

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

TAX INCREMENT FINANCING LEGISLATIVE REPORT

TIF Reports for the Year Ended December 31, 2008
TIF Audits Concluded for the Year Ended December 31, 2009

Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 160 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits for local governments;

Government Information - collects and analyzes financial information for cities, towns, counties, and special districts;

Legal/Special Investigations - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government.

Pension - monitors investment, financial, and actuarial reporting for approximately 730 public pension funds; and

Tax Increment Financing - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employee's Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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TAX INCREMENT FINANCING LEGISLATIVE REPORT

TIF Reports for the Year Ended December 31, 2008
TIF Audits Concluded for the Year Ended December 31, 2009



February 8, 2010

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TAX INCREMENT FINANCING REPORT

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EXECUTIVE SUMMARY

Current Trends

- A total of **\$10,971,913** in tax increment revenues was returned to county auditors for redistribution as property taxes in calendar year 2008. (p. 19)
- Eighty-seven TIF districts were certified in Minnesota during calendar year 2008, while 115 TIF districts were decertified. (p. 24)
- In 2008, 33% of the TIF districts were located in the Metro Area; 67% were located in Greater Minnesota. However, 82% of the tax increment generated in 2008 was from districts located within the Metro Area. (p. 19)
- In 2008, 70% of the TIF districts in the state were located in third- and fourth-class cities. (p. 16)

Long-Term Trends

- When examining trends over the five-year period between 2004 and 2008, the number of economic development districts increased, while the number of housing districts declined. Over the same period, redevelopment districts showed no consistent trend. (p. 22)
- The total number of districts certified dropped sharply from 2001 to 2002 and, after a slight increase in 2003, the number of districts certified has continued to decrease. (p. 26)
- Over the ten-year period covering 1998 through 2008, the number of districts certified has declined approximately 42%. (p. 26)

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Scope and Methodology

In 1995, the Minnesota Legislature assigned compliance oversight for tax increment financing (TIF) to the Office of the State Auditor.¹ This oversight includes examining and auditing the use of TIF by political subdivisions, as authorized by the Minnesota Tax Increment Financing Act (TIF Act).²

The TIF Act requires an authority to file annual financial reports for each of its TIF districts with the Office of the State Auditor. This reporting requirement applies to all TIF districts regardless of when they were created. An authority must submit its reports on or before August 1 of each year, starting in the year in which the district is certified.

A total of 443 development authorities had 2,057 TIF districts for which they were required to file TIF reports with the Office of the State Auditor for the year ended December 31, 2008. To date, the Office of the State Auditor has received reports for 2,048 of the TIF districts.

Of the 443 development authorities required to file reports, 414 submitted complete reports by the statutory deadline of August 1. On August 19, 2008, letters were sent to the remaining 29 development authorities, addressed to the governing board of the municipality, advising them that the required reports had not been filed.

Of the 29 authorities that had not filed complete reports by the statutory deadline, 11 still had not filed all of the required reports as of October 1, 2008. Pursuant to Minnesota law, a notice was mailed to each of the applicable county auditors to withhold tax increment that otherwise would have been distributed to the authorities from the identified TIF districts.³ As of the date of this report, two authorities have not yet completed filing their reports.⁴

A legislative report containing a summary of the TIF reports and audits is provided annually to the chairs of the legislative committees with jurisdiction over TIF matters.⁵ This fourteenth Annual Legislative Report was compiled from information received from the 443 municipalities and development authorities currently authorized to exercise TIF powers in Minnesota. The report summarizes the data received from approximately 2,048 unaudited TIF reports for the year ended December 31, 2008, and provides a summary of the violations cited in the limited-scope audits concluded by the Office of the State Auditor in 2009.

¹ Minn. Stat. § 469.1771.

² Minn. Stat. §§ 469.174 through 469.1799 inclusive, as amended.

³ Minn. Stat. § 469.1771, subd. 2a. Any authority which has not filed complete TIF reports by October 1 will have 100% of the tax increment withheld from any payment scheduled to be made after October 1 until the authority has filed complete reporting forms with the Office of the State Auditor.

⁴ The City of Hitterdal and the Le Sueur Economic Development Authority have not filed the required reporting forms for 2008.

⁵ Minn. Stat. § 469.1771, subd. 1(c).

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TAX INCREMENT FINANCING LEGISLATIVE REPORT

BACKGROUND

What is Tax Increment Financing?

Tax increment financing (TIF) is a tool created by the Legislature to promote economic development, redevelopment, and housing development in areas where it would not otherwise occur. A development authority, which could be either a city, an entity created by a city, or an entity created by a county, “captures” the revenues generated by an increase in net tax capacity. New development within a designated geographic area, called a TIF district, generates the increase in tax capacity. The development authority uses the tax increment revenues to finance public improvements and other qualifying costs related to the new development.

Tax increment financing is not a property tax abatement program. The owner of the property located in the TIF district continues to pay the same amount of property taxes that would have otherwise been paid. Instead of being paid to the local taxing jurisdictions for their general use, the portion of property taxes generated by the new development is used to pay for public improvements and qualifying costs that made the new development possible. Examples of such costs include: land and building acquisition, demolition of structurally substandard buildings, removal of hazardous substances, site preparation, installation of utilities, and road improvements. The costs that may be paid from tax increment revenues depend on the type of development activity taking place, the type of TIF district created, and the year in which the TIF district was created.

In some TIF districts, bonds are sold by the municipality or development authority at the outset of the development activity so that funds are available for front-end costs, such as pollution clean-up. The bonds are then fully or partially paid with tax increment revenues from the TIF district. In other TIF districts, the authority or municipality loans or advances money from its general fund or from any other fund for which it has legal authority. The loan or advance must be authorized by resolution of the governing body before money is transferred, advanced, or spent. The terms and conditions for repayment of the loan must be provided in writing and include, at a minimum, the principal amount, the interest rate, and maximum term.¹

Pay-as-you-go (PAYG) financing is often used as an alternative to up-front bond financing. Under this type of bond, the development costs are initially paid by the developer pursuant to the terms of a (re)development agreement. After the qualifying costs are substantiated, the developer is then reimbursed pursuant to the terms of the PAYG note if, and when, tax increment is generated by the TIF district. Generally, in

¹ Minn. Stat. § 469.178, subd. 7.

PAYG financing, the developer accepts the risks of failed development. If the tax base does not increase and tax increments are not generated as anticipated, then the developer does not get reimbursed.

Who is Authorized to Create TIF Districts?

Development authorities within municipalities may create TIF districts.² Development authorities derive their powers from the Housing and Redevelopment Authorities (HRA) Act, the Port Authorities Act, the Economic Development Authorities (EDA) Act, and the Rural Development Financing Authorities Act.³ Any municipality administering a city development district or the powers of a port authority under any general or special law is also a development authority.⁴ City council members may also serve on the board of an HRA, an EDA, or a port authority established by the city they serve. Counties do not have independent development powers but can establish county HRAs and EDAs on which county board members may serve. A development authority must be in place before a TIF district can be created.

