

**TAX INCREMENT
FINANCING REPORT**

March 8, 2000

TAX INCREMENT FINANCING REPORT

TABLE OF CONTENTS

I. GENERAL INFORMATION	1
A. INTRODUCTION	1
B. BACKGROUND	1
1. What Is Tax Increment Financing?	1
2. Overview of Tax Increment Financing Act	2
3. Who Uses Tax Increment Financing?	4
4. Statistics on Use of Tax Increment Financing	5
C. OSA’S TIF ENFORCEMENT AUTHORITY	8
II. VIOLATIONS	9
A. “POOLING” OF TAX INCREMENT FROM 1979-82 TIF DISTRICTS	
1. City of Faribault	10
2. City of Cambridge	10
3. City of Dodge Center	12
B. EXPENDITURES OF TAX INCREMENT NOT AUTHORIZED IN TIF PLAN	
1. Bagley HRA	13
2. City of Cambridge	14
C. ADMINISTRATIVE EXPENSES IN EXCESS OF STATUTORY LIMIT	
City of Roseville	14
D. TAX INCREMENT RECEIVED AFTER MAXIMUM DURATION LIMIT	
1. City of Faribault	15
2. City of Cambridge	16
E. IMPROPER WAIVING OF TAX INCREMENT	
City of Faribault	17
F. INADEQUATELY DOCUMENTED EXPENDITURES	
1. City of Faribault	18
2. City of Cambridge	19
G. COSTS NOT ELIGIBLE FOR PAYMENT WITH TAX INCREMENT	
1. City of Faribault	19
2. City of Cambridge	20
H. PAYMENT OF TAX INCREMENT TO PROPERTY OWNERS NOT	
AUTHORIZED IN TIF PLAN	
City of Cambridge	22
I. EXPENDITURE OF TAX INCREMENT FROM A HOUSING DISTRICT OUTSIDE	
VALID HOUSING PROJECT AREA	
City of Cambridge	23

J. LACK OF EVIDENCE THAT BUILDING WAS STRUCTURALLY SUBSTANDARD	
City of Cambridge	24
K. NON-CONTIGUOUS AREAS DID NOT QUALIFY FOR INCLUSION IN RENEWAL AND RENOVATION DISTRICT	
City of Cambridge	26
L. IMPROPER LOCAL TAX RATE	
City of Cambridge	27
M. INCOMPLETE MAP ACCOMPANYING PUBLIC HEARING NOTICE	
City of Cambridge	28
N. UNAUTHORIZED EXPENDITURES OF TAX INCREMENT FROM A SOILS CONDITION	
City of Cambridge	29
O. FAILURE TO INFORM COUNTY AUDITOR OF BUILDING PERMIT ISSUED BEFORE APPROVAL OF TIF PLAN	
City of Cambridge	30
III. STATUTORY ISSUES	31
A. SPENDING TAX INCREMENT IN EXCESS OF LINE-ITEM BUDGET AMOUNTS	31
B. COMMINGLING OF TAX INCREMENT WITH OTHER SOURCES OF FUNDS	33
C. DEFINITION OF “ADMINISTRATIVE EXPENSES”	34
D. DEFINITIONS OF “HOUSING DISTRICT,” “PROJECT,” AND “HOUSING PROJECT”	34
E. DEFINITION OF “INCREMENT”	36
F. DISCOUNT RATE TO CALCULATE PRESENT VALUE OF TAX INCREMENT	37
G. LIMITATION ON ADMINISTRATIVE EXPENSES	37
H. USE OF TAX INCREMENT FOR TOURISM FACILITIES	38
I. EXTENSION OF TIME TO RESPOND TO NOTICES OF NONCOMPLIANCE	38
IV. CONCLUSION	39
EXHIBIT 1—Statistics on TIF Reporting for Year Ended December 31, 1998	41

TAX INCREMENT FINANCING REPORT

I. GENERAL INFORMATION

A. INTRODUCTION

In the 1995 Omnibus Tax Act, the Legislature transferred authority for legal-compliance oversight of all tax increment financing (TIF) districts in the state to the Office of the State Auditor (OSA). Local governments were required to file reports with the OSA for more than 2,000 TIF districts for the year ended December 31, 1998. The OSA is required to provide an annual summary of its findings of noncompliance with the state TIF laws and the responses to those findings by the governing bodies of the relevant municipalities.¹ This report is submitted to the chairs of the legislative committees which have jurisdiction over tax increment financing.

B. BACKGROUND

1. What Is Tax Increment Financing?

Tax increment financing (TIF) is a statutory tool to promote economic development, redevelopment, and housing in areas where it otherwise would not have occurred. A TIF authority, typically a city, a county, or an entity created by a city or county, captures the increase in net tax capacity resulting from new development within a designated geographic area called a TIF district. The TIF authority uses the tax increments, which are the property taxes paid on the captured increase in net tax capacity, to pay for TIF-eligible costs of the new development that generated the increase in net tax capacity.

The property taxes on the captured net tax capacity are paid to the TIF authority rather than to the city or town, county, and school district. The school district recovers most of the property tax revenue it loses to the TIF authority through an increase in state education aid payments.

TIF is not a property tax abatement program. The owner of the property in the TIF district continues to pay the full amount of property taxes. The portion of those property taxes generated by the new development, however, is used to pay some of the development costs that the owner, developer, or local government otherwise would have paid.

Examples of TIF-eligible costs are land and building acquisition, demolition of structurally substandard buildings, site preparation, installation of utilities, road improvements, and construction of low- or moderate-income housing. The costs that are eligible to be paid from tax increment vary depending on the type of TIF district created and the year in which the district was created.

¹ Minn. Stat. § 469.1771, subd. 1(c) (1998).

The up-front costs of TIF-subsidized development frequently have been financed with the proceeds of general obligation bonds, revenue bonds, loans from external sources, or interfund loans, or through other financing arrangements. The debt service on those obligations is paid with tax increment generated by one or more TIF districts.

An alternative to bonded debt or loans, known as pay-as-you-go financing, is being used with increasing frequency. Under a pay-as-you-go financing arrangement, the property owner or developer pays the development costs up front and is reimbursed if, and when, tax increment is generated by the TIF district.² The risk of insufficient tax increment to reimburse all of the TIF-eligible costs rests with the property owner or developer, rather than with the TIF authority.³

2. Overview of Tax Increment Financing Act

The Minnesota Tax Increment Financing Act (TIF Act) governs the creation and administration of TIF districts.⁴ The following is a summary of the provisions of the TIF Act:

C	Minn. Stat. § 469.174	Definitions;
C	Minn. Stat. § 469.175	Contents of TIF plans, procedures for approving and amending them, and reporting requirements;
C	Minn. Stat. § 469.176	Limitations on expenditure of tax increment and maximum duration limits for TIF districts;
C	Minn. Stat. § 469.1761	Income requirements for housing projects;
C	Minn. Stat. § 469.1762	Arbitration of disputes over county costs;
C	Minn. Stat. § 469.1763	Pooling restrictions and the five-year rule;
•	Minn. Stat. § 469.1764	Ratification of pooling from 1979-82 TIF districts;
C	Minn. Stat. § 469.1765	Rules governing guaranty funds;
C	Minn. Stat. § 469.1766	Restrictions on developer payments;
C	Minn. Stat. § 469.177	Computation of tax increment, requirement to repay excess increment, and deduction to fund OSA enforcement function;
C	Minn. Stat. § 469.1771	Remedies for violations and OSA enforcement authority;
C	Minn. Stat. § 469.178	Tax increment bonding;

² The TIF authority may use tax increment to reimburse only those costs that are TIF-eligible and that the property owner or developer actually has incurred. The TIF authority must obtain from the developer and retain in its files documentation of the costs being reimbursed.

³ Even in situations where bonds are issued or the TIF authority receives an advance of funds, TIF authorities frequently structure the financing arrangements to shift the risk of insufficient tax increment from the TIF authority to the property owner or developer.

⁴ Laws 1979, ch. 322. Initially, the TIF Act was codified at Minn. Stat. §§ 273.71 through 273.78. In 1987, the TIF Act was recodified at Minn. Stat. §§ 469.174 through 469.179.

- C Minn. Stat. § 469.1781 Required expenditures of tax increment for a neighborhood revitalization program where certain bonds have been refunded;
- C Minn. Stat. § 469.1782 Provisions applicable to TIF districts with extended durations as a result of special laws; and
- C Minn. Stat. § 469.179 Presumptions regarding the effective dates of amendments to the TIF Act.

The TIF Act has been amended frequently since its creation in 1979. A TIF district usually is governed by the laws in effect in the year in which the district was created.

The TIF Act divides TIF districts into a number of types, each of which has different requirements for the creation of a district, different maximum duration limits, and different restrictions on the use of tax increment from the district:

- C Pre-1979 districts;
- C Economic development districts;
- C Housing districts;
- C Mined underground space districts;
- C Redevelopment districts;
- C Renewal and renovation districts; and
- C Soils condition districts.

In addition, the TIF Act permits the creation of a hazardous substance subdistrict within a TIF district. A hazardous substance subdistrict has its own statutory requirements for the creation of a subdistrict, maximum duration limit, and restrictions on the use of tax increment.

A related statute⁵ grants special status to certain TIF districts which meet additional qualifications:

- C Qualified housing districts;
- C Qualified ethanol production facility districts;
- C Qualified agricultural processing facility districts; and
- C Qualified manufacturing districts.⁶

In addition, uncodified laws have authorized the creation of a wide variety of special-purpose TIF districts.

⁵ Minn. Stat. § 273.1399 (1998).

⁶ The portion of the statute that granted special status to qualified manufacturing districts was repealed effective for districts with certification request dates after June 30, 1994. Laws 1995, ch. 264, art. 5, sec. 4 and 49.

3. Who Uses Tax Increment Financing?

The TIF Act authorizes TIF authorities to create TIF districts. TIF authorities include housing and redevelopment authorities, port authorities, economic development authorities, municipal redevelopment agencies, rural development financing authorities, cities, and counties. The TIF authority takes the first step in creating a TIF district by adopting a TIF plan for the district. The TIF plan provides information about the project being funded by tax increment from the TIF district, authorizes the use of tax increment from the district to pay TIF-eligible project costs, and establishes a budget for tax increment expenditures.⁷

The governing body of the municipality in which the TIF district is located must approve the TIF plan for the district.⁸ For example, if a city's port authority proposes to create a TIF district in the city, the city council must approve the TIF plan for the district. If a county's housing and redevelopment authority proposes to create a TIF district in a township in the county, the county board must approve the TIF plan.⁹

Before a TIF district is created, the TIF authority must provide certain information about the proposed TIF district to the county board, county auditor, and school board and offer to meet with the county board and school board to discuss the proposed district.¹⁰ The county board and school board may comment on the proposed district, but cannot prevent the creation of the district (except that the county board may prevent creation of the TIF district if the county is the municipality that must approve the TIF plan).

Minnesota local governments' use of TIF is a controversial subject, as is evident from the frequent letters, published in newspapers around the state, criticizing or defending uses of TIF. Recently, controversies over uses of TIF have spawned litigation in Minnesota and throughout the United States.¹¹

⁷ Minn. Stat. § 469.175, subd. 1 and subd. 6(c)(3) (1998).

⁸ Minn. Stat. § 469.175, subd. 3 (1998).

⁹ If a county's housing and redevelopment authority proposes to create a TIF district in a city, it is not clear whether the municipality that must approve the TIF plan is the city, the county, or both.

¹⁰ Minn. Stat. § 469.175, subd. 2 (1998).

¹¹ See, e.g., *Minneapolis Community Dev. Agency v. Opus Northwest, LLC*, 582 N.W. 2d 596 (Minn. Ct. App. 1998); J. Gibeaut, "The Money Chase," *ABA Journal*, March 1999, p. 58.

