# ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - TAX INCREMENT FINANCING DISTRICTS

Pursuant to North Dakota Century Code Section 54-35-26, created by 2015 Senate Bill No. 2057, a variety of economic development tax incentives are to be reviewed by a Legislative Management interim committee every 6 years. The study is aimed at ensuring that economic development tax incentives are serving their intended purposes in a cost-effective and equitable manner. This memorandum has been provided to assist in the review of tax increment financing (TIF) districts and provides an explanation of TIF districts, the perceived goals of the Legislative Assembly in creating or altering TIF district provisions, and the data and testimony that will be required to conduct an effective analysis of TIF districts.

## EXPLANATION OF TAX INCREMENT FINANCING DISTRICTS

Pursuant to Chapter 40-58, a city may establish a TIF district by adopting a resolution finding that one or more slum or blighted areas or industrial or commercial properties exist which require development, rehabilitation, or conservation in the public interest. The city must prepare a development or renewal plan and hold a public hearing for consideration of the plan. After the hearing, the governing body may approve the plan. Approved development or renewal plans must be filed with the Department of Commerce, Division of Community Services.

To implement the plan, the city may borrow money and accept financial assistance from any available source. The city may appropriate funds and make expenditures to carry out the plan. The city may issue bonds to finance the project and may issue refunding bonds to retire bonds previously issued.

Tax increment financing is used as the repayment mechanism for bonds issued for a development plan. Property values within the TIF district are "frozen" for property tax purposes at the time the district is established. Taxing districts with taxable property situated in the TIF district may continue to levy property tax against the frozen value of the properties. As the district is developed and property values increase, the city may impose a TIF district special fund levy against any valuation exceeding the frozen value of properties in the district. The valuation exceeding the frozen value is referred to as the "incremental value" of the property. Revenue from the TIF district special fund levy is placed in a special fund and used to repay bonds or other financing for TIF district projects.

As an alternative to sale of bonds for a TIF district, the city may grant a total or partial property tax exemption for the project to provide assistance to a project developer. The property tax exemption only applies to the incremental value of the property and may not extend for more than 15 years. The amount to be reimbursed through the property tax exemption is limited to all or a portion of the eligible public costs paid by the project developer, plus interest at a rate of no more than 10 percent per annum, amortized according to an agreement between the project developer and the city. A project developer receiving a property tax exemption as an alternative to tax increment financing may not receive a new business exemption under Chapter 40-57.1.

The governing body of a city shall file a report with the Department of Commerce by July 31 of each year following a year a TIF district was in place. The report must include the name of the TIF district, the total outstanding indebtedness of the district, and the balance of funds on hand. When the cost of projects in the district and any related indebtedness has been fully paid and all bonds have been retired, any amount on hand in the tax increment special fund must be distributed by the county treasurer to the state and all political subdivisions having power to tax the property in amounts proportionate to the amount of tax losses.

A city considering a property tax incentive on any parcel of property for which a development agreement is entered on or after August 1, 2017, which would extend for more than 5 years, shall provide notice to any counties or school districts that would be impacted by the incentive. A county or school district receiving notice shall inform the city, within 30 days of receiving the notice, if the county or school district elects to preclude the incentive from applying to its portion of the property tax levied against the property.

## PERCEIVED GOALS OF THE LEGISLATIVE ASSEMBLY IN CREATING OR ALTERING TAX INCREMENT FINANCING DISTRICT PROVISIONS

Chapter 40-58, regarding urban renewal law, was first enacted in 1955 through the passage of House Bill No. 774. The bill contained provisions noting slum and blighted areas exist in cities and these areas contribute to the spread of disease and crime and substantially impair the sound growth of municipalities. The bill further provided that these areas contribute little in tax revenue while consuming an excessive portion of revenue for police, fire, and other forms of public protection and services. The statement of necessity contained in the bill provided that slum and blighted areas are a matter of state policy and state concern. The bill provisions encouraged cities to provide maximum opportunity for the "rehabilitation or redevelopment of the urban renewal area by private enterprise." The

bill also allowed a city to formulate a workable program for utilizing appropriate private and public resources to "eliminate, and prevent the development or spread of, slums and urban blight, to encourage needed urban rehabilitation."

Specific provisions relating to TIF districts were added to Chapter 40-58 in 1973 by Senate Bill No. 2352. The bill created Section 40-58-20, which provided for the computation, certification, and remittance of tax increments resulting from urban renewal for reimbursement of the cost of urban renewal and the interest and redemption premiums on obligations issued to pay urban renewal costs. Testimony provided on the bill indicated urban renewal efforts had been cut off at the national level and a need existed for local communities to take on renewal projects. The estimated fiscal impact of Section 40-58-20 could not be determined during the 1973 legislative session.