Each underlying development entity has unique development powers which come from the development authority. These powers identify the purposes for which tax increment can be used. The TIF Act, however, limits the development authority powers.⁵

The development authority laws and the TIF Act are linked through the term “project.”⁶ The term “project” is used differently in each of the development authority laws. A project can be: any combination of a housing project, a housing development project, or a redevelopment project; property/cash/assets/funds held or used in connection with the development or operation of a project in the HRA Act⁷; or simply a designated area within a city in the City Development Districts Act.⁸

When the TIF Act was enacted in 1979, the Legislature intended a TIF district to be the parcel(s) on which new development activity was occurring. The geographic area of a project was intended to be only modestly larger than the TIF district to permit tax increment revenues to be spent outside the district but within a larger area. Tax increment could then be used to connect utilities and other infrastructure from the developed area of the community to the site. However, no specific statutory limits were

² Minn. Stat. § 469.174, subd. 2 and subd. 6. Counties are defined as “municipalities” for projects undertaken by county development authorities.

³ Minn. Stat. § 469.174, subd. 2, lists the statutory citations for the HRA Act, the Port Authorities Act, the EDA Act, the City Development Districts Act, and the Rural Development Financing Authorities Act.

⁴ Minn. Stat. § 469.14, subd. 2. HRAs, port authorities, and EDAs are public bodies, corporate and politic; rural development financing authorities are public nonprofit corporations; city development districts are designated areas within the corporate limits of a city.

⁵ Minn. Stat. §§ 469.174 to 469.1799, as amended. The Act also provides procedures for establishing TIF districts and for the administration of districts, as well as providing additional development powers.

⁶ Minn. Stat. § 469.174, subd. 8.

⁷ Minn. Stat. § 469.002, subd. 12.

⁸ Minn. Stat. § 469.125, subd. 9.

placed on the size of the geographic area of a project, and the development authority laws themselves do not contain clear or explicit limits on the size of areas that can qualify as projects.

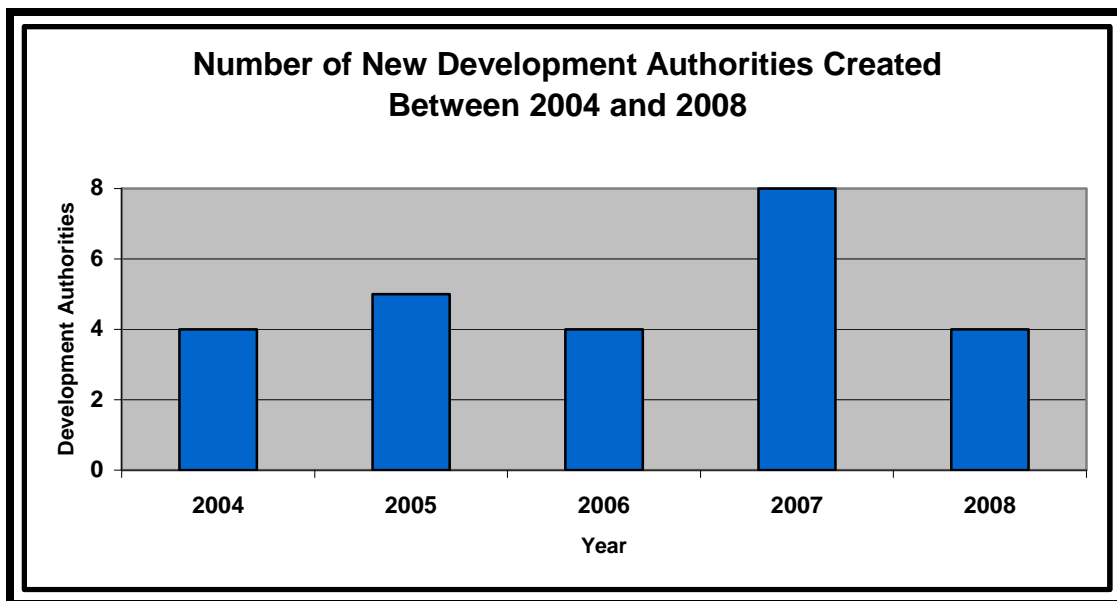
The various uses of the term “project” in the underlying development authority laws, and the fact that the TIF Act does not contain an express limitation on the size of a project, have allowed projects to become increasingly larger over time. An informal office review of TIF plans and project area maps shows approximately 46% of active development authorities have project areas in which the boundaries are coterminous with the geographic boundaries of the municipality. Authorities in those cities have apparently been advised that tax increment generated from a TIF district can be used to finance needed capital improvements anywhere within the city. This advice is given primarily for TIF districts established prior to 1990 when pooling of tax increment revenues was not restricted.⁹

Development Authorities

In 2008, four new development authorities were created, for a current total of 443 development authorities.

Figure 1 below shows the number of new development authorities created over the past five years.

Figure 1.