4. Statistics on Use of Tax Increment Financing

A total of 433 TIF authorities had active TIF districts for which TIF authorities and municipalities were required to report information to the OSA for the year ended December 31, 1998. These TIF authorities and municipalities were required to file reports regarding 2,061 TIF districts. According to the information municipalities filed with the OSA, these 2,061 TIF districts consisted of the following types of TIF districts:¹²

Pre-1979 districts	89
Economic development districts	746
Housing districts	306
Mined underground space districts	0
Redevelopment districts	853
Renewal and renovation districts	19
Soils condition districts	41
Districts authorized by uncodified laws	3
Not reported	<u>4</u>
Total	<u>2,061</u>

Over the years, the number of TIF districts created annually has fluctuated. The following table lists the number of each type of TIF district grouped by the year of each TIF district's certification request date (CRD), starting in 1988.¹³ This unaudited information was reported by municipalities for the year ended December 31, 1998, and therefore does not include information about TIF districts which were decertified and not required to report for the year ended December 31, 1998.

¹² This is unaudited information. A number of municipalities reported that they had economic development, housing, or redevelopment districts with certification request dates on or before July 31, 1979, which is impossible under the law. Any TIF district with a certification request date on or before July 31, 1979, is a pre-1979 district. In addition, the OSA has determined through TIF legal compliance audits that a number of municipalities incorrectly reported the types of their TIF districts.

¹³ This table does not include TIF districts reported to be pre-1979 districts, mined underground space districts, districts authorized by uncodified laws, and districts for which no type was reported. TIF districts with certification request dates before 1988 also were excluded. Many economic development districts created before 1988 were no longer required to report for the year ended December 31, 1998. Therefore, including TIF districts with certification request dates before 1988 would have created the false impression that few economic development districts were created during those earlier years.

CRD Year	Economic Development	Housing	Redevelopment	Renewal & Renovation	Soils Condition	Total
1988	63	9	54	n/a	3	129
1989	109	14	52	n/a	4	179
1990	71	12	48	0	1	132
1991	24	9	18	0	2	53
1992	33	11	29	3	8	84
1993	50	13	49	3	8	123
1994	52	22	42	3	4	123
1995	65	43	60	3	8	179
1996	61	31	68	1	2	163
1997	80	31	59	4	0	174
1998	<u>60</u>	<u>26</u>	<u>55</u>	<u>2</u>	<u>1</u>	<u>144</u>
Total	<u>668</u>	<u>221</u>	<u>534</u>	<u>19</u>	<u>41</u>	<u>1,483</u>

The following tables summarize unaudited financial information reported to the OSA for the year ended December 31, 1998.¹⁴

Source of Funds	Prior Years	Calendar 1998	Total
Tax increment revenue	\$2,386,337,565	\$287,972,245	\$2,674,309,810
Interest on invested funds	416,205,578	30,868,415	447,073,993
Bond proceeds	2,478,286,382	125,916,387	2,604,202,769
Loan proceeds	129,813,777	10,153,150	139,966,927
All other sources of funds (including transfers in)	366,746,134	170,832,996	537,579,130
Total of reported sources of funds	<u>\$5,777,389,435</u>	<u>\$625,743,194</u>	<u>\$6,403,132,629</u>

¹⁴ The numbers in these tables are rounded to the nearest dollar.

Use of Funds	Prior Years	Calendar 1998	Total
Land/building acquisition	\$1,020,623,003	\$74,998,616	\$1,095,621,619
Site improvement/preparation costs	468,993,364	47,949,377	516,942,741
Installation of public utilities	313,390,424	18,802,919	332,193,343
Parking facilities	130,400,777	25,580,410	155,981,186
Streets and sidewalks	184,921,484	15,940,503	200,861,987
Public park facilities	25,877,644	2,681,444	28,559,088
Social, recreational, conference facilities	72,926,391	23,502,080	96,428,471
Bond principal payments	822,260,546	159,104,329	981,364,875
Bond interest payments	694,347,968	52,979,094	747,327,061
Loan principal payments	97,483,139	7,576,689	105,059,828
Loan/note interest payments	46,019,818	12,988,499	59,008,317
Administrative expenses	217,548,845	9,538,302	227,087,147
All other uses of funds (including transfers out)	1,873,039,283	200,737,038	2,073,776,321
Total of reported uses of funds	<u>\$5,967,832,685</u>	<u>\$652,379,399</u>	<u>\$6,620,211,984</u>

In both calendar year 1998 and prior years, the total of the reported uses of funds exceeds the total of reported sources of funds. In other words, TIF authorities reported that their TIF districts spent more money than their TIF districts had available to spend.¹⁵

¹⁵ One possible explanation for this anomaly is the frequent practice of using a non-TIF fund to pay a TIF district's up-front costs, and then improperly recording the up-front costs as being paid from the TIF district's fund. This creates a negative balance in the TIF district's fund, because the TIF district has not yet started to generate tax increment and has received no other sources of funds. Later, when the TIF district generates tax increment and receipts of the increment are recorded in the TIF district's fund, it appears as if the tax increment paid the up-front costs. In such a situation, however, the tax increment did not pay the up-front costs, because the costs were paid before the tax increment was received. It is the OSA's position that a TIF district's account cannot have a negative balance. If no loan or transfer was made to the TIF district's fund to pay the up-front costs, then the expenditures for these costs should be recorded in the fund whose money was used to pay these costs.

C. OSA'S TIF ENFORCEMENT AUTHORITY

The 1995 Omnibus Tax Act transferred the responsibility for investigating and reporting whether local governments are in compliance with the TIF Act from the Department of Revenue to the OSA.¹⁶ The OSA may examine and audit the accounts and records of TIF authorities on a random basis to determine if they are complying with the TIF Act.¹⁷ The 1995 act also transferred to the OSA the responsibility for collecting the information that TIF authorities and municipalities are required to report annually about their TIF districts.¹⁸

The OSA created a TIF Division to perform these TIF enforcement functions. The TIF Division began its enforcement activities on January 1, 1996. The TIF Division currently consists of a director, seven TIF auditors, and an office specialist.

The operations of the TIF Division are funded exclusively from revenue derived by deducting 0.25 percent of all tax increment that county treasurers distribute to TIF authorities and municipalities.¹⁹ The county treasurers deduct the revenue before distributing the tax increment to the local governments, and then pay the deducted revenue to the state treasurer. The amount of revenue to fund the TIF Division will vary with the number of TIF districts and the amount of tax increment generated.

The TIF Division focuses on annual collection and review of TIF reports, on conducting legal compliance audits and investigations, and on education. Exhibit 1 to this report, beginning on page 41, reviews the statutory reporting requirements for TIF districts and details the statistics on TIF reporting for the year ended December 31, 1998. Section II of this report, which immediately follows this section, discusses details of the various TIF legal compliance audits and investigations completed in the past year. Complete copies of the initial and final notices of noncompliance and the municipalities' responses are proved in the separately bound appendix to this report.

The TIF Division also has worked actively in the area of tax increment financing education on a statewide level. In June and July of 1999, the OSA provided eight workshops in five locations around the state to assist local governments with completing the 1998 TIF reports. In September and October of 1999, the TIF Division presented a day-long seminar on the basics of tax increment financing, holding one seminar

¹⁶ Laws 1995, ch. 264, art. 5, sec. 34.

¹⁷ Minn. Stat. § 469.1771, subd. 1(b) (1998).

¹⁸ Laws 1995, ch. 264, art. 5, sec. 19 and 21. Prior to 1995, TIF authorities and municipalities reported certain statutorily required information to the Department of Revenue and other required financial information to the OSA.

¹⁹ The TIF enforcement deduction rate was increased from 0.10 percent to 0.25 percent effective for distributions of tax increment to TIF authorities and municipalities made after June 30, 1998. Laws 1998, ch. 366, sec. 79 and 91.

in St. Paul and the second in Alexandria. These seminars were attended by over 230 local government officials and staff, state employees from the executive and legislative branches, and professional TIF advisors. This the second year that the OSA has conducted this day-long seminar. Due to overwhelming positive response, a similar seminar will again be held in the fall of 2000.

II. VIOLATIONS

If the OSA finds that a TIF authority is not in compliance with the TIF Act, a notice of noncompliance is sent to the governing body of the municipality that approved the TIF district in which the violation arose.²⁰ The notice of noncompliance provides the facts and law upon which the OSA relied in making its finding that the TIF authority is not in compliance. In addition, the notice of noncompliance may inform the municipality that Minnesota law requires the TIF authority to pay an amount of money to the county auditor as required to redress certain violations of the TIF Act.²¹

The governing body must respond in writing to the OSA within 60 days after receiving the notice of noncompliance. In its response, the municipality must state whether it accepts, in whole or in part, the OSA's findings. If the municipality does not accept any part of the findings, its response must indicate the basis for its disagreement with the findings.²² The OSA must provide all information regarding unresolved findings of noncompliance to the county attorney, who may bring an action to enforce the TIF Act.²³

The OSA also must provide a summary of the responses it receives from the municipalities, and copies of the responses themselves, to the chairs of the legislative committees with jurisdiction over tax increment financing.²⁴ Appendices A through E of this report contain copies of notices of noncompliance regarding the City of Cambridge, City of Faribault, City of Dodge Center, City of Roseville, and the Bagley HRA and the municipalities' responses. This section discusses the more significant findings, in terms of financial impact and frequency of occurrence, contained in these notices of noncompliance.

²⁰ Minn. Stat. § 469.1771, subd. 1(c) (1998).

²¹ *See* Minn. Stat. § 469.1771, subd. 2 and 3 (1998).

²² Minn. Stat. § 469.1771, subd. 1(c) (1998).

²³ Minn. Stat. § 469.1771, subd. 1(b) (1998). A new enforcement mechanism involving the attorney general applies only to final notices of noncompliance issued by the OSA after December 31, 1999. *See* Minn. Stat. § 469.1771, subd. 2b (Supp. 1999); Laws 1999, art. 10, sec. 5, 6, and 29. Therefore, this mechanism does not apply to any of the notices of noncompliance discussed in this report.

²⁴ Minn. Stat. § 469.1771, subd. 1(c) (1998).

A. “POOLING” OF TAX INCREMENT FROM 1979-82 TIF DISTRICTS

1. City of Faribault

On May 1, 1998, the OSA sent the City of Faribault a notice of noncompliance. In the notice, the OSA found that the city had improperly spent tax increment from the Redevelopment TIF District on activities outside the geographic boundaries of the TIF district. The city requested certification of the Redevelopment TIF District on August 28, 1981. It was the OSA’s position that the TIF Act did not permit “pooling” of tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982.²⁵

After the OSA issued the May 1, 1998, notice of noncompliance to the city, the Legislature confirmed that pooling of tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982, was not permitted by the TIF Act, except to pay debt service on city development district revenue bonds issued pursuant to Minn. Stat. § 469.129, subd. 2.²⁶ Those TIF authorities that improperly pooled tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982, are now subject to a new law under which the pooling expenditures before December 31, 1999, are ratified, but such TIF districts now are required to restrict expenditures of tax increment for activities within and outside the district and are required to be decertified early.²⁷ The OSA concluded that this finding of noncompliance was resolved by the 1999 enactment of Minn. Stat. § 469.1764.

The OSA referred other findings of noncompliance in this matter to the Rice County Attorney by letter dated November 19, 1999. Copies of the OSA’s notices of noncompliance and the city’s responses regarding this matter are included in Appendix A.

2. City of Cambridge

On December 31, 1998, the OSA sent the City of Cambridge a notice of noncompliance. In the notice, the OSA found that the city had improperly transferred \$344,942.13 of tax increment out of the funds for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 (Kroy Industries) to be spent on activities outside the geographic boundaries of the TIF district that generated the tax increment.

²⁵ “Pool” or “pooling” are words commonly used to describe spending tax increment on activities outside the geographic boundaries of the TIF district that generated the increment.

²⁶ See Minn. Stat. § 469.1764, subd. 1 (Supp. 1999). City development district revenue bonds may not be issued under Minn. Stat. § 469.129, subd. 2 after April 30, 1990.

²⁷ See Minn. Stat. § 469.1764, subd. 3 and 4 (Supp. 1999).

