' TIF finances or their compliance with state law. We only found a few specific situations that did not appear to meet the intent of the Minnesota TIF Act, but we discovered several compliance-related issues.<sup>19</sup>

State law requires cities and development authorities to file TIF plans with the state. Over the years the agency required to receive TIF plans changed from State

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<sup>19</sup> For instance, the city of Buffalo expanded the area of its pre-1979 district twice in the early 1990s. City officials told us that the expansions were made to correct mistakes between the map and the legal description in the original documentation.

Planning to the Department of Energy and Economic Development/Trade and Economic Development to the Department of Revenue, where it currently rests. We collected plans for our sample cities from both DTED and the Revenue Department. For cities with post-1990 districts, we found that:

- **Five cities had not filed any TIF plans with the Revenue Department, nearly half had filed some but not all TIF plans, and about 40 percent had filed all TIF plans.**

In addition, some cities submitted plans using "boilerplate" language which did not identify specific development objectives or activities, making it difficult to determine how some cities are using TIF.

TIF laws require cities and development authorities to make annual financial and disclosure reports for *all* tax increment districts to the Office of the State Auditor. State law specifies the content for each of these reports. The State Auditor's Office developed the annual financial reporting form, called the Schedule of Sources and Uses of Public Funds. According to the State Auditor's Office, 21 of the over 340 Minnesota cities with TIF districts in 1994 did not file an annual financial report for their TIF districts. We also found that:

- **The quality of annual financial reports for tax increment districts is mixed.**

While nearly all cities and development authorities file annual financial reports with the Office of the State Auditor, some cities had not included reports for all of their districts. For instance, some cities only filed a report for districts with captured value. Several cities filed one combined statement for all pooled districts, making it impossible to analyze revenues and spending for individual districts.<sup>20</sup> Many cities filed incomplete statements. For instance, few cities provided information on the nature of land write-downs given, as statutes require. Finally, nine of the sample cities filed unaudited annual TIF financial reports.

Another possible compliance issue is the monitoring of low- and moderate-income requirements for housing districts. Cities have a variety of methods for monitoring income requirements. If the project received state or federal funding, in addition to tax increment support, then state or federal housing or financial agencies may conduct the monitoring. Some city HRAs, which are frequently the TIF development authorities, are responsible for monitoring. One city in our sample contracts with the county HRA for monitoring services. Some cities require the building owner to submit annual reports on occupancy and income to the city. However, we also found that some cities do not appear to have any monitoring procedures in place or do not appear to be enforcing the monitoring requirements for housing districts.

During our city visits and interviews with county officials, we asked about implementation of "knock-down provisions" of state law. These provisions limit the ability of a city to collect increments from a district or parcels in a district if the

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**Some cities may not be enforcing housing district income requirements.**

<sup>20</sup> One city's annual financial statement was based on bonds issued not TIF districts.

city has not, within a specified time limit, issued bonds or constructed public improvements, or if the parcel has not been developed. (See the discussion of the "knock-down provisions" in Chapter 1.) City officials told us they allow parcels to be knocked down and then bring those parcels back into the district, with updated tax capacity values, when the city is ready to make public improvements or when a development project is ready to move forward. Some cities told us they have made public improvements to prevent a district from being decertified or parcels from being knocked down. However, a few city officials also told us that they were not sure if county auditors are implementing the knock-down provisions.

## HAVE RESTRICTIONS LIMITED THE ABILITY OF CITIES TO USE TIF?

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**Legislative restrictions have limited the use of economic development districts.**

We think that the legislative restrictions passed in the late 1980s and in 1990 have restricted certain types of development activity. For the most part, 1990 restrictions on the activities in economic development districts have restricted their use to assisting manufacturing and related activities, as defined in statute. In our sample, only five post-1990 economic development districts involved "retail" activity: two districts involved retail development in cities with fewer than 5,000 people and qualified for the 5,000 square foot exception, one supported development of a motel that qualified as a tourism facility, and two assisted electrical service contractors.<sup>21</sup> No post-1990 economic development districts contained office buildings without warehouse facilities.

Restrictions on the blight requirements for redevelopment districts have reduced the tendency of cities to create very large redevelopment districts or to use redevelopment districts for purposes other than rehabilitating blighted parts of the city. Our review of post-1990 redevelopment districts found that these districts were smaller than pre-1990 districts, were contiguous, and were focused on individual projects.

Some cities in our sample used soils condition districts to assist retail stores, manufacturing and office developments, and housing projects. In 1995, the Legislature restricted the use of soils condition districts to contamination and pollution clean-up. While tax increments from economic development districts will be able to correct for sites with bedrock soil conditions, this change means tax increments cannot be used for land needing extensive grading, excavation, filling, and soil compacting. If the new soils condition district criteria had been in effect earlier, most districts in our sample would not have qualified as soils condition districts.