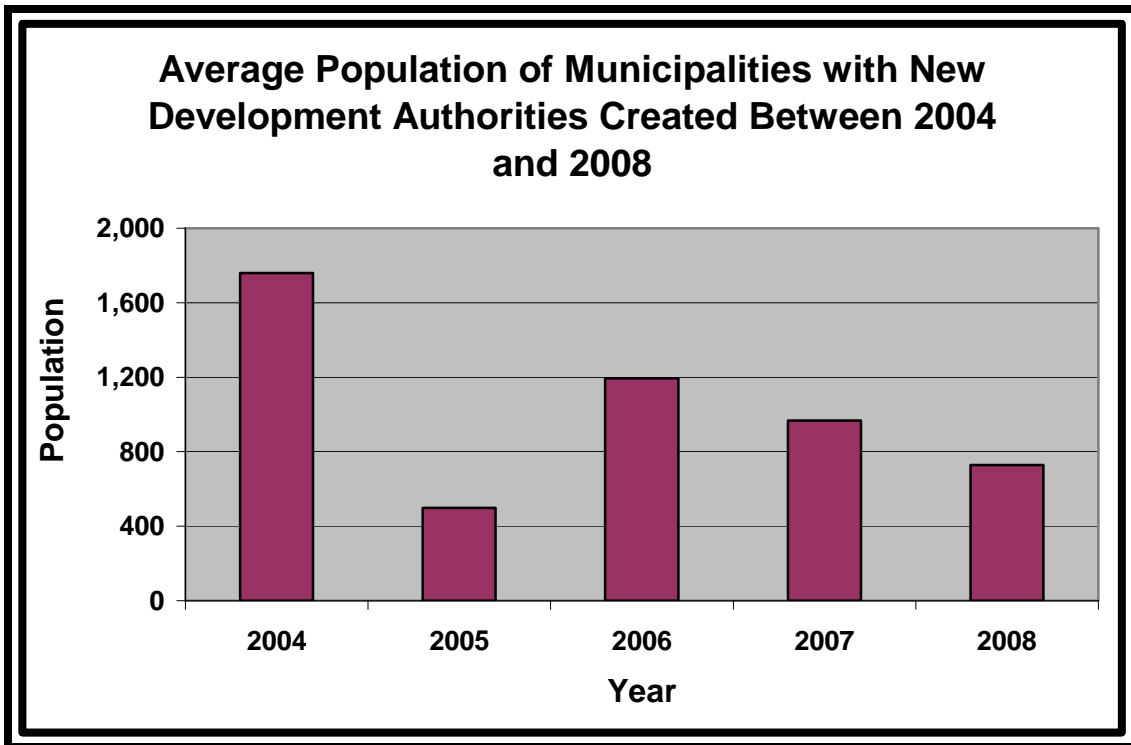


⁹ “Pooling” is discussed but not defined in the TIF Act. *See* Minn. Stat. § 469.1763, subd. 6 (Pooling permitted for deficits). Pooling means the sharing or “pooling” of tax increment revenues from one or more TIF districts to be spent for development purposes within the district and the project area. Tax increment revenues, whether spent inside or outside a TIF district, are to be spent for the purposes authorized in the underlying development authority laws.

Since 2004, 25 new authorities have been created.¹⁰ The average population of the municipalities with new development authorities created since 2004 is approximately 998.

Figure 2 below shows the average population of the municipalities with new development authorities each year.

Figure 2.



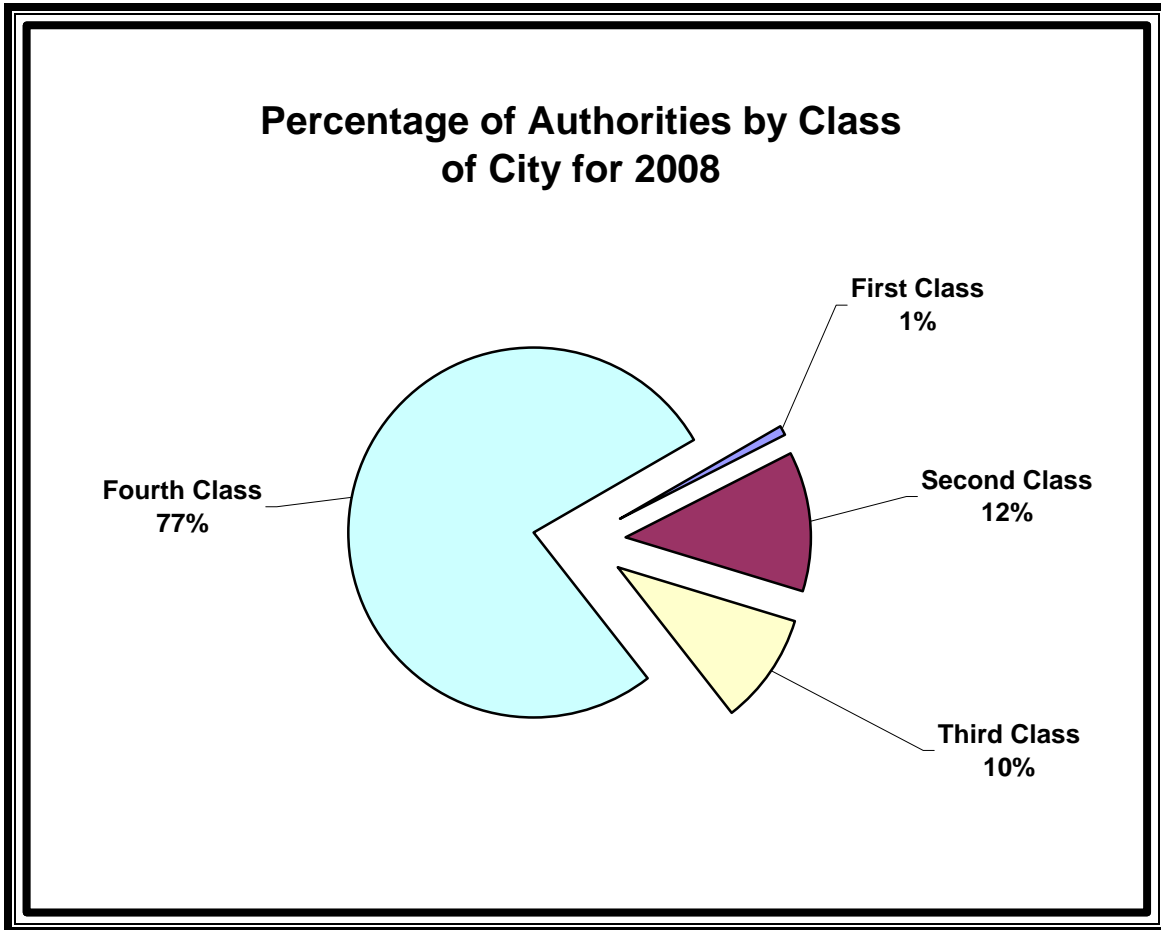
State law divides Minnesota’s 854 cities into four different classes based on population.¹¹ First-class cities are those with more than 100,000 people. There are currently three first-class cities in Minnesota: Minneapolis, St. Paul, and Duluth.¹² Second-class cities have populations between 20,000 and 100,000; third-class cities have populations between 10,000 and 20,000; and fourth-class cities have populations of no more than 10,000 people.

¹⁰ This number does not include the two new county development authorities or the new authorities created by the seven municipalities already using TIF.

¹¹ Minn. Stat. § 410.01.

¹² Duluth no longer has a population of more than 100,000, but it retains its status as a first-class city. *See* Minn. Stat. § 410.01. (“Once a city is defined to be a city of the first class, it shall not be reclassified unless its population decreases by 25 percent.”)

Figure 3.