The certification request dates for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 were between July 31, 1979, and July 1, 1982. It was the OSA's position that the TIF Act did not permit "pooling" of tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act does not apply to \$62,583.22 of the \$344,942.13 improperly transferred, because \$62,583.22 was transferred on or before December 31, 1990.²⁸ The remaining transfers of \$282,358.91 occurred after December 31, 1990, and are subject to the provisions of the violations payment statute.²⁹

After the OSA issued the December 31, 1998, notice of noncompliance to the city, the Legislature confirmed that pooling of tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982, was not permitted by the TIF Act, except to pay debt service on city development district revenue bonds issued pursuant to Minn. Stat. § 469.129, subd. 2.³⁰ Those TIF authorities that improperly pooled tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982, are now subject to a new law under which the pooling expenditures before December 31, 1999, are ratified, but such TIF districts now are required to restrict expenditures of tax increment for activities within and outside the district and are required to be decertified early.³¹

This new law, however, does not resolve this finding, because the TIF-plan budgets for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 did not authorize the city to transfer these TIF district's tax increment to another TIF district or fund. Tax increment may be transferred or spent only as authorized in the TIF plan.³²

In its response, the city did not dispute that it transferred the amounts of tax increment listed above out of the fund for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 to pay for activities outside the geographic boundaries of the TIF district that generated the tax increment.³³ In addition, for all but one of these findings, the city did not dispute that these transfers violated the TIF Act

²⁸ The 1990 act that created the violations statute within the TIF Act, Minn. Stat. § 469.1771, provided that the statute applies only to violations occurring after December 31, 1990. Laws 1990, ch. 604, art. 7, sec. 25 and 31(a).

²⁹ See Minn. Stat. § 469.1771, subd. 3 (1998).

³⁰ See Minn. Stat. § 469.1764, subd. 1 (Supp. 1999). City development district revenue bonds may not be issued under Minn. Stat. § 469.129, subd. 2 after April 30, 1990.

³¹ See Minn. Stat. § 469.1764, subd. 3 and 4 (Supp. 1999).

³² Minn. Stat. § 469.176, subd. 4 (1998).

³³ The city's response did, however, provide sufficient documentation to allow the OSA to determine that the \$296.90 transfer to an unknown fund actually was a \$52.83 transfer.

if they were made with tax increment.³⁴ Instead, the city argued that the transfers were proper because the city “characterized as non-tax increment monies” the money that it transferred out of the funds for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1.

On December 30, 1999, the OSA sent the city its final notice of noncompliance. The OSA reiterated its findings that the city improperly transferred tax increment out of the funds for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 to be spent on activities outside the geographic boundaries of the TIF district that generated the tax increment, because these transfers were not included in the TIF-plan budgets.³⁵ OSA audit staff was unable to find any documentation to demonstrate that the monies transferred out of the funds for Elderly Housing District 1, Family Housing District 1, and Economic Development District 1 were non-tax increment rather than tax increment. The city’s response provided no such documentation. Therefore, the OSA could not verify that the transfers were made in compliance with the TIF Act.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA’s notices of noncompliance and the city’s responses regarding this matter are included in Appendix B.

3. City of Dodge Center

On May 17, 1999, the OSA sent the City of Dodge Center a notice of noncompliance. In the notice, the OSA found that the city had improperly transferred \$40,000 of tax increment from the fund for TIF District 1 (South Park Manor) to the Wastewater Treatment Plant Fund and the Water Tower Project Fund to spend on activities outside the geographic boundaries of the TIF district. The city requested certification of TIF District 1 on September 25, 1979. It was the OSA’s position that the TIF Act did not permit “pooling” of tax increment from TIF districts with certification request dates after July 31, 1979, and before July 1, 1982.

The city responded that this finding of noncompliance was resolved by the 1999 enactment of Minn. Stat. § 469.1764. On July 8, 1999, the OSA sent the city a final notice of noncompliance in which the OSA

³⁴ The city stated that the transfer of \$153,243 of tax increment from Economic Development District 1 to Economic Development District 2-1 was authorized in the TIF plan for Economic Development District 1 because the city modified the TIF plans for these TIF districts to make them both part of the same large project area. The OSA found that the city did not comply with the statutory procedure for amending the TIF plans for these TIF districts and, therefore, the TIF-plan amendments that enlarged their project areas were not valid. The OSA also concluded that the enlargement of the project areas was irrelevant to this finding, because neither the original nor modified TIF plan for Economic Development District 1 budgeted a transfer to Economic Development District 2-1.

³⁵ The OSA reduced the amount of one of the findings from \$296.90 to \$52.83.

agreed that this finding was resolved. Consequently, the OSA did not refer this matter to the county attorney.

Copies of the OSA's notices of noncompliance and the city's response regarding this matter are included in Appendix C.

B. EXPENDITURES OF TAX INCREMENT NOT AUTHORIZED IN TIF PLAN

1. Bagley HRA

On May 19, 1999, the OSA sent the City of Bagley a notice of noncompliance. In the notice, the OSA found that the Bagley Housing and Redevelopment Authority (HRA) allowed the Clearwater County Treasurer to pay \$34,981.58 more tax increment from Housing District 1 to the developer than authorized in the TIF plan. The TIF plan provided that up to 75 percent of the tax increment from Housing District 1 would be paid to the developer under an interest reduction program. The county treasurer had been paying 100 percent of the tax increment to the developer.³⁶ Tax increment may be spent only as authorized in the TIF plan.³⁷ The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$34,981.58 of tax increment that the Bagley HRA improperly allowed the county treasurer to pay to the developer.³⁸

The city's response argued that the TIF plan did not limit the payments to the developer to 75 percent of the tax increment and that the Bagley HRA did not improperly spend tax increment from Housing District 1 because it did not receive the tax increment generated by that TIF district.

On December 30, 1999, the OSA sent the city its final notice of noncompliance. The OSA reiterated its finding that the Bagley HRA allowed the Clearwater County Treasurer to pay \$34,981.58 more tax increment from Housing District 1 to the developer than authorized in the TIF plan. The OSA reviewed the TIF plan and again concluded that it limited the payments to the developer to 75 percent of the tax increment. The OSA disagreed with the city's assertion that the HRA was not responsible for the expenditures of Housing District 1's tax increment. The HRA created Housing District 1. Under the TIF Act, it was the HRA's responsibility to ensure that tax increment from the TIF district it created was spent in accordance with the law.

³⁶ When the OSA began investigating this matter, officials of the city and the HRA were not aware that the county treasurer was paying tax increment from Housing District 1 directly to the developer. These officials told the OSA they believed that the City of Mora was responsible for administering Housing District 1, even though this TIF district is located in Bagley.

³⁷ Minn. Stat. § 469.176, subd. 4 (1998).

³⁸ See Minn. Stat. § 469.1771, subd. 3 (1998).

The OSA referred this matter to the Clearwater County Attorney by letter dated January 4, 2000. Copies of the OSA's notices of noncompliance and the city's response regarding this matter are included in Appendix D.

2. City of Cambridge

In the December 31, 1998, notice of noncompliance, the OSA made a number of findings that the City of Cambridge had spent tax increment on categories of costs or made transfers of tax increment not authorized in the TIF plans for the relevant TIF districts. For examples of such findings, please review findings 12, 14, 15, 24, and 42 in the OSA's initial and final notices of noncompliance and the city's responses to those findings, copies of which are included in Appendix B.

C. ADMINISTRATIVE EXPENSES IN EXCESS OF STATUTORY LIMIT

City of Roseville

On July 8, 1999, the OSA sent the City of Roseville a notice of noncompliance. In the notice, the OSA found that the city spent \$398,691 more tax increment from TIF District 10 on administrative expenses than permitted by statute. For TIF districts with certification request dates before August 1, 1979, or after June 30, 1982, the amount of tax increment that may be spent on administrative expenses is limited to ten percent of the total estimated tax increment expenditures authorized in the TIF plan or ten percent of the total tax increment expenditures for the project, whichever is less.³⁹ The city reported that the TIF plan for TIF District 10 authorized total estimated tax increment expenditures of \$21,857,569. Ten percent of this amount is \$2,185,757. The city reported that it spent \$2,584,448 of TIF District 10's tax increment on administrative expenses through December 31, 1997. Therefore, the city spent \$398,691 (\$2,584,448-\$2,185,757) more tax of TIF District 10's tax increment on administrative expenses than permitted by statute.⁴⁰ The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$398,691 of tax increment spent on administrative expenses in excess of the statutory limit.⁴¹

³⁹ Minn. Stat. § 469.176, subd. 3(a) (1998). The certification request date for TIF District 10 was November 3, 1988.

⁴⁰ The total tax increment expenditures for the project could not be determined at the time the OSA issued the notice of noncompliance. If ten percent of the tax increment expenditures for the project ends up being *less* than ten percent of the total tax increment expenditures authorized in the TIF plan, then the limit will be less than \$2,185,757, and the city will have exceeded the limit by more than \$398,691.

⁴¹ See Minn. Stat. § 469.1771, subd. 3 (1998).

In its response, the city did not dispute that the amount of TIF District 10's tax increment that it was permitted to spend on tax increment was limited to \$2,185,757. Instead, the city argued that its expenditures for administrative expenses were proper because they were made with non-tax increment. The city stated that it paid the \$2,584,448 of administrative expenses from the fund for its TIF districts, but that the city had deposited sufficient non-tax increment revenue in this fund to pay these expenditures.

On December 29, 1999, the OSA sent the city its final notice of noncompliance. The OSA reiterated its finding that the city spent \$398,691 more tax increment from TIF District 10 on administrative expenses than permitted by statute. The OSA noted that the city was required to have an accounting system that keeps receipts and expenditures of tax increment from each of its TIF districts separate from the receipts and expenditures of all other sources of funds, including tax increment from other TIF districts.⁴² The city's response did not provide any documentation to demonstrate that the administrative expenses were paid with non-tax increment rather than tax increment. Therefore, the OSA could not verify that these expenditures were made in compliance with the TIF Act.

The OSA referred this matter to the Ramsey County Attorney by letter dated January 4, 2000. Copies of the OSA's notices of noncompliance and the city's response regarding this matter are included in Appendix E.

D. TAX INCREMENT RECEIVED AFTER MAXIMUM DURATION LIMIT

1. City of Faribault

In the May 1, 1998, initial notice of noncompliance, the OSA found that the City of Faribault received \$9,710.60 of tax increment from Development District 23 (Industrial), an economic development district, after the statutory maximum duration limit for that TIF district.⁴³ The city responded by paying \$9,710.60 to the Rice County Auditor. In the November 10, 1999, final notice of noncompliance, the OSA concluded that the payment to the county auditor resolved this finding.

The OSA referred other findings of noncompliance in this matter to the Rice County Attorney by letter dated November 19, 1999. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix A.

⁴² Minn. Stat. § 469.177, subd. 5 (1998).

⁴³ *See* Minn. Stat. § 273.75, subd. 1 (1982). The city received \$17,641.72 of tax increment from this TIF district after the statutory maximum duration limit, but the OSA determined that \$7,931.12 of this amount was tax increment from delinquent property taxes, which the city was entitled to receive. *See* Minn. Stat. § 469.176, subd. 1f (1998).

2. City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge improperly received \$37,611.91 of tax increment from Elderly Housing District 1 after the maximum duration limit in the TIF plan. The TIF plan for this district, as adopted in 1980, limited the duration of this district to a date 25 years after the receipt of the first tax increment or until all tax increment bonds to finance the project had been paid or discharged. The only bonds for the project were fully paid in 1995. Therefore, this TIF district should have been decertified when the final payment on the bonds was made in 1995. The OSA informed the city that the statute which requires a TIF authority to make a payment to the county auditor if the TIF authority receives tax increment it should not have received does not apply to the \$37,611.91 of improperly received tax increment, because the city received the tax increment as a result of the failure to decertify the TIF district at the end of the duration limit specified in the TIF plan.⁴⁴

The city responded that it is not clear that the duration of the TIF district had expired because the city retained the authority to modify the TIF plan and issue additional bonds.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly received \$37,611.91 of tax increment from Elderly Housing District 1 after the maximum duration limit in the TIF plan. The OSA agreed that the city could have modified its TIF plan, prior to the final payment on the TIF bonds issued for the project, either to revise the duration provided in the TIF plan or to authorize additional TIF bonds. The city, however, did not take action to do so. Therefore, the TIF-plan maximum duration limit remained the date of the last payment on the bonds in 1995.