It is difficult to quantify the extent to which cities have not pursued development projects because of possible state aid reductions. Based on interviews with city officials, one impact of the state aid reductions has been to reduce the number of tax increment financing projects that cities have decided to pursue. Some city offi-

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<sup>21</sup> Between 1990 and 1995, cities with a population of less than 5,000 could use economic development districts for up to 5,000 square feet of commercial or retail space.

cials told us that their city councils or development boards have rejected projects because they were not willing to lose any of their state aid. Officials from cities with pre-1990 districts but without any post-1990 districts told us that they were not certifying any additional TIF districts because of the state aid reductions. However, some city officials told us that their city councils took a long-term perspective and were willing to take state aid reductions in return for bringing jobs to the community or increasing the tax base.

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**Some cities have not created new TIF districts because of the state aid reductions.**

In 1995, the Legislature provided cities with an alternative to the state aid reduction. The amendment allows cities to make an annual local contribution to the tax increment district instead of having state aid payments reduced. Cities are still in the process of evaluating the impact of the local contribution. Only a few cities in our sample have used the local contribution option for their recently certified districts. Consequently, it is too early to assess how the local contribution alternative will affect cities' decisions to create new tax increment districts.

Some people suggested to us that cities and other development authorities were creating redevelopment districts instead of economic development districts and were shortening the duration of districts to avoid state aid reductions. We found that, when possible, cities create redevelopment districts. However, only one city in our sample created an odd shaped post-1990 redevelopment district for a project that could have been an economic development district (Glencoe and its Nordic Track district). City officials told us they created a redevelopment district because they needed additional years of increment collection (25 instead of 8) to provide enough revenues to make debt service payments. Regarding early decertification of districts, we found relatively few instances where cities planned to decertify redevelopment districts before their statutory time period expired.

City officials and development consultants expressed concerns about restrictions related to housing districts. First, current legislation limits interest rate reduction (IRR) programs for rental housing projects to a duration of 12 years. However, many low- and moderate-income housing projects receive financing from a combination of sources, including federal low-income housing tax credits which have a term of 15 years. This inconsistency between the IRR program and tax credits means that cities and development authorities need to find other sources of funding for the last three years of an IRR program.

Second, 1993 legislation created a "qualified housing district," for residential rental projects in which all the properties receiving TIF assistance must meet the requirements for federal low-income housing tax credits, regardless of whether the project actually receives a tax credit. Qualified housing districts created after August 1, 1993 are exempt from the state aid reduction. City officials and development consultants expressed an interest in applying the qualified housing district designation to housing districts that meet the criteria but were certified between May 1, 1990 (the effective date of the state aid reduction) and August 1, 1993 and that are currently subject to state aid reductions. However, cities calculated the state aid reduction into the cash flow analysis for housing districts certified prior to August 1, 1993. To change that requirement retroactively could provide those districts with additional, unanticipated tax increment revenues.

## METROPOLITAN COUNCIL POLICIES

The Metropolitan Council coordinates regional development through decisions on regional systems, such as wastewater treatment, transportation, and parks in the seven-county Twin Cities metropolitan area. The Council's *Regional Blueprint* outlines policies needed for the short- and long-term health of the region. We examined the *Blueprint* to determine how its policies compare with how cities are using tax increment financing.

The *Blueprint* contains several policies that are related to local development and the investment of public dollars. The Council supports "local economic development initiatives that retain and foster the growth of local businesses, bring new businesses to the region, add to the tax base and generate new jobs for the region as a whole."<sup>22</sup> The *Blueprint* also states, however, that public resources should be targeted to areas of the region needing redevelopment rather than to undeveloped areas.

The Council will lead a(n)... effort to carry out redevelopment strategies focused on revitalization of distressed areas of the region, especially commercial/industrial revitalization and efforts to strengthen neighborhood vitality. The Council will support the targeting of public and private financial resources for redevelopment and reinvestment.<sup>23</sup>

The policy emphasizes focusing public dollars in the region's distressed areas. It promotes the continued use of TIF to reduce the cost difference between suburban development on vacant land and urban redevelopment of blighted property. The Metropolitan Council has been trying to maximize the use of existing public infrastructure before encouraging development of new infrastructure.