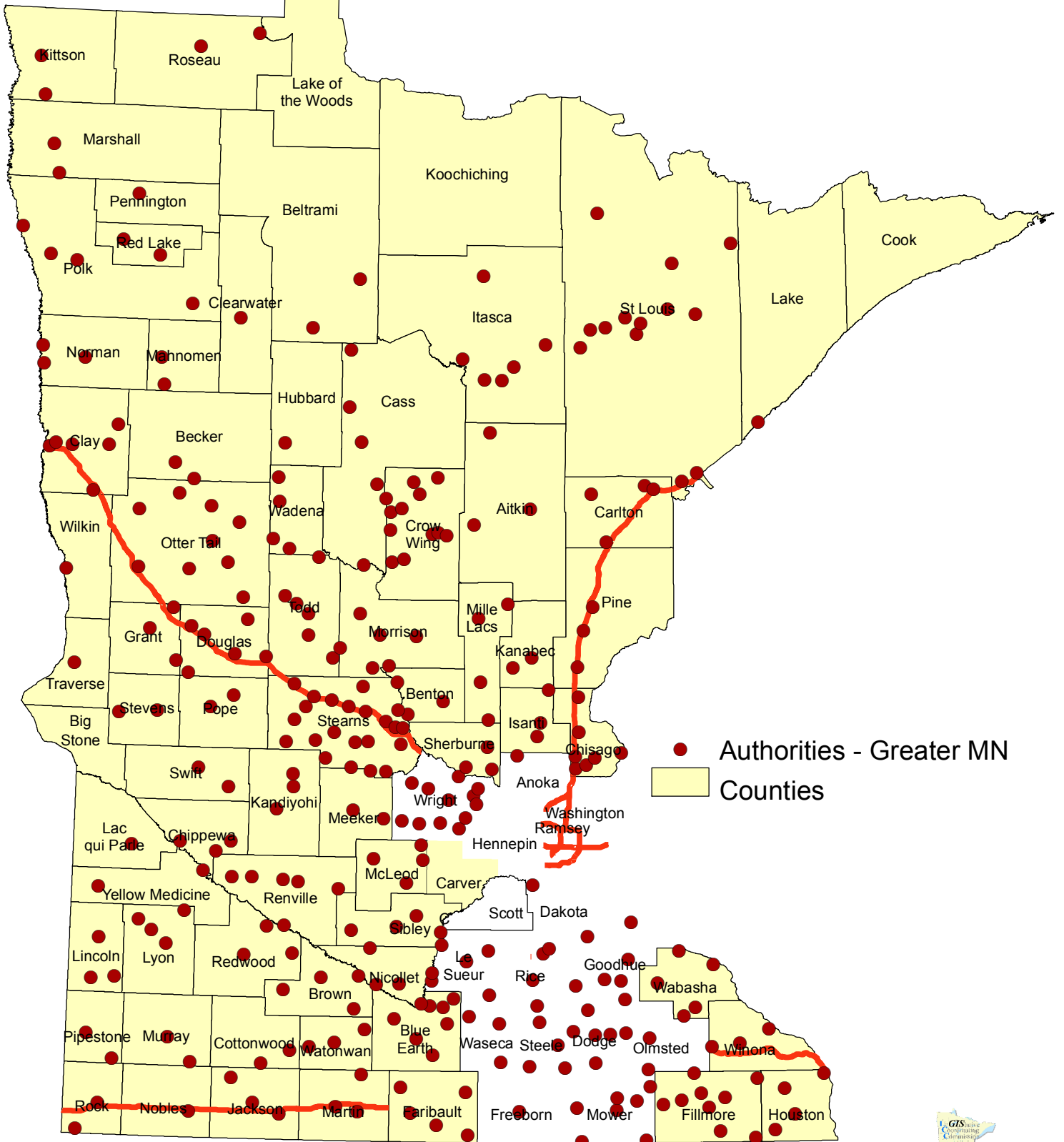


Fourth-class cities comprise approximately 90% of the cities within the state. Second- and third-class cities comprise approximately 5% and 4% of the cities within the state, respectively. The largest percentage of development authorities exists in fourth-class cities. Second- and third-class cities have a near equal percentage of authorities: 12% and 10%, respectively.

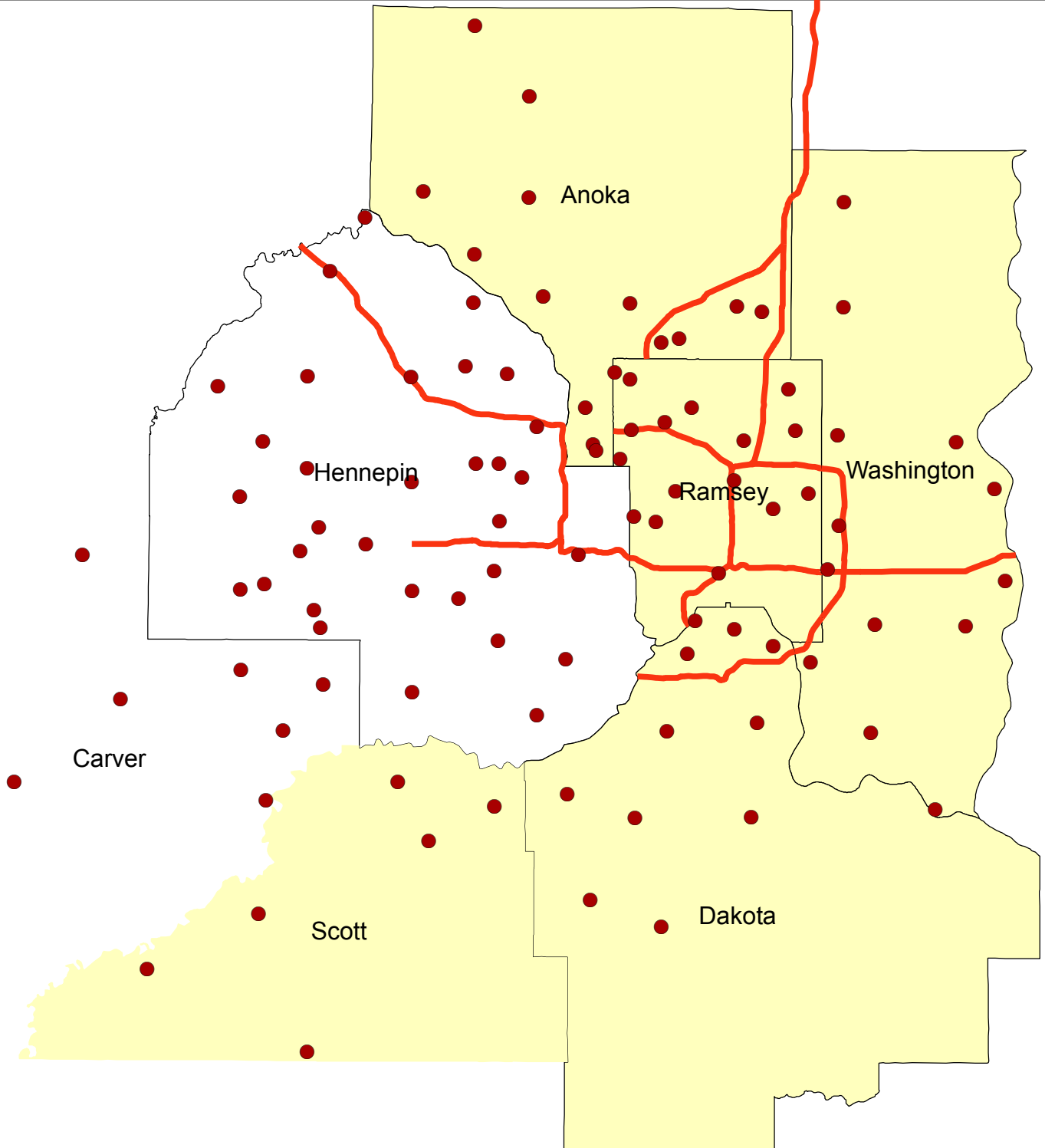
Development Authorities by Location

Development authorities using TIF powers are located throughout the State of Minnesota. Of the 443 development authorities, 336 are located in Greater Minnesota and 107 are located in the Seven-County Metropolitan Area (Metro Area). Maps 1 and 2 on the following pages show the locations of these authorities.