In the December 31, 1998, initial notice of noncompliance, the OSA also found that the city improperly received \$9,384.72 of tax increment from Family Housing District 1 after the maximum duration limit in the TIF plan. The OSA's analysis and the city's response were the same as for the finding regarding Elderly Housing District 1 discussed above. In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly received tax increment from Family Housing District 1 after the maximum duration limit in the TIF plan.

In addition, in the December 31, 1998, initial notice of noncompliance, the OSA found that the city improperly received \$98,263.31 of tax increment from Economic Development District 1 (Kroy Industries) after the statutory maximum duration limit.⁴⁵ The OSA noted that the statute which requires a TIF authority to make a payment to the county auditor applies to the \$98,263.31 of improperly received tax increment, because the city received the tax increment as a result of the failure to decertify the TIF district when the statutory maximum duration limit was reached.⁴⁶

⁴⁴ See Minn. Stat. § 469.1771, subd. 2 (1998).

⁴⁵ See Minn. Stat. § 273.75, subd. 1 (1980).

⁴⁶ See Minn. Stat. § 469.1771, subd. 2 (1998).

In its response, the city did not dispute that the city improperly received this tax increment after the statutory maximum duration limit. Instead, the city disputed the OSA's conclusion that the violation payment statute applies to the tax increment that the city improperly received. This statute provides that no payment is required if the tax increment was improperly received as the result of "a failure to decertify a district at the end of the duration limit specified in the tax increment financing plan." Minn. Stat. § 469.1771, subd. 2 (1998).

In the December 30, 1999, final notice of noncompliance, the OSA reiterated that the city improperly received \$98,263.31 of tax increment from Economic Development District 1 (Kroy Industries) after the statutory maximum duration limit and that Minn. Stat. § 469.1771, subd. 2 applies to this improperly received tax increment. The OSA found that the city improperly received the tax increment after the TIF district should have been decertified at the end of the statutory maximum duration limit, not that the city received the tax increment after the TIF district should have been decertified at the end of the duration limit specified in the TIF plan.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

E. IMPROPER WAIVING OF TAX INCREMENT

City of Faribault

In the May 1, 1998, initial notice of noncompliance, the OSA found that the City of Faribault improperly included in the TIF plan for Development District 7 (Met-Con), an economic development district, a provision which stated that the city waived the receipt of any tax increment generated in 1998. The TIF district did not meet the statutory requirements for delaying the first receipt of tax increment from this TIF district, because it is an economic development district.⁴⁷

The city's response argued that the city should have the right to waive receipt of tax increment because the TIF Act does not prohibit the city from doing so. The response stated that if the city were not allowed to waive the first year's tax increment, the city might receive only a small amount of increment in 1998 and *eight* full years of increment during 1999-2006. It is the OSA's position that when tax increment is first generated in an economic development district, the county must distribute the tax increment to the TIF authority and the duration of the TIF district must start. Under the OSA's interpretation of the statutory maximum duration limit, the city would be entitled to receive any small amount of increment in 1998 plus *nine* full years of increment in 1999-2007.

⁴⁷ See Minn. Stat. § 469.175, subd. 1(b) (1998). This statute, which provides a mechanism for delaying the first receipt of tax increment, applies only to redevelopment districts, housing districts, and hazardous substance subdistricts.

In the November 10, 1999, final notice of noncompliance, the OSA concluded that this finding had been resolved. The Rice County Auditor confirmed that no tax increment was generated by this TIF district in 1998, which rendered this finding moot. According to the Rice County Auditor, this TIF district will first generate increment, and the city will first receive it, in 1999.

The OSA referred other findings of noncompliance in this matter to the Rice County Attorney by letter dated November 19, 1999. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix A.

F. INADEQUATELY DOCUMENTED EXPENDITURES

1. City of Faribault

In the May 1, 1998, initial notice of noncompliance, the OSA found that the City of Faribault improperly spent \$26,692 of tax increment from Housing District 1. OSA TIF audit staff found trial balance entries for transfers from Housing District 1 to the General Operating Fund and the Community Development Fund totaling \$26,692 during calendar year 1995, which were noted as being for administrative expenses, but this was the only documentation available. According to the city's former finance director, the city estimated and paid Housing District 1's administrative expenses in the district's last year, calendar year 1995. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$26,692 of inadequately documented expenditures.⁴⁸

After submitting its response, the city filed its 1997 TIF Authority Report for Housing District 1, which indicated that the city spent at total of \$107,425, not \$26,692, of Housing District 1's tax increment on administrative expenses through December 31, 1997. The information in this report contradicted the information in the city's earlier reports and the information contained in its response to the initial notice of noncompliance.

In the November 10, 1999, final notice of noncompliance, the OSA found that the city improperly spent or transferred \$107,425 from Housing District 1 to reimburse the city for paid administrative expenses because the city lacked adequate documentation to show it actually incurred this amount of administrative expenses and because the TIF plan did not authorize the city to spend any amount of tax increment on administrative expenses. The city's response and supplemental information did not include adequate documentation, such as copies of invoices, to support all of these claimed administrative expenses.

The OSA's audit staff also found that the city exceeded the statutory limitation on administrative expenses applicable to this TIF district. TIF authorities are limited in the amount of tax increment they may spend

⁴⁸ See Minn. Stat. § 469.1771, subd. 3 (1998).

on administrative expenses.⁴⁹ According to the 1997 TIF Authority Report for Housing District 1, the city was authorized to spend \$385,500 of tax increment from Housing District 1. Ten percent of that amount is \$38,550. The 1997 TIF Authority Report also indicated that the city spent \$107,425 of tax increment from Housing District 1 on administrative expenses through December 31, 1997. Therefore, as of December 31, 1997, the city spent \$68,875 (\$107,425–\$38,550) more of Housing District 1’s tax increment on administrative expenses than permitted by statute.⁵⁰

The OSA referred this matter to the Rice County Attorney by letter dated November 19, 1999. Copies of the OSA’s notices of noncompliance and the city’s responses regarding this matter are included in Appendix A.

2. City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA made a number of findings that the City of Cambridge had spent tax increment improperly because there was not adequate documentation to allow the OSA to verify that the expenditures were made in compliance with the TIF Act. For examples of such findings, please review findings 6, 7, 8, 37, and 43 in the OSA’s initial and final notices of noncompliance and the city’s responses to those findings, copies of which are included in Appendix B.

G. COSTS NOT ELIGIBLE FOR PAYMENT WITH TAX INCREMENT

1. City of Faribault

In the May 1, 1998, initial notice of noncompliance, the OSA found that the City of Faribault improperly spent \$2,000 of tax increment from Development District 1 (Airtech) on lobbying costs, because these costs did not qualify as administrative expenses eligible for payment or reimbursement with tax increment.

⁴⁹ See Minn. Stat. § 469.176, subd. 3(a) (1998). According to the 1997 Municipality Report for Housing District 1, the certification request date for Housing District 1 was December 11, 1985. Therefore, the limitation on administrative expenses in Minn. Stat. § 469.176, subd. 3(a) applies to Housing District 1.

⁵⁰ The limitation on administrative expenses has two parts. The limit is 1) ten percent of the total tax increment expenditures authorized in the TIF plan or 2) ten percent of the tax increment expenditures for the project, whichever is less. The total tax increment expenditures for the project cannot be determined at this time. If, however, ten percent of the tax increment expenditures for the project ends up being *less* than ten percent of the total tax increment expenditures authorized in the TIF plan, then the limit will be less than \$38,550 and the city will have exceeded the limit by more than \$68,875.

The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$2,000 spent on costs that did not qualify as administrative expenses.⁵¹

Despite the objections raised in the city's response, the city indicated it would reimburse Development District 1 for these expenses on or before August 1, 1998, with funds transferred from the Community Development Department's General Fund. The city later confirmed that it transferred \$2,000 from the Community Development Department's General Fund to Development District 1 to make this reimbursement.

In the November 10, 1999, notice of noncompliance, the OSA reiterated its finding that the city improperly spent \$2,000 of tax increment from Development District 1 on lobbying costs. If a TIF authority improperly pays or transfers tax increment, it is subject to the payment provision under Minn. Stat. § 469.1771, subd. 3. Therefore, the OSA concluded that returning money to the TIF district did not resolve this finding. The OSA also noted that local governments often engage in lobbying efforts that focus on a variety of topics relevant to their constituents. While, in general, lobbying is a permissible activity, the OSA found no provision in the TIF Act authorizing the expenditure of tax increment to fund TIF-related lobbying efforts.

The OSA referred this matter to the Rice County Attorney by letter dated November 19, 1999. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix A.

2. City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA made a number of findings that the City of Cambridge spent tax increment on costs that are not eligible for payment or reimbursement with tax increment, because the costs paid with these expenditures did not qualify as administrative expenses eligible for payment or reimbursement with tax increment.

First, the OSA found that the city improperly spent \$957.09 of tax increment from Economic Development District 2-2 (Imperial Motel, Nordberg, Dubanoski) on costs of an improvement bond issue and on lobbying costs, because these costs did not qualify as administrative expenses eligible for payment or reimbursement with tax increment. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act does not apply to the \$957.09 spent on costs that did not qualify as administrative expenses, because these expenditures were made on or before December 31, 1990.⁵²

⁵¹ See Minn. Stat. § 469.1771, subd. 3 (1998).

⁵² The 1990 act that created the violations statute within the TIF Act, Minn. Stat. § 469.1771, provided that the statute applies only to violations occurring after December 31, 1990. Laws 1990, ch. 604, art. 7, sec. 25 and 31(a).

The city responded that the improvement bond issue was in aid of the project, and therefore costs of the bond issue were administrative expenses. The city also responded that the lobbying costs were related to issues that affected the project, and therefore these costs were administrative expenses.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly spent \$957.09 of tax increment from Economic Development District 2-2 on costs of an improvement bond issue and on lobbying costs. The OSA noted that none of the budgets in the TIF plans for the TIF districts in the project authorized the city to spend tax increment on debt service on these improvement bonds. Therefore, the OSA concluded that it could not verify that the costs associated with issuing these improvement bonds were administrative expenses of this TIF district or of the TIF-financed portion of the project. In response to the city's position that lobbying costs were incurred in support of issues related to the project, the OSA noted that it recognized that local governments often engage in lobbying efforts that focus on a variety of topics relevant to their constituents. While, in general, lobbying is a permissible activity, the OSA found no provision in the TIF Act authorizing the expenditure of tax increment to fund TIF-related lobbying efforts.

Second, the OSA found that the city improperly spent \$933.10 of tax increment from Economic Development District 3-1 (Mill Ridge) on wastewater treatment facility operations, unspecified meetings, and memberships for building officials, because these costs did not qualify as administrative expenses eligible for payment or reimbursement with tax increment. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$933.10 spent on costs that did not qualify as administrative expenses.⁵³

The city responded that the law provides that administrative expenses are "all expenditures of an authority" and that the costs need only be related to the "project." The project that the city referred to is the project area (the underlying development district) for many of its TIF districts, which currently includes the entire City of Cambridge.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly spent \$933.10 of tax increment from Economic Development District 3-1 on wastewater treatment facility operations, unspecified meetings, and memberships for building officials. The OSA noted that these costs appeared to be normal and routine operating costs of the city. The OSA found no statutory authority which would authorize payment of normal and routine operating costs of the city as administrative expenses of the project.