House Bill No. 1463 (1981) retroactively amended Section 40-58-20 as it related to the method for computing the original taxable value of a city-owned parcel for purposes of tax increment financing. The bill provided that property acquired by a city or a city's urban renewal agency before July 1, 1973, or more than 5 years before the approval of an urban renewal plan, whichever is later, is deemed to have an original taxable value of zero. House Bill No. 1645 (1983) authorized a city or the state to acquire fee title to a state historic site or to acquire a historic easement with respect to a privately owned site. The bill also authorized the expenditure of public funds for this purpose, including the proceeds of tax increments or bonds. The bill amended Section 40-58-20 to allow the costs associated with historic preservation projects for which a historic easement is obtained to be included as project renewal costs subject to reimbursement. Senate Bill No. 2427 (1985) provided cities the option to grant a full or partial property tax exemption for up to 15 years, as an alternative to the sale of bonds to be amortized with tax increments, to provide assistance to project developers in urban renewal areas. The amount to be reimbursed through the property tax exemption was limited to an amount sufficient to reimburse all or a portion of the project operator's eligible costs.

Senate Bill No. 2042 (1989), recommended by the 1987-88 interim Job Development Commission, expanded the use of tax increment financing for the development of slum or blighted areas to include financing for the development of unused or underutilized industrial commercial property. The bill authorized a city to use tax increment financing to assist a project developer in the development of unused or underutilized industrial commercial property pursuant to an agreement between the city and the developer. The bill specified the eligible public costs incurred in preparing the property for private development, which would be reimbursable by tax increments. The bill required cities to hold a public hearing and notify potential competitors of the prospective industrial or commercial enterprise prior to entering an agreement with a developer of industrial or commercial property to determine whether the agreement would result in unfair competition and would be in the best interest of the city as a whole. The bill also precluded a project developer receiving a property tax exemption as an alternative to tax increment financing from receiving a new business incentive under Chapter 40-57.1.

Senate Bill No. 2050 (2011) revised the definition of "blighted area" to exclude land assessed as agricultural property within the last 10 years, unless the land was located within the interior boundary of a city for at least 10 years. The bill also required a city to file approved development or renewal area plans with the Department of Commerce. The bill provided that for a TIF district established before July 1, 2011, the base year for purposes of computing tax increments may not be used for more than 25 taxable years without the governing body of the city establishing a new base year using taxable values, established as of February 1 of the following year, which are no more than 15 years old. The new base year may be used to compute tax increments for up to 15 additional years, after which time the TIF district must be closed. An exception was provided for tax increments pledged for indebtedness incurred before July 1, 2011, to allow use of the original base year until the indebtedness is paid.

For a TIF district established after July 1, 2011, the bill provided the base year for purposes of computing tax increments may not be used for more than 25 taxable years without the governing body of the city establishing a new base year using taxable values, established as of February 1 of the following year, which are no more than 15 years old. The new base year may be used to compute tax increments for up to 5 additional years, at which time the TIF district must be closed. The bill authorized the governing body of a city with an active TIF district to identify funds on hand which are in excess of the costs it determines necessary to complete the activities included in the last approved urban renewal plan. The city then may cause the surplus to be transferred to the county treasurer for distribution to the political subdivisions having power to tax property in the area in amounts proportionate to the most recent 5-year average of the property tax levy within the district. The bill also required the governing body of a municipality to conduct a public hearing before approving development or renewal plans and required the filing of an annual report with the Department of Commerce for each development or renewal area in existence at the end of a calendar year.

Senate Bill No. 2166 (2017) provided for the enactment of Section 40-05-24, which requires a city considering a property tax incentive on any parcel of property which would extend for more than 5 years to provide notice regarding the terms of the incentive to any county or school district that would be impacted by the incentive. An impacted county or school district may elect to preclude the incentive from applying to its portion of the property tax levied against the property. A county or school district shall provide the city written notice of its election to opt out within 30 days of receiving the notice from the city. Pursuant to 2017 House Bill No. 1015, property subject to a development agreement entered pursuant to Section 40-58-20.1 before August 1, 2017, is exempt from the requirements under Section 40-05-24.

## DATA AND TESTIMONY REQUIRED TO CONDUCT AN EFFECTIVE ANALYSIS OF TAX INCREMENT FINANCING DISTRICTS

Data pertaining to the following items will need to be collected to effectively analyze the incentive:

1. The number of claimants;
2. The fiscal impact of the incentive;
3. Employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive;
4. Negative impacts created as a result of the incentive; and
5. Benefits that flow to out-of-state concerns resulting from the incentive.

Testimony will need to be solicited from the following parties to effectively analyze the incentive:

1. The Department of Commerce;
2. The Tax Department; and
3. The North Dakota Economic Development Foundation.