2008 Authorities in Greater Minnesota



2008 Authorities in Seven-County Metro Area



- Authorities - Seven-County Metro Area
- Counties



Map 3 on the following page identifies the various counties throughout the state that have created a separate authority to use TIF.¹³

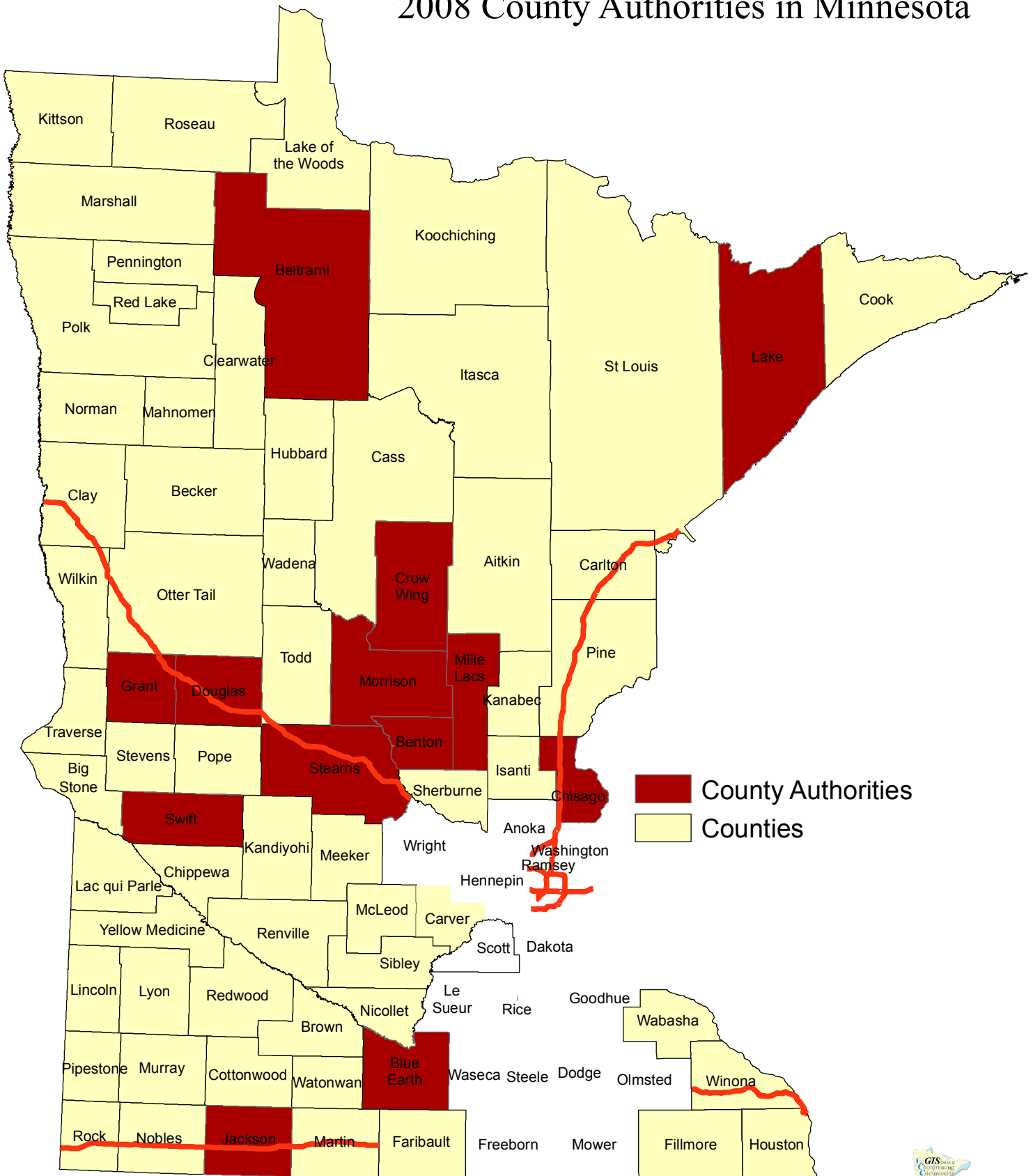
Map 4 shows the distribution of development authorities among the regional development commissions (RDCs). RDCs are not limited to the boundaries of local units of government. RDCs work with authorities and on behalf of authorities to develop plans and implement programs addressing economic and governmental concerns of a regional nature.¹⁴ The RDCs in Minnesota are:

- Region 1 Northwest RDC
- Region 2 Headwaters RDC
- Region 3 Arrowhead RDC
- Region 4 West Central Initiative Fund
- Region 5 RDC
- Region 6E Mid-Minnesota Valley RDC
- Region 6W Upper Minnesota Valley RDC
- Region 7E East Central RDC
- Region 7W RDC
- Region 8 Southeast RDC
- Region 9 RDC
- Region 10 RDC
- Region 11 Metropolitan Council

¹³ This map does not include multi-county or joint authorities.

¹⁴ Minn. Stat. § 462.383, subd. 2 (authorizing the establishment of RDCs).