Third, the OSA found that the city improperly spent \$498 of tax increment from Economic Development District 6-1 (SE Cambridge Industrial Area) on costs related to a Juvenile Officers Conference, because these costs did not qualify as administrative expenses eligible for payment or reimbursement with tax increment. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$498 spent on costs that did not qualify as administrative

⁵³ See Minn. Stat. § 469.1771, subd. 3 (1998).

expenses.⁵⁴ The city responded that this TIF district had sufficient non-tax increment revenues available to pay these expenditures.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly spent \$498 of tax increment from Economic Development District 6-1 on costs related to a Juvenile Officers Conference. OSA audit staff was unable to find any documentation to demonstrate that the monies spent from the fund for Economic Development District 6-1 on costs of the Juvenile Officers Conference were non-tax increment rather than tax increment. The city's response provided no such documentation. Therefore, the OSA could not verify that these expenditures were made in compliance with the TIF Act.⁵⁵

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

H. PAYMENT OF TAX INCREMENT TO PROPERTY OWNERS NOT AUTHORIZED IN TIF PLAN

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge spent \$67,500 of tax increment from Economic Development District 2-2 (Imperial Motel, Nordberg, Dubanoski) on something other than land acquisition costs authorized in the TIF plan. The TIF plan authorized the city to spend tax increment to acquire certain parcels of property and then to sell each of the parcels to developers for \$1. The city did not acquire the parcels, but instead paid the \$67,500 to the owners of the parcels, who also were the developers identified in the TIF plan. These owners acquired the parcels as much as eight years before the creation of the TIF district. Tax increment may be spent only as authorized in the TIF plan.⁵⁶ The OSA determined that the TIF plan did not authorize the city to pay the \$67,500 to the property owners unless it did so to acquire the parcels, and the city never acquired title to the parcels. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$67,500 of tax increment that the city improperly paid to the developer.⁵⁷

⁵⁴ See Minn. Stat. § 469.1771, subd. 3 (1998).

⁵⁵ In addition, the OSA expressed concern that the city was accounting for routine and normal operating costs in a capital project fund that should be used only to account for expenditures related to specific development projects.

⁵⁶ Minn. Stat. § 469.176, subd. 4 (1998).

⁵⁷ See Minn. Stat. § 469.1771, subd. 3 (1998).

The city agreed with the OSA that the TIF plan authorized expenditure of tax increment to finance acquisition of the parcels. However, the city stated that rather than taking title to the property and risking liability for removal of hazardous waste, the city chose to reimburse the property owners for property they owned prior to the creation of the TIF district. In addition, the city responded that nothing in the statute prohibits reimbursement for land previously acquired by a developer as long as the “but for” test is met.

In the December 31, 1999, final notice of noncompliance, the OSA reiterated its finding that the city spent \$67,500 of tax increment from Economic Development District 2-2 on something other than land acquisition costs authorized in the TIF plan. The OSA found no provision in the TIF Act authorizing a TIF authority to spend tax increment on costs not authorized in the TIF plan.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA’s notices of noncompliance and the city’s responses regarding this matter are included in Appendix B.

I. EXPENDITURE OF TAX INCREMENT FROM A HOUSING DISTRICT OUTSIDE VALID HOUSING PROJECT AREA

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge improperly transferred \$19,000 of tax increment from Housing District 5-1 to Economic Development District 2-1 (Sias) and spent \$30,590.60 of Housing District 5-1’s tax increment on activities outside the valid housing project area for Housing District 5-1. Tax increment from a housing district with a certification request date after May 1, 1998, may be spent only on a housing project as defined in Minn. Stat. § 469.174, subd. 11.⁵⁸ According to the version of Minn. Stat. § 469.174, subd. 11 that applies to Housing District 5-1, the project area that contains a housing district is not a valid project—

if the fair market value of the improvements which are constructed for commercial uses or for uses other than low and moderate income housing consists of more than one-third of the total fair market value of the planned improvements in the development plan or agreement.”

Minn. Stat. § 469.174, subd. 11 (1988).⁵⁹ The city attempted to increase the size of the project area that contained Housing District 5-1 to contain the entire city, including Economic Development District 2-1.

⁵⁸ Minn. Stat. § 469.176, subd. 4d (1998). The certification request date for Housing District 5-1 was October 11, 1998.

⁵⁹ This statute was amended in 1990 to change the ratio from one-third to 20 percent. This amendment applies to housing districts with certification request dates after April 30, 1990. *See* Laws 1990, ch. 604, art. 7, sec. 7 and 31(a).

The OSA could not find documentation to verify that the entire city met the requirements in Minn. Stat. § 469.174, subd. 11 for a valid housing project. Therefore, the OSA found that when the city transferred Housing District 5-1's tax increment to Economic Development District 2-1 and spent it on activities outside Housing District 5-1, it did not comply with the requirement to spend Housing District 5-1's tax increment only on a housing project as defined in Minn. Stat. § 469.174, subd. 11. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$19,000 of transferred tax increment and the \$30,590.60 of tax increment spent on activities outside the TIF district.⁶⁰

The city responded that the \$19,000 transfer to Economic Development District 2-1 was made with Homestead and Agricultural Credit Aid (HACA) rather than tax increment and, therefore, the transfer did not violate the TIF Act. The city responded that it did not violate the TIF Act when it spent \$30,590.60 of Housing District 5-1's tax increment because the words "housing project" in Minn. Stat. § 469.176, subd. 4d and "project" in the second sentence of Minn. Stat. § 469.174, subd. 11 mean a group of housing facilities and related public improvements, not the project area that contains the housing district.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its findings that the city improperly transferred \$19,000 of tax increment from Housing District 5-1 to Economic Development District 2-1 and spent \$30,590.60 of Housing District 5-1's tax increment on activities outside the valid housing project area for Housing District 5-1. The city's response did not provide documentation that would allow the OSA to verify that the \$19,000 transfer was made with HACA rather than tax increment. In addition, the OSA found no statutory support for the city's position on the meaning of the word "project."

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

J. LACK OF EVIDENCE THAT BUILDING WAS STRUCTURALLY SUBSTANDARD

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge did not comply with the statute requiring documentation to support the city's finding that a parcel containing a movie theater qualified for inclusion in Redevelopment District 6-2 (G.T.I. Remodeled Theatre).⁶¹ The city was required to "set forth in writing the reasons and supporting facts for each determination" that the city was required to make in the process of approving the TIF plan, including the determination that the

⁶⁰ See Minn. Stat. § 469.1771, subd. 3 (1998).

⁶¹ Redevelopment District 6-2 consisted only of the parcel containing the movie theater.

parcel containing the theater building qualified for inclusion in a redevelopment district.⁶² Absent such “reasons and supporting facts,” the parcel did not qualify for inclusion in the TIF district, in which event the city improperly received \$35,975 from Redevelopment District 6-2. The OSA noted that the statute which requires a TIF authority to make a payment to the county auditor if the TIF authority receives tax increment it should not have received applies to the \$35,975 of tax increment that the city received from the parcel.⁶³

The city conceded it was required to include information showing that the theater building was structurally substandard in its “reasons and supporting facts” for its finding that the parcel qualified for inclusion.⁶⁴ The city agreed with the OSA that the only “reasons and supporting facts” for the city’s finding that the parcel qualified for inclusion in a redevelopment district was a single sentence in a letter regarding the structural integrity of the theater building: “There are several large cracks in the existing concrete block exterior walls that rises (sic) my concern as to their structural intrugrity (sic).” Letter from Robert F. Vanney, AIA, President of Vanney Associates, to Mr. Dick Guetschoff, Cambridge Cinema III, dated May 17, 1991. The city’s response characterized this statement as a determination that the building lacked structural integrity.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the parcel containing the movie theater did not qualify for inclusion in a redevelopment district because the city lacked the statutorily required documentation to support its finding that the building was structurally substandard. The OSA concluded that the statement in Mr. Vanney’s letter was not sufficient to show that the theater building met the statutory requirements for being structurally substandard.

⁶² Minn. Stat. § 469.175, subd. 3 (1990).

⁶³ *See* Minn. Stat. § 469.1771, subd. 2 (1998). The city received the \$35,975 of tax increment from this district on or before December 31, 1996. The OSA informed the city that any tax increment received by the city from this TIF district after December 31, 1996, also is subject to the provisions of Minn. Stat. § 469.1771, subd. 2. Therefore, the OSA recommended that the city request decertification of this TIF district to avoid ongoing violations of the TIF Act.

⁶⁴ *See* Minn. Stat. § 469.174, subd. 10(b) (1990). The city’s response noted that Mr. Vanney’s letter did not contain any of the following: 1) an opinion that the theater building did not meet the building code applicable to new buildings; 2) an estimate of the cost of bringing the building up to code, so the renovation cost could be compared to the cost of constructing a new building; 3) any information about the size, type, or age of the building that would be evidence that the building did not meet code and would be expensive to bring up to code; 4) any information about the average cost of plumbing, electrical, or structural repairs required to bring a building up to code. Such information would have been sufficient to meet this aspect of the required “reasons and supporting facts” for the city’s finding that the parcel qualified for inclusion.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

K. NON-CONTIGUOUS AREAS DID NOT QUALIFY FOR INCLUSION IN RENEWAL AND RENOVATION DISTRICT

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that parcels 15-047-0110, 03-068-0030, and 03-027-1400 did not qualify for inclusion in the City of Cambridge's Renewal and Renovation District 6-4. The OSA determined that these parcels did not meet the requirements of Minn. Stat. § 469.174, subd. 10a, based on plat maps and the city's own analysis in the TIF plan. The OSA noted that the statute which requires a TIF authority to make a payment to the county auditor if the TIF authority receives tax increment it should not have received applies to all tax increment the city has received to date from this renewal and renovation district.⁶⁵

The city indicated in its initial response that the TIF plan failed to include required information for parcel 15-047-0110 and included incorrect information for parcels 03-068-0030, and 03-027-1400. The city added that records on file with the city at the time of TIF-plan approval provided the missing information or corrected the incorrect information in the TIF plan. Therefore, the city believed that there was adequate information to support the required findings that allow for the parcels' inclusion in this TIF district. However, the city's initial response did not provide the OSA with copies of the purported documentation. The OSA wrote to the city and requested that the city provide copies of the documentation that supported the city's statement that these three parcels qualified for inclusion in a renewal and renovation district. The city did not provide this documentation.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that parcels 15-047-0110, 03-068-0030, and 03-027-1400 did not qualify for inclusion in Renewal and Renovation District 6-4. Absent such documentation, the OSA could not verify that the noncontiguous areas comprising these parcels met the requirements of Minn. Stat. § 469.174, subd. 10a.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

⁶⁵ See Minn. Stat. § 469.1771, subd. 2 (1998). The city received the \$35,975 of tax increment from this TIF district on or before December 31, 1996. The OSA informed the city that any tax increment received by the city from this TIF district after December 31, 1996, also is subject to the provisions of Minn. Stat. § 469.1771, subd. 2. Therefore, the OSA recommended that the city request decertification of this TIF district to avoid ongoing violations of the TIF Act.

L. IMPROPER LOCAL TAX RATE

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the “original local tax rate” included in a 1996 TIF-plan amendment, which added twelve parcels to the City of Cambridge’s Renewal and Renovation District 6-4 (McDonalds), was not in compliance with Minn. Stat. § 469.177, subd. 1a. When the city modified the TIF plan in 1996 to enlarge this TIF district geographically, the city included in the modified TIF plan a provision that applied the 1996/1997 local tax rate as the “original local tax rate” for the added parcels, instead of applying the “original local tax rate” certified when the net tax capacity of the original TIF district was certified.

The city responded that the “original local tax rate,” in cases of added parcels, is the rate in effect at the time of the addition of any parcels to the TIF district and not the rate certified for the original TIF district. The city argued that “the OSA’s reading is inconsistent with the general premise that additions to a district are certified and treated in most respects like new districts.” The city cited Minn. Stat. § 469.179, subd. 3(c)(2), which the city paraphrased as stating that “changes in the law apply ‘only to the area of the district added by tax increment financing plan amendments for which certification is requested after the specified date.’”

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the “original local tax rate” included in the 1996 amended TIF plan for the twelve parcels added by the amendment is not in compliance with the TIF Act. The OSA concluded that this situation does not involve determining whether the pre-amendment or post-amendment version of a statute applies to parcels added to a TIF district. The language of Minn. Stat. § 469.177, subd. 1a has not changed since it was enacted in 1988, except to substitute “net tax capacity” for “assessed value” and “local tax rate” for “mill rate.”⁶⁶ The city requested certification of the original TIF district on June, 26, 1993, and requested certification of the geographic enlargement on November 12, 1996, both of which occurred after the effective date of Minn. Stat. § 469.177, subd. 1a.⁶⁷ Therefore, Minn. Stat. § 469.179, subd. 3(c)(2) does not apply to this situation.