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**Some TIF-supported projects may not be consistent with Metropolitan Council policies.**

Consistent with the Metropolitan Council policies, the cities of Minneapolis and St. Paul and other inner-ring metropolitan suburbs have used TIF to finance redevelopment projects. But TIF has been used by other cities to subsidize new development in some of the fastest growing, most desirable locations within the metropolitan area. For example, suburban cities have used TIF to support commercial/industrial developments along I-694, near the junction of I-694 and Highway 36, along I-94, and near of I-94 and I-494 in the western suburbs.

Some second- and third-tier suburban cities have used TIF to increase the capacity of the metropolitan area's public infrastructure. Examples of TIF-supported public improvements include sewer interceptors, water towers and systems, freeway interchanges, bridges, ring roads, and highway bypasses. Even if cases such as these resulted in increasing jobs and tax base for the region as a whole, the use of public subsidies to support such project may not have been consistent with the Metropolitan Council's regional development goals.

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<sup>22</sup> Metropolitan Council, *Regional Blueprint* (St. Paul, September 1994), 18.

<sup>23</sup> *Regional Blueprint*, 23.

As discussed earlier, legislative changes have made it more difficult for suburban cities to use TIF on vacant land. For example, the Legislature reduced the ability of cities to create large redevelopment districts by adopting stricter blight requirements and eliminating poor soils as justification for a redevelopment district.<sup>24</sup> In addition, legislation restricted economic development districts to manufacturing, warehousing, and related activities. As a result of these restrictions, retail and office projects have occurred, for the most part, in areas that needed redevelopment, rather than on vacant land.

While legislative changes have restricted the use of TIF in suburban cities, it is also possible that some of these restrictions may have limited the ability of the central and inner-ring metropolitan cities to use TIF to eliminate blight and foster redevelopment. For example, the city of St. Paul has not created any new tax increment districts since early 1990. City officials told us that they have been unwilling to lose local government aid from the state, so they have preferred to concentrate on redevelopment projects within districts that were certified prior to 1990.

## SUMMARY

Cities and development authorities have certified 346 tax increment financing districts since April 30, 1990, when legislative amendments on economic development districts, state aid reductions, pooling, and spending restricted the use of TIF. We reviewed 172 post-1990 districts certified in our 46 sample cities and counties. There is less evidence from recently-created tax increment districts of some of the more questionable uses of TIF found in an earlier 1986 evaluation. We found that about two-fifths of the post-1990 districts were created to assist new or existing manufacturing businesses, while office developments, retail facilities, and housing projects each accounted for one-fifth of the districts.

For the most part, 1990 statutory restrictions have limited economic development districts to assisting manufacturing and related activities. While some cities in our sample used soils condition districts to assist with construction of retail stores and office buildings on bare ground, the Legislature addressed this issue in 1995 when it restricted the use of soils condition districts to contamination and pollution clean-up.

Legislative restrictions on the "blight" requirements for redevelopment districts have reduced the tendency of cities to create very large redevelopment districts or to use redevelopment districts for purposes other than rehabilitating blighted parts of the city. Most post-1990 redevelopment districts were smaller than pre-1990 districts, were contiguous, and were focused on individual projects.

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<sup>24</sup> The 1989 Legislature required that, for noncontiguous districts, all parts of the district (plus the district as a whole) must separately meet the law's blight requirements. It also required that 90 percent of the tax increments be used to correct the blight conditions used to justify creation of the district. In 1988, the Legislature removed poor soils as a criterion for redevelopment districts and created a 12-year soils condition district. Legislative amendments in 1995 limited the use of increments from soils condition districts to pollution clean-up, so tax increments from these districts can no longer be used to finance extensive excavation, soil compacting, grading, and filling.

We also found that some cities have created large project areas, encompassing either the entire city or large portions of it, in order to pool of tax increments between two or more districts or to spend tax increments outside the boundaries of the tax increment district. Of the cities and counties in our sample with more than one TIF district, two-thirds have pooled tax increment revenues among districts or have project area configurations that will permit pooling. We found no cities pooling increments from post-1990 districts. However, many post-1990 districts are just starting to generate the tax increments; over half of these districts were certified in 1992 and 1993. Thus, it is still too early to evaluate the 1990 legislative restrictions on pooling and spending placed on post-1990 districts.

Many cities and development authorities have amended existing pre-1990 tax increment plans to authorize increased spending of tax increments on general public improvements and community projects. The use of tax increments to finance public improvements and community projects is not evident in post-1990 districts at this time.

In 1990, the Legislature authorized reductions in state aid to local governments that created new TIF districts. It is difficult to quantify the extent to which cities have not pursued development projects because of possible state aid reductions, although some city officials told us that potential state aid changes have caused them to reduce the number of tax increment projects that they otherwise would have created.