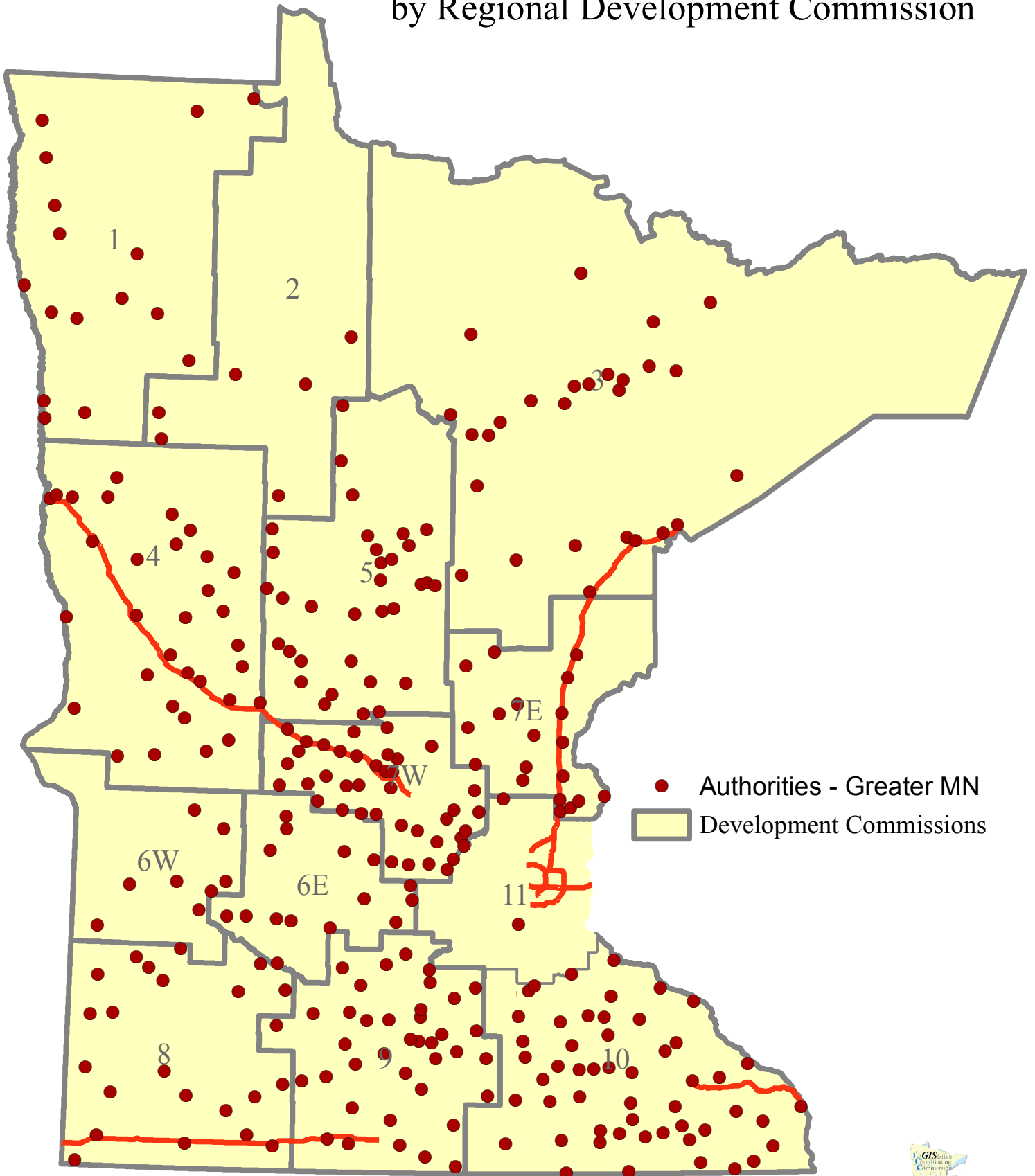
2008 County Authorities in Minnesota



County Authorities
Counties



2008 Authorities in Greater Minnesota by Regional Development Commission



Creation of TIF Districts

Adopting a TIF plan for a district is the first step a development authority takes in creating a TIF district. The TIF plan outlines the development activity to be funded with tax increment and authorizes the use of tax increment to pay TIF-eligible project costs.¹⁵

To create a new TIF district, an authority must obtain approval of the TIF plan from the governing body of the municipality in which the TIF district is to be located after the municipality has published a notice for and held a public hearing.¹⁶ For example, if a city's port authority proposes creating a TIF district in the city, the city council must first approve the TIF plan for the district.¹⁷ If a county HRA proposes creating a TIF district in a township in the county, the county board must approve the TIF plan.

Before a TIF district is created, the development authority must also provide a copy of the proposed TIF plan and certain information about the proposed TIF district to the county auditor and the clerk of the school board who, in turn, provide copies of these documents to the members of the county board of commissioners and the school board.¹⁸ The county board and school board may comment on the proposed district, but cannot prevent its creation.¹⁹

Types of TIF Districts

The TIF Act divides TIF districts into the following categories based on the physical condition of the site and on the type of construction that is to occur:

- Redevelopment districts
- Economic development districts
- Housing districts
- Renewal and renovation districts
- Soils condition districts

In addition to the types of districts listed above, there are districts that were created prior to the enactment of the TIF Act (called "pre-1979 districts") and districts that have been created under special laws. Each type of TIF district has different requirements for its creation. Each type of district also has different maximum duration limitations and different restrictions on the use of tax increment revenue.

¹⁵ Minn. Stat. § 469.175, subd. 1.

¹⁶ Minn. Stat. § 469.175, subd. 3.

¹⁷ In many cases, the commissioners of the TIF authority include some or all of the council members.

¹⁸ Minn. Stat. § 469.175, subd. 2.

¹⁹ In those situations in which the county is the municipality that must approve the TIF plan, the county board may prevent creation of a TIF district.

Redevelopment Districts – The primary purpose of a redevelopment district is to eliminate blighting conditions.²⁰ Qualifying tax increment expenditures include acquiring sites containing substandard buildings or improvements; demolishing and removing substandard structures; eliminating hazardous substances; clearing the land; and installing utilities, sidewalks, and parking facilities. This activity, paid for with tax increment, is often referred to as “leveling the playing field.” It allows developed cities to compete for development with outlying cities with bare land. Redevelopment districts are intended to conserve the use of existing utilities, roads, and other public infrastructure and to discourage urban sprawl.

Economic Development Districts – An economic development district may not meet the requirements of any other type of district. It is a type of district that consists of a project which an authority considers to be in the public interest because it will (i) discourage commerce, industry or manufacturing from moving to another state or city; (ii) increase employment in the state; or (iii) preserve and enhance the tax base.²¹ Economic development districts are short-term districts (eight years). Tax increment revenues from economic development districts are used primarily to assist manufacturing, warehousing, storage and distribution, research and development, telemarketing, and tourism. Commercial development (retail sales) is excluded by law, except in “small cities.”²²

Housing Districts – The purpose of a housing district is to encourage development of owner-occupied and rental housing for low- and moderate-income individuals and families by using tax increment revenues as a type of financial assistance. Tax increment revenues can be used in the construction of low- and moderate-income housing, as well as to acquire and improve the housing site. The TIF Act’s low- and moderate-income limits are the same income limits found in the Internal Revenue Code.²³ However, the income limits for “qualified” housing districts are tied to the stricter federal low-income tax credit guidelines, regardless of whether tax credits are used. The 2008 Minnesota Legislature repealed the definition of “qualified housing.” Nevertheless, this more restrictive type of housing district designation continues to be used for qualified housing districts created prior to March 8, 2008.

Renewal & Renovation Districts – The purpose of a renewal and renovation district is similar to that of a redevelopment district, except the amount of blight to be removed may be less, and the development activity is more closely related to inappropriate or obsolete land use.

Soils Condition District – The purpose of a soils condition district is to assist in the redevelopment of property which cannot otherwise be developed due to the existence of hazardous substances, pollutants, or contaminants. The presence of these materials

²⁰ Minn. Stat. § 469.174, subd. 10(a)(1).

²¹ Minn. Stat. § 469.174, subd. 12.

²² Minn. Stat. § 469.174, subd. 27 and Minn. Stat. § 469.176, subd. 4c.