The OSA noted that the city’s interpretation of Minn. Stat. § 469.177, subd. 1a was contrary to the Department of Revenue’s longstanding directive. A Department of Revenue TIF property tax procedures

⁶⁶ Compare Minn. Stat. § 469.177, subd. 1a (1988) and Minn. Stat. § 469.177, 1a (1992). See also Laws 1988, ch. 719, art. 12, sec. 20 and Laws 1 Sp. 1989, ch. 2, art. 2, sec. 11 (instructing the Revisor of Statutes to substitute “net tax capacity” for “assessed value” and “local tax rate” for “mill rate” throughout the statutes).

⁶⁷ See Laws 1988, ch. 719, art. 12, sec. 20 and 30.

manual, dated July 1, 1992, clearly states that the addition of parcels to a TIF district does not change the reference year for the “original local tax rate.”⁶⁸

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. The OSA also forwarded the information in this finding to the Isanti County Auditor. Copies of the OSA’s notices of noncompliance and the city’s responses regarding this matter are included in Appendix B.

M. INCOMPLETE MAP ACCOMPANYING PUBLIC HEARING NOTICE

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that parcel 15-072-0080 (Al Anlauf site) did not qualify for inclusion in the City of Cambridge’s Renewal and Renovation District 6-4 (McDonalds) due to insufficient public notice. Specifically, in the notice regarding the public hearing on approval of a modified TIF plan for this TIF district, the city failed to include this parcel in the map of the area of the TIF district from which increments may be collected. The OSA noted that the statute which requires a TIF authority to make a payment to the county auditor if the TIF authority receives tax increment it should not have received applies to all tax increment the city has received to date from this parcel.⁶⁹

In its response, the city conceded that the published map did not include the parcel. However, the city stated that the parcel was named in the notice. Furthermore, the city stated that the deficiency cited by the OSA does not rise to the level that would justify invalidation of the October 16, 1996, modification of the TIF plan for Renewal and Renovation District 6-4.

In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that parcel 15-072-0080 (Al Anlauf site) did not qualify for inclusion in Renewal and Renovation District 6-4 due to insufficient public notice. The statute relevant to this finding mandates that the “notice *must* include a map of the area of the district from which increments may be collected and, if the project area includes additional area, a map of the project area in which the increments may be expended.” Minn. Stat. § 469.175, subd. 3 (1990) (emphasis added). As mentioned above, the city conceded that it did not fully comply with Minn. Stat. § 469.175, subd. 3, because the city failed to include the parcel in the published map. The OSA concluded that the issues of whether the city’s public hearing notice substantially complied with the requirements of Minn. Stat. § 469.175, subd. 3 and whether the doctrine of substantial compliance applies

⁶⁸ The city adopted the TIF plan for this TIF district on July 26, 1993, and adopted the relevant modification of the TIF district on October 16, 1996. The Department of Revenue’s manual was available to the city for more than four years prior to the October 16, 1996, modification of the TIF plan.

⁶⁹ See Minn. Stat. § 469.1771, subd. 2 (1998). The OSA informed the city that any tax increment received by the city from this parcel after December 31, 1996, also is subject to the provisions of Minn. Stat. § 469.1771, subd. 2.

to this statutory notice requirement were determinations appropriate for the county attorney and the courts. Accordingly, the OSA referred this finding to the county attorney for review.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

N. UNAUTHORIZED EXPENDITURES OF TAX INCREMENT FROM A SOILS CONDITION DISTRICT

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge improperly spent \$57,366 of tax increment from Soils Condition District 6-5 (Medical Center/Community College) to reimburse a developer for site improvement costs and costs of installing public utilities. Of the \$400,423 of documented costs incurred by the developer, the OSA only was able to verify that a \$201,000 charge for excavation and backfill met the statutory restrictions on spending tax increment from this soils condition district. Of the remaining \$199,423 of documented developer costs, the OSA determined that the costs did not meet the statutory restrictions on spending tax increment from this soils condition district or OSA audit staff was unable to find documentation sufficient to verify that the costs met the statutory restrictions on spending tax increment from a soils condition district. The city reimbursed the developer \$258,366, which exceeded the amount of documented, TIF-eligible costs by \$57,366. The OSA noted that the statutory requirement to make a payment to the county auditor for violations of the TIF Act applies to the \$57,366 of tax increment that the city improperly paid to the developer.⁷⁰

In its response, the city stated that the "necessary soil removal and filling could not be done without relocating the existing utilities." The documentation provided by the city was insufficient to allow the OSA to verify This statement. In the December 30, 1999, final notice of noncompliance, the OSA reiterated its finding that the city improperly spent \$57,366 of tax increment from this TIF district on site improvement costs and costs of installation of public utilities.

The city's response did not address the disallowed costs that were not costs of rerouting utilities, which included \$47,000 for sewer and water accessibility charges, \$45,832.96 for conversion of power lines from above ground to underground,⁷¹ and \$117 for removal of an elm tree and an unknown charge of \$10.50. In the initial notice of noncompliance, the OSA determined that these costs did not meet the statutory restrictions on spending tax increment from this soils condition district, because they were not

⁷⁰ See Minn. Stat. § 469.1771, subd. 3 (1998).

⁷¹ According to the map provided by the city, the above-ground power lines were buried directly below where they had been suspended overhead, which was outside the area marked on the map as being the area requiring soils correction.

costs of correcting unusual terrain or soils deficiencies or additional costs of installing public improvements directly caused by the deficiencies.⁷² The city's response did not appear to dispute this determination.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

O. FAILURE TO INFORM COUNTY AUDITOR OF BUILDING PERMIT ISSUED BEFORE APPROVAL OF TIF PLAN

City of Cambridge

In the December 31, 1998, initial notice of noncompliance, the OSA found that the City of Cambridge failed to provide the county auditor with a list of the building permits that had been issued for parcels in Soils Condition District 6-5 (Medical Center/Community College) during the 18 months immediately preceding approval of the TIF plan for this district on November 15, 1993. The OSA determined that the city issued the building permits for the Cambridge Medical Center development, which was located on parcels within this TIF district, before November 15, 1993. The city did not inform the county auditor that these building permits had been issued before the city approved the TIF plan. This failure resulted in the county auditor's not adjusting the original net tax capacity of this TIF district by the net tax capacity of each improvement for which a building permit was issued.⁷³

During the on-site inspection of the city's TIF records in November 1997, OSA audit staff found a copy of a letter from an architect's firm to the city which indicated that there were two building permits for the Cambridge Medical Center development, one of which was issued before November 5, 1993. The OSA sent the city a letter requesting copies of the building permits referred to in the letter from the architect's firm. The city sent a letter which confirmed that there were two building permits, but copies of the permits were not enclosed with the letter. Instead, copies of two applications for building permits for the Cambridge Medical Center development were enclosed. The first application, dated August 10, 1993, was for \$1 million for foundation/structure/sitework only for the additions to the existing hospital and clinic. The second application, dated September 22, 1993, was for \$10 million for all work on the Cambridge Medical Center not covered by the earlier application. A notation on the second application, made by city personnel at some later date, indicated that the city received a payment of \$6,531.59 on October 1, 1993, which is consistent with the amount indicated in the architecture firm's letter as the fee paid for the early building permit. A notation on the first application, made by city personnel at some later date, indicated that the city received payment for the final building permit on November 9, 1993, which is consistent with the architecture firm's letter and the city's letter. Based on this information, the OSA made this finding of noncompliance.

⁷² See Minn. Stat. § 469.176, subd. 4b (1992).

⁷³ See Minn. Stat. § 469.177, subd. 4 (1998).

The city responded that it issued no building permits for parcels in Soils Condition District 6-5 before it approved the TIF plan for this district on November 15, 1993. According to the city, the developer of the Cambridge Medical Center submitted an initial building permit application for \$1 million of foundation and site work and a supplementary building permit application for the remainder of the construction. The city stated that it issued only one building permit (number 93115) for the entire development, even though an initial and a supplementary building permit application were filed. The city stated that its customary practice is to assign a number to a building permit at the time it delivers the permit to the applicant, and then to record the permit in a record book. The city's response, however, did not indicate the date on which the city issued the building permit number 93115 to the developer of the Cambridge Medical Center. It appears the city has no record of this date. Instead, the city stated that the application for building permit number 93113 was dated November 24, 1993, the application for permit number 93114 was not dated, and the application for building permit number 93116 was dated December 6, 1993. Based on this information, the city concluded that it must have issued building permit number 93115 after November 24, 1993, the date of the application for building permit number 93113.

In the December 30, 1999, final notice of noncompliance, the OSA found that the city failed to inform the county auditor that it had issued the first building permit for the Cambridge Medical Center development within the 18 months before the city approved the TIF plan for this district on November 15, 1993. The OSA concluded, based on all available documentation, that the city had issued two building permits for this development. The architecture firm's letter indicated that as of November 5, 1993, the initial building permit already had been issued. It appears the initial building permit was issued on or about October 1, 1993, when the city received the payment of \$6,531.59. The OSA found that this documentation, taken as a whole, indicates that the city issued the initial building permit for the Cambridge Medical Center development before the city approved the TIF plan for this district on November 15, 1993.

The OSA referred this matter to the Isanti County Attorney by letter dated January 3, 2000. The OSA also forwarded the information in this finding to the Isanti County Auditor. Copies of the OSA's notices of noncompliance and the city's responses regarding this matter are included in Appendix B.

III. STATUTORY ISSUES

Through municipalities' responses to notices of noncompliance and questions received from city and county officials and employees, the OSA has identified a number of areas where the TIF Act is ambiguous or the OSA's findings of noncompliance have conflicted with practitioners' varying interpretations of the law. This report to the legislative committees with jurisdiction over TIF identifies certain ambiguities and conflicting statutory interpretations in order to facilitate public policy discussion and allow for amendments to clarify the law retroactively or to change the law prospectively.

A. SPENDING TAX INCREMENT IN EXCESS OF LINE-ITEM BUDGET AMOUNTS

A TIF plan must include a line-item budget, because a TIF authority is required to report the line-item budget contained in the TIF plan:

(c) The annual financial report must also include the following items:

* * *

(3) for the reporting period and for the duration of the district, ***the amount budgeted under the tax increment financing plan***, and the actual amount expended for, at least, the following categories: (i) acquisition of land and buildings through condemnation or purchase; (ii) site improvements or preparation costs; (iii) installation of public utilities, parking facilities, streets, roads, sidewalks, or other similar public improvements; (iv) administrative costs, including the allocated cost of the authority; (v) public park facilities, facilities for social, recreational, or conference purposes, or other similar public improvements[.]

Minn. Stat. § 469.175, subd. 6(c)(3) (1998) (emphasis added). This requirement for each district's TIF plan to include a line-item budget for the use of tax increment from the ***TIF district*** (and all public funds to be spent in or on behalf of the district) is in addition to the requirement to include an estimate of the cost of the ***project***.⁷⁴ Tax increment may be spent or transferred out only as authorized in the TIF plan.⁷⁵ If, for example, a TIF-plan budget indicates that the TIF authority will spend \$100,000 of tax increment from the TIF district on site improvements and the TIF authority spends \$125,000 on site improvements, the TIF authority has not spent tax increment as authorized in the TIF plan. It is the OSA's position that such unauthorized spending of tax increment (*i.e.*, spending the additional \$25,000 of tax increment on site improvements) violates the TIF Act.

In responses to notices of noncompliance containing findings on this issue, municipalities have responded that there was no legal obligation for a TIF authority to include a line-item budget in the TIF plan, and therefore a TIF authority does not violate the TIF Act when it spends more tax increment on a line item (*e.g.*, site improvements) than the amount that the TIF plan authorized for that item. Municipalities also have asserted that TIF authorities and municipalities throughout the state believe the TIF Act requires a TIF plan only to include estimates of costs, which TIF authorities may exceed without consequence, provided the ***total actual*** tax increment expenditures do not exceed the ***total estimated*** tax increment expenditures in the TIF plan.

The OSA recommends that this issue be clarified through statutory change.⁷⁶ If the Legislature determines that a TIF authority should be able to spend more tax increment on a category of costs (*e.g.*, site

⁷⁴ See Minn. Stat. § 469.175, subd. 1(a)(5)(i) (1998).