²³ Minn. Stat. § 469.1761. Income limits for owner-occupied housing units are identified in section 143(f) of the Internal Revenue Code. Income limits for rental housing units are identified in section 142(d) of the Internal Revenue Code.

requires removal or remedial action before the property can be used, and the estimated cost of the proposed removal and remediation must exceed the fair market value of the land before the remediation is completed.²⁴

Pre-1979 Districts – Districts created prior to the enactment of the TIF Act on August 1, 1979, are called pre-1979 districts. On April 1, 1990, many of the pre-1979 districts still in existence had significant amounts of debt outstanding. Tax increment from these districts could then be used only to retire that debt. Since August 1, 2009, pre-1979 districts can no longer receive tax increment payments.²⁵

Uncodified District – A special law may be enacted that permits the generation of tax increment revenues from a geographic area not meeting the definition of a type of TIF district authorized by Minnesota law. This type of district is referred to as an “uncodified” district. Examples of uncodified districts are housing transition districts for the cities of Crystal, Fridley, St. Paul, and Minneapolis, and a district with distressed rental properties in Brooklyn Park.

Special Legislation

In some cases, special legislation has been enacted to allow an exception to the general law for a development authority. As of 2008, 73 TIF districts reported having received one or more pieces of special legislation. The most common reasons for enacting special legislation are: (i) extending the five-year deadline for entering into contracts;²⁶ (ii) extending the duration limits of a TIF district;²⁷ (iii) creating an exception to requirements or findings needed to create a TIF district;²⁸ and (iv) creating an exception to the limitations on the use of tax increment.²⁹

Number of TIF Districts

In 2008, 95% of the 2,048 TIF districts were redevelopment, economic development, and housing districts. Figure 4 on the following page shows TIF districts by type on a statewide basis.

²⁴ Minn. Stat. § 469.174, subd. 19.

²⁵ Minn. Stat. § 469.176, subd. 1c.

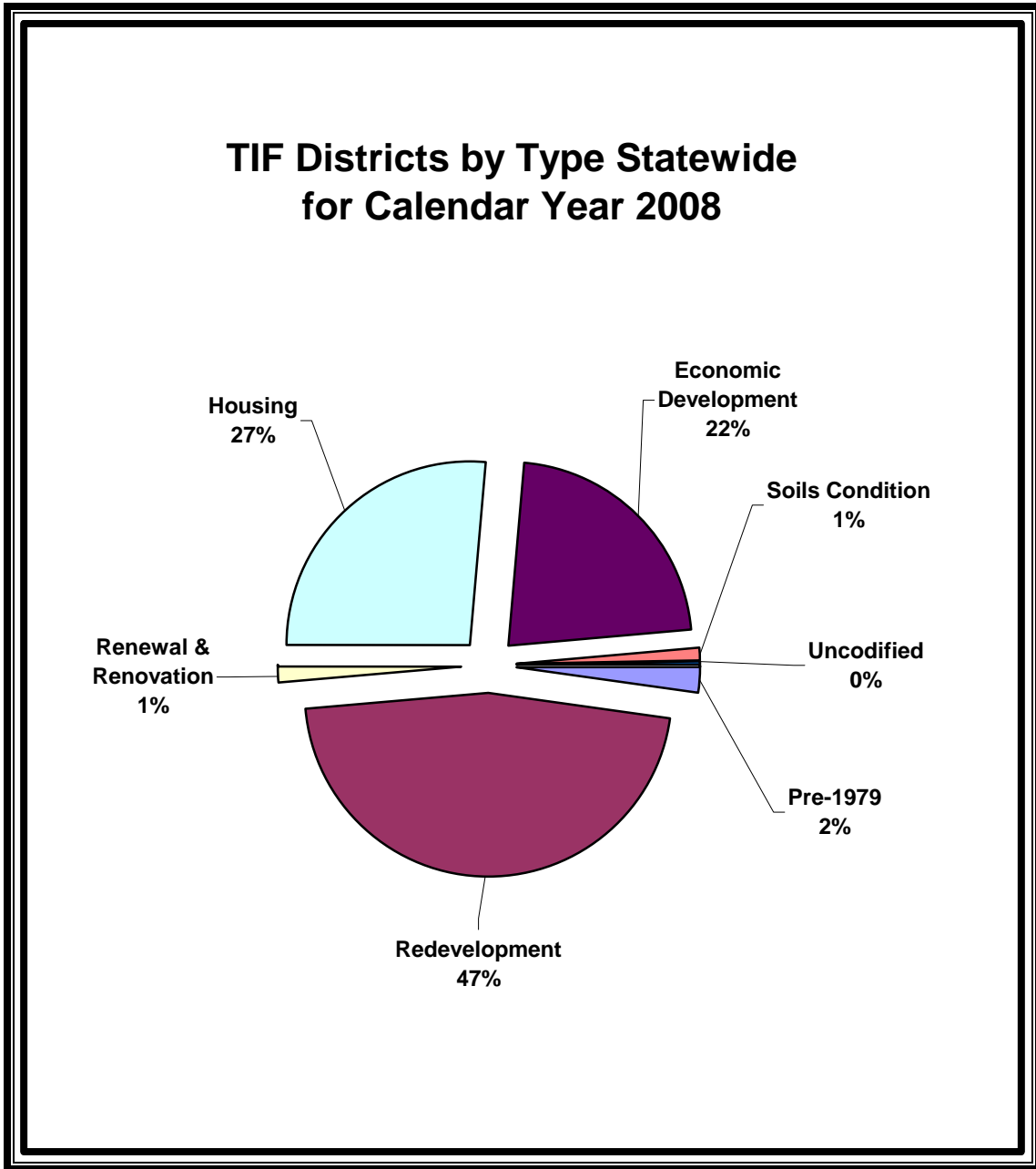
²⁶ See Minn. Stat. § 469.1763, subd. 3.

²⁷ See Minn. Stat. § 469.176, subd. 1b.

²⁸ See Minn. Stat. § 469.174 and Minn. Stat. § 469.175.

²⁹ See Minn. Stat. § 469.176.

Figure 4.



As shown in Figure 5 and Figure 6 on the following page, redevelopment districts make up the largest percentage of districts in both the Metro Area and in Greater Minnesota.

Figure 5.