⁷⁵ Minn. Stat. § 469.176, subd. 4 (1998).

⁷⁶ The OSA has discontinued making findings that a TIF authority violates the TIF Act by spending more tax increment on a line item than the TIF plan authorized. The OSA may resume making findings of noncompliance on this issue depending upon what action, if any, the Legislature takes.

improvements) than the amount included in the TIF-plan budget for that category of costs, without first amending the TIF plan to authorize the additional spending, the OSA recommends that the Legislature amend the statute that requires tax increment to be spent in accordance with the TIF plan so that this statute is consistent with the Legislature's intent.

On the other hand, if the Legislature determines that a TIF authority which intends to spend more tax increment on a category of costs than the amount included in the TIF-plan budget must first amend the TIF plan to authorize the additional spending, the OSA recommends that the Legislature specify a procedure for such an amendment. The TIF Act specifies the procedure for approving certain kinds of TIF-plan amendments, but is silent about the procedure for adopting other kinds of amendments, such as an amendment to the amount budgeted for a category of costs.

If the Legislature decides to enact either of these amendments, the OSA recommends that the amendment be effective retroactively and apply to TIF districts with certification request dates after July 31, 1979. The OSA believes that adopting a prospective effective date for either of these amendments would create great controversy regarding the proper interpretation of the law before the effective date.

B. COMMINGLING OF TAX INCREMENT WITH OTHER SOURCES OF FUNDS

A provision in the TIF Act requires a TIF authority to segregate tax increment from each TIF district in a special account on the TIF authority's books and records.⁷⁷ In auditing expenditures of tax increment, the OSA reviews whether a TIF authority has an accounting system that allows it to establish which expenditures were paid with tax increment from a particular TIF district and which were paid with some other source of funds. A TIF authority may spend tax increment only as authorized by the TIF Act and bears the burden of demonstrating it has complied with the law.

The OSA has found that it is common practice for a TIF authority to have a separate capital project fund for each TIF district and to deposit into a TIF district's capital project fund all sources of funds that will be used to pay the publicly financed portion of the costs of the TIF-assisted development. For example, a TIF authority might deposit into the capital project fund for TIF District 1 the tax increment from the TIF district, plus special assessment revenue collected from property in the district, plus a grant from the Department of Trade and Economic Development obtained to assist the TIF-assisted development. In addition, the TIF authority might deposit in the fund the interest earned on the balance in the fund.⁷⁸

The practice of depositing tax increment and non-tax increment revenues into the same fund may or may not violate the requirement to segregate the tax increment from each TIF district in a special account. If

⁷⁷ Minn. Stat. § 469.177, subd. 5 (1998).

⁷⁸ Some interest earned on tax increment balances is tax increment and some is not, depending on the certification request date of the TIF district and when the interest revenue is received. *See* Minn. Stat. § 469.174, subd. 25 (1998); Laws 1997, ch. 231, art. 10, sec. 2 and 25.

the TIF authority records each deposit of money into the fund as a deposit into a revenue account for each specific source of funds (*e.g.*, tax increment, special assessments, grant, interest earnings) and codes each expenditure as being from a particular source of funds within the fund, then the tax increment will be segregated. The TIF authority will be able to demonstrate which expenditures were made with tax increment, which were not, and how much tax increment remains in the fund.

It appears that many TIF authorities record each deposit of money into the fund as a deposit into a revenue account for each specific source of funds, but do not code the expenditures in a like manner. The result of this practice is that the TIF authority cannot demonstrate whether tax increment or some other source of funds was used to make a particular expenditure, and cannot demonstrate how much tax increment remains in the fund. In such a situation, the deposit of non-tax increment revenue in the same fund with tax increment results in the improper commingling of these different sources of funds. Commingling tax increment from a TIF district with other sources of funds, including tax increment from another TIF district, makes it impossible for the OSA to verify that tax increment was spent or transferred in accordance with the TIF Act.

The Legislature may decide it would be good public policy to authorize TIF authorities retroactively to declare how much of their past expenditures were made with tax increment and how much tax increment remains in their funds. For example, the Legislature might enact a law permitting TIF authorities to adopt a resolution dividing the total expenditures from each of its TIF districts into amounts paid with tax increment and amounts paid with non-tax increment. In the resolution, the TIF authority also would declare how much of each TIF district's fund balance was tax increment and how much was non-tax increment. If such an approach were adopted, a TIF authority that had been commingling tax increment with other sources of funds would have a "clean slate" upon adoption of the resolution and would then be responsible for segregating the tax increment from each of its TIF districts going forward.

C. DEFINITION OF "ADMINISTRATIVE EXPENSES"

Under the definition of "administrative expenses," many kinds of costs, such as bond principal payments, loan principal and interest payments, and development and relocation costs incurred outside the TIF district but within the project, appear to be classified as administrative expenses, even though the OSA and all practitioners advising local governments assume that these costs are not administrative expenses.

The OSA recommends that the Legislature amend the definition of "administrative expenses" to clarify these issues. The OSA also recommends that the amendment be effective retroactively and apply to TIF districts with certification request dates before, on, or after August 1, 1979. The OSA believes that adopting a prospective effective date for the amendment would create great controversy regarding the proper interpretation of the law before the effective date.

D. DEFINITIONS OF "HOUSING DISTRICT," "PROJECT," AND "HOUSING PROJECT"

For housing districts with certification request dates after May 1, 1988, the tax increment from these housing districts "must be used solely to finance the costs of *housing projects*, as defined in section

469.174, subdivision 11.” Minn. Stat. § 469.176, subd. 4d (1998) (emphasis added). For purposes of the pooling⁷⁹ restrictions, any expenditure of tax increment from a housing district to finance costs of a “*housing project*, as defined in section 469.174, subdivision 11, is an activity in the district.” Minn. Stat. § 469.1763, subd. 2(b) (1998) (emphasis added).

According to the statutes quoted above, Minn. Stat. § 469.174, subd. 11 contains the definition of “housing project.” Section 469.174, subdivision 11, is the definition of “housing district,” not “housing project.” This definition, however, imposes certain requirements on the “project” area that contains a housing district, and in that sense might be considered to define “housing project”:

“Housing district” means a type of tax increment financing district which consists of a *project*, or a portion of a *project*, intended for occupancy, in part, by persons or families of low and moderate income A *project* does not qualify under this subdivision if the fair market value of the improvements which are constructed for commercial uses or for uses other than low and moderate income housing consists of more than 20 percent of the total fair market value of the planned improvements in the development plan or agreement. The fair market value of the improvements may be determined using the cost of construction, capitalized income, or other appropriate method of estimating market value.

Minn. Stat. § 469.174, subd. 11 (1998) (emphasis added).

It is the OSA’s position that a housing project is an example of a project area, as defined in Minn. Stat. § 469.174, subd. 8. Therefore, tax increment from a housing district may be spent on activities in the project area that contains the housing district only if the project area meets the qualifications for a housing project under Minn. Stat. § 469.174, subd. 11. Furthermore, for purposes of the pooling restrictions, any expenditure of tax increment from a housing district to finance the costs of the project that meets the requirements for Minn. Stat. § 469.174, subd. 11 counts as an expenditure for an activity inside the housing district, even if the activity actually is located outside the housing district.⁸⁰ Some TIF authorities and municipalities, and the attorneys who advise them about TIF issues, disagree with certain aspects of the OSA’s position and have offered a variety of alternative interpretations of these provisions of the TIF Act.

The OSA recommends that the Legislature review the definition of “housing district,” the limitation on the use of tax increment from housing districts, and the limitation on pooling to ensure that these statutes match the Legislature’s intent. If the Legislature decides to enact any amendments to the definition of “housing district” and the limitation on the use of tax increment from housing districts, the OSA recommends that the amendment be effective retroactively and apply to TIF districts with certification request dates after May

⁷⁹ “Pool” or “pooling” are terms used to mean the expenditure of tax increment on costs of activities that occur outside the geographic boundaries of the TIF district that generated the tax increment.

⁸⁰ See Minn. Stat. § 469.1763, subd. 2(b) (1998).

1, 1988. The OSA believes that adopting a prospective effective date for the amendment would create great controversy regarding the proper interpretation of the law before the effective date.

E. DEFINITION OF “INCREMENT”

In 1997, the Legislature enacted a definition of “increment.”⁸¹ The effective date for this definition is extremely complex. Certain aspects of the effective date are difficult for the OSA and users of TIF to understand, and other aspects have resulted in disagreements between the OSA and users of TIF.

First, the definition of “increment” includes “taxes paid by the captured net tax capacity, but excluding any excess taxes, as computed under section 469.177.”⁸² This tax increment sometimes is referred to as “raw” tax increment, to distinguish it from other forms of tax increment derived from “raw” tax increment. This part of the definition is effective only for TIF districts with certification request dates after July 31, 1979, and for payments received after July 1, 1997.⁸³ If this effective-date language were applied literally, any “raw” tax increment received before July 2, 1997, would not be tax increment.

Second, there is disagreement regarding whether clause (3) or clause (4) of the definition of “increment” applies to loan interest payments received by a TIF authority on a loan made with tax increment. Determining which clause applies is important, because clauses (3) and (4) have different effective dates. The effective date for clause (3) is later, and thus more favorable for TIF authorities, than clause (4).

Some TIF authorities and municipalities have argued that loan interest payments fall within clause (3) of the definition, which applies to “repayments of loans or other advances made by the authority with tax increments.” Minn. Stat. § 469.174, subd. 25 (1998). It is the OSA’s position that interest on a loan made with tax increment is “interest or investment earnings on or from tax increments” and is subject to clause (4) of the definition. Minn. Stat. § 469.174, subd. 25 (1998). Clause (3) of the definition of “increment” explicitly applies only to “*repayments of loans*” by a borrower, not all of the debt service payments by a borrower. Minn. Stat. § 469.174, subd. 25 (1998) (emphasis added). The principal portions of debt service payments are “repayments of loans,” because the TIF authority disburses the loan principal to the borrower, and the borrower repays the principal. In contrast, the TIF authority does not pay the interest to the borrower, so the borrower does not *repay* the interest. Therefore, the interest portions of debt service payments are not “repayments of loans.”

⁸¹ See Laws 1997, ch. 231, art. 10, sec. 2 (enacting Minn. Stat. § 469.174, subd. 25).

⁸² Minn. Stat. § 469.174, subd. 25(1) (1998).

⁸³ Laws 1997, ch. 231, art. 10, sec. 25.

F. DISCOUNT RATE TO CALCULATE PRESENT VALUE OF TAX INCREMENT

As part of the “but for” test, a municipality must make the following finding before it may approve the TIF plan after June 30, 1995:

[T]he increased market value of the site that could reasonably be expected to occur without the use of tax increment financing would be less than the increase in the market value estimated to result from the proposed development after subtracting the *present value of the projected tax increments* for the maximum duration of the district permitted by the plan. The requirements of this clause do not apply if the district is a qualified housing district, as defined in section 273.1399, subdivision 1.⁸⁴

Minn. Stat. § 469.175, subd. 3 (1998) (emphasis added). To calculate the present value of a projected stream of revenue, such as tax increment from a new TIF district, one must use a discount rate. This statute does not specify a discount rate.

The OSA recommends that the Legislature amend this statute to specify a discount rate or a formula and a source of data for calculating a discount rate to assist in determining compliance with this statute. If the Legislature enacts such an amendment, the OSA recommends that the amendment be effective prospectively and apply only to TIF districts with certification request dates after some future date.

G. LIMITATION ON ADMINISTRATIVE EXPENSES

For TIF districts with certification request dates before August 1, 1979, or after June 30, 1982, the amount of tax increment that may be used to pay administrative expenses is limited to ten percent of the total estimated tax increment expenditures authorized in the TIF plan or ten percent of the total tax increment expenditures for the project, whichever is less.⁸⁵ It is difficult to determine ten percent of the total tax increment expenditures for the project, because there may be more than one TIF district in a project and the duration of the project may extend many years beyond the duration of a particular TIF district.

The OSA recommends that the Legislature amend the limitation on administrative expenses to provide that the limit is ten percent of the estimated tax increment expenditures authorized in a district’s TIF plan for a district or ten percent of *the district’s* total tax increment expenditures for the project, whichever is less.

⁸⁴ The “clause” referred to in this last sentence includes not only this market value test quoted above, but also the “but for” test itself. Qualified housing districts were not exempt from the “but for” test before the amendment that added this language. *See* Minn. Stat. § 469.175, subd. 3 (1994); Laws 1995, ch. 264, art. 5, sec. 18. The apparent exemption of post-1995 qualified housing districts from the “but for” test appears to be a drafting error.

⁸⁵ Minn. Stat. § 469.176, subd. 3(a) (1998).

The OSA recommends that this amendment apply prospectively only to TIF districts, or geographic enlargements of existing TIF districts, with certification request dates after some future date.

H. USE OF TAX INCREMENT FOR TOURISM FACILITIES

In 1999, the Legislature amended Minn. Stat. § 469.176, subd. 4g to prohibit the use of tax increment for a commons area used as a public park or for a facility used for social, recreational, or conference purposes, except that tax increment may be used for the renovation or construction of a privately owned conference facility.⁸⁶ An earlier statute provides that tax increment from an economic development district may be used to finance development of a facility if at least 85 percent of the buildings and facilities are used for a tourism facility.⁸⁷ The definition of “tourism facility” includes a facility used for social or recreational purposes or a publicly owned conference facility, all of which now are prohibited uses of tax increment under the amendment to Minn. Stat. § 469.176, subd. 4g.⁸⁸ Therefore, it appears these two statutes are in conflict.

Furthermore, it is difficult to determine compliance with the definition of “tourism facility.” Specifically, a facility qualifies as a “tourism facility” if, among other things, it—

is located in a county in which, excluding the cities of the first class in that county, the earnings on tourism-related activities are 15 percent or more of the total earnings in the county[.]

Minn. Stat. § 469.174, subd. 22 (1998). The statute does not specify the source of data for the amount of earnings in each county on tourism-related activities, and the OSA is not aware of any source for this data. Therefore, the OSA cannot determine which facilities are located in a county which meets this qualification.

The OSA recommends that the Legislature delete “tourism facilities” from the list in Minn. Stat. § 469.176, subd. 4c of approved uses of tax increment from an economic development district and repeal the definition of “tourism facility” in Minn. Stat. § 469.174, subd. 22. If the Legislature enacts these amendments, the OSA recommends that the amendments be effective prospectively and apply only to TIF districts with certification request dates after some future date.

I. EXTENSION OF TIME TO RESPOND TO NOTICES OF NONCOMPLIANCE

If a municipality receives a notice from the OSA that its TIF authority is not in compliance with the TIF Act, the municipality must respond in writing within 60 days after receiving the notice of noncompliance. The

⁸⁶ Laws 1999, ch. 243, art. 10, sec. 2.

⁸⁷ Minn. Stat. § 469.176, subd. 4c (1998).

⁸⁸ Minn. Stat. § 469.174, subd. 22 (1998).

municipality's written response must state whether it accepts, in whole or in part, the OSA's findings of noncompliance. If the municipality disagrees with any of the findings, the written response must indicate the basis for the disagreement.⁸⁹

Many municipalities have informed the OSA that the 60-day statutory response period is difficult to meet. The OSA's initial notice of noncompliance often will contain numerous findings which the municipality must review and research prior to preparing a written response to the notice of noncompliance.

Therefore, the OSA recommends that the Legislature amend Minn. Stat. § 469.1771, subd. 1(c) to extend the time within which a municipality must submit its written response to a notice of noncompliance from 60 days to 90 days after receiving the notice.⁹⁰ If the Legislature enacts this amendment, the OSA recommends that the amendment be effective prospectively and apply only to responses to notices of noncompliance issued after some future date.

IV. CONCLUSION

In December 1998, the TIF Division moved its offices to a new location:

Office of the State Auditor
Tax Increment Financing Division
505 Spruce Tree Centre
1600 University Ave. W.
St. Paul, MN 55104
Telephone: (651) 642-0767
Fax: (651) 642-0769
email: tifdivision@osa.state.mn.us

⁸⁹ Minn. Stat. § 469.1771, subd. 1(c) (1998).

⁹⁰ Regarding a related provision, the OSA also recommends that the Legislature extend the time period after which violation payments are considered late from 60 days to 90 days after the municipality receives the OSA's notice of noncompliance. *See* Minn. Stat. § 469.1771, subd. 5 (1998).

The TIF Division's staff is available to answer questions you may have relating to TIF. Please feel free to contact any of our staff at the telephone numbers listed below.

Bill Connors, TIF Division Director	(651) 642-0837
Marsha Pattison, Office Specialist	(651) 642-0767
Hassan Bastani	(651) 642-0775
Paul Eisenmenger	(651) 642-0892
Matthew Gaetz	(651) 643-2132
Kurt Mueller	(651) 642-0832
James Silen	(651) 642-0823
Linda Thomas	(651) 642-0815
David Wilwert	(651) 642-0824

EXHIBIT 1

Statistics on TIF Reporting for Year Ended December 31, 1998

Three statutory subdivisions impose annual reporting obligations on TIF authorities and municipalities and describe the TIF information they must submit.⁹¹ All three TIF-reporting subdivisions apply to all TIF districts regardless of when they were created. All three subdivisions mandate that TIF authorities and municipalities submit the required information to the OSA.

In 1998, at the OSA's request, the Legislature lengthened the time that TIF authorities and municipalities have to prepare their TIF reports by changing the filing deadline from July 1 to August 1 each year.⁹² This new filing deadline was effective starting with the TIF reports that were required to be filed in 1999.⁹³

In addition to filing TIF reports, a TIF authority must publish certain statutorily required financial information about each of its TIF districts in a newspaper of general circulation.⁹⁴ The Legislature changed the publication deadline from July 1 to August 15 effective starting with the publications that were required to be made in 1999.⁹⁵

In 1998, the Legislature also enacted Minn. Stat. § 469.1771, subd. 2a, which establishes a procedure for tax increment to be withheld by the county auditor if the TIF authority or municipality fails to file reports containing the required TIF information, or a copy of the annual disclosure statement, by the statutory deadline.⁹⁶ The withheld tax increment will be released and distributed whenever substantially complete TIF reports eventually are filed. These changes were effective starting with the TIF reports and annual disclosure statement that were required to be filed in 1999.⁹⁷

⁹¹ See Minn. Stat. § 469.175, subd. 5, 6, and 6a (1998).

⁹² Laws 1998, ch. 389, art. 11, sec. 2, 3 and 4.

⁹³ Laws 1998, ch. 389, art. 11, sec. 29. These were the TIF reports and disclosure statement for the year ended December 31, 1998.

⁹⁴ See Minn. Stat. § 469.175, subd. 5(b) (1998).

⁹⁵ Laws 1998, ch. 389, art. 11, sec. 2 and 29.

⁹⁶ See Laws 1998, ch. 389, art. 11, sec. 8.

⁹⁷ Laws 1998, ch. 389, art. 11, sec. 29.

A total of 433 TIF authorities had TIF districts for which they and their municipalities were required to file TIF reports with the OSA for the year ended December 31, 1998, which were due by August 2, 1999.⁹⁸ These TIF authorities and municipalities were required to file reports for 2,061 TIF districts.

The OSA returns TIF reports that are not substantially complete and treats them as not filed. Of the 433 TIF authorities with TIF districts for which filing was required, 305 had substantially complete TIF reports for all their TIF districts and copies of their annual disclosure statements filed with the OSA by the August 2, 1999, deadline.⁹⁹ In addition, 65 TIF authorities had at least some of the required TIF reports filed with the OSA by the August 2, 1999, deadline, but either (1) not all of the required reports were filed, (2) not all of the required reports were substantially complete, or (3) the copy of the annual disclosure statement was not filed by the deadline.¹⁰⁰

In contrast, the following 63 TIF authorities had no reports for their TIF districts filed with the OSA by the August 2, 1999, deadline:

Aitkin, City of	Clarkfield HRA	Hallock, City of
Bagley, City of	Cologne, City of	Hector, City of
Bagley HRA	Cook County/Grand	Hibbing, City of
Belle Plaine EDA	Marais Joint EDA	Hinkley, City of
Benton County	Coon Rapids, City of	Hoffman, City of
Brooklyn Center, City of	Cottonwood County	Holdingsford, City of
Brooklyn Park, City of	Deephaven, City of	Howard Lake, City of
Browns Valley, City of	Dexter, City of	Hutchinson, City of
Butterfield, City of	Dundas, City of	Isanti, City of
Caledonia, City of	Elgin, City of	Isle, City of
Cannon Falls, City of	Frazee, City of	Lake City, City of
Carver, City of	Freeborn County HRA	Mapleview, City of
Clara City, City of	Goodview, City of	Medford, City of

⁹⁸ The statutory deadline was August 1, 1999, which was a Sunday. Consequently, the OSA treated as timely any substantially complete TIF reports that were filed on or before Monday, August 2, 1999.

⁹⁹ The percentage of TIF authorities with substantially complete 1998 TIF reports for all their TIF districts filed by the August 2, 1999, was 70.4 percent. In comparison, the percentage of TIF authorities with substantially complete 1997 TIF reports for all their TIF districts filed by the July 1, 1998, was 42.4 percent.

¹⁰⁰ The percentage of TIF authorities without substantially complete 1998 TIF reports for all their TIF districts but which filed something by the August 2, 1999, was 15.0 percent. In comparison, the percentage of TIF authorities without substantially complete 1997 TIF reports for all their TIF districts but which filed something by the July 1, 1998, was 34.7 percent.

Meire Grove, City of	City of	Spring Lake Park, City of
Montgomery EDA	Onamia, City of	Verndale, City of
Montrose, City of	Ortonville, City of	Virginia, City of
Moose Lake, City of	Pillager, City of	Wabasha, City of
Mounds View EDA	Richmond, City of	Wahkon, City of
Minneapolis Community	Rush City, City of	Waldorf, City of
Development Agency	St. Bonifacius, City of	Watertown, City of
North Branch, City of	Savage, City of	Woodbury, City of
Norwood/Young America,	Sebeka, City of	Wyoming, City of

On August 16, 1999, the OSA mailed notices to 128 TIF authorities informing them that the OSA had not received substantially complete 1998 TIF reports for one or more of their TIF districts as of August 2, 1999, and that tax increment from those districts would be withheld pursuant to Minn. Stat. § 469.1771, subd. 2a. On November 19, 1999, the OSA mailed notices to county auditors to withhold distributions of tax increment from identified TIF districts to the following 19 TIF authorities because, as of November 16, 1999, the OSA had not yet received substantially complete 1998 TIF reports for the identified TIF districts:

Bagley HRA	Elgin, City of	Norwood/Young America,
Benton County	Hector, City of	City of
Brooklyn Park, City of	Holdingsford, City of	Onamia, City of
Caledonia, City of	Howard Lake, City of	Pillager, City of
Clara City, City of	Medford, City of	Wabasha, City of
Clarkfield HRA	Mounds View EDA	Wyoming, City of
Cologne, City of	Northwest MN Multi- County HRA	

In addition to reviewing all TIF reports for completeness, the TIF Division staff reviews the contents of many of the TIF reports each year for reporting accuracy and potential legal compliance issues. During the course of these in-depth reviews, the TIF Division staff may find situations where a TIF authority has received tax increment after the TIF district was required to be decertified or has made unauthorized expenditures of tax increment. From January 1, 1996, to date, the review of reports by the TIF Division staff and subsequent contact with reporting local government units, plus the legal compliance auditing performed by the TIF Division staff, has resulted in over \$2.7 million being paid to county auditors voluntarily or as the result of settlement agreements with county attorneys. This amount was redistributed to the cities, towns, counties, and school districts in which the relevant TIF districts were located.¹⁰¹ In addition, the OSA's TIF enforcement activities may have prompted internal examinations that resulted in additional voluntary payments to county auditors of which the OSA is unaware.

¹⁰¹ See Minn. Stat. §§ 469.176, subd. 2, and 469.1771, subd. 2 and 3 (1998). Some of the school districts which received these redistributions had their state aid decreased by the amount received from the redistributions, which resulted in a savings to the state's General Fund.