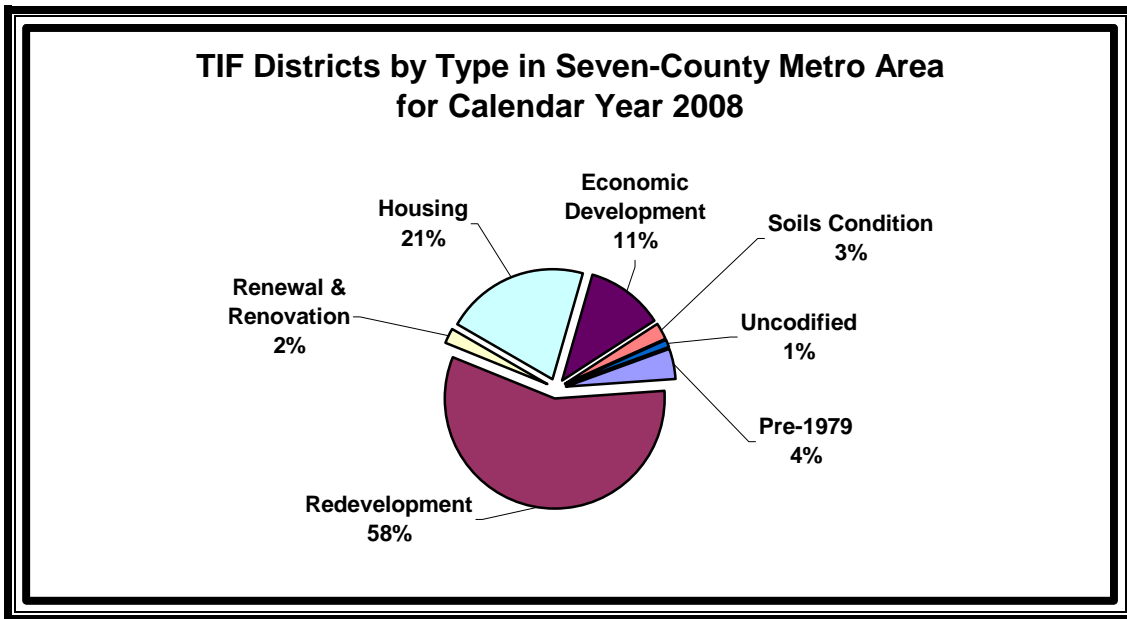
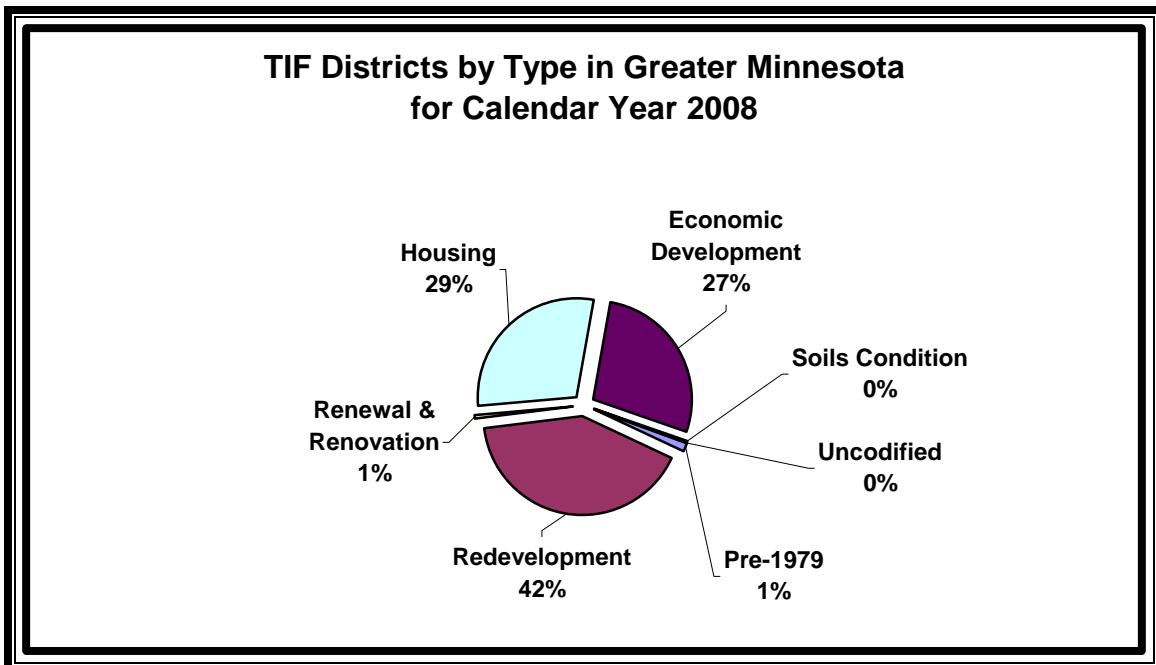


Figure 6.



Economic development districts focus on job production rather than on clearance and preparation of a development site. Therefore, Greater Minnesota, with open space and a critical need for employment, uses economic development districts more frequently than

the more fully-developed Metro Area. The land on which an economic development district is established may be bare land. The eight-year term of the district is generally sufficient as less tax increment is needed to pay for site preparation.

Figure 7 below shows that 70% of the TIF districts in the state are located in third- and fourth-class cities.

Figure 7.

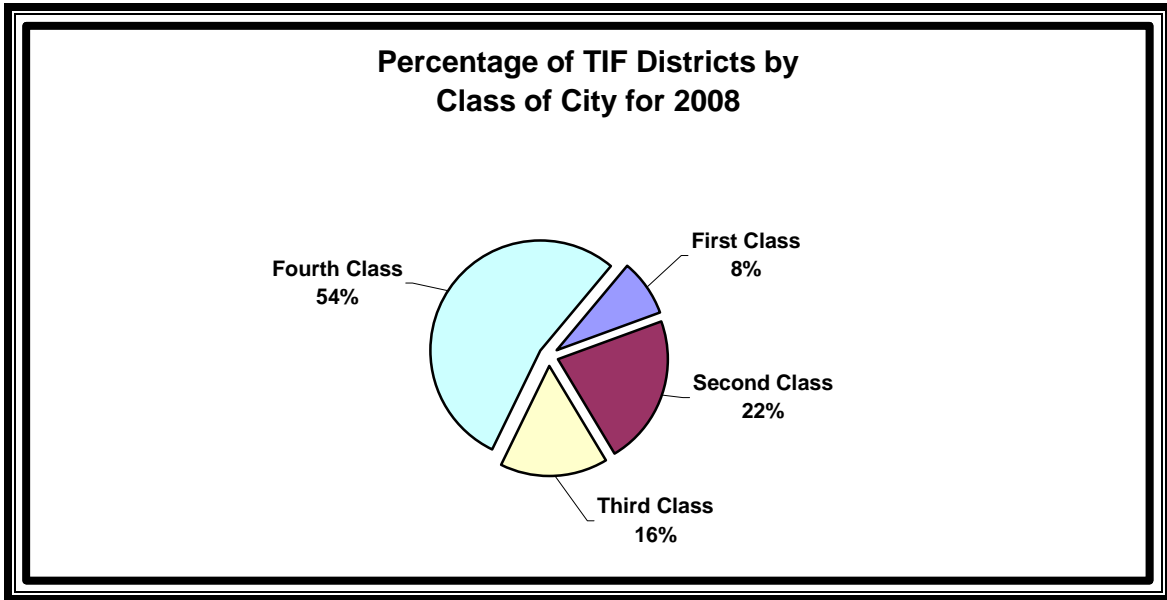


Figure 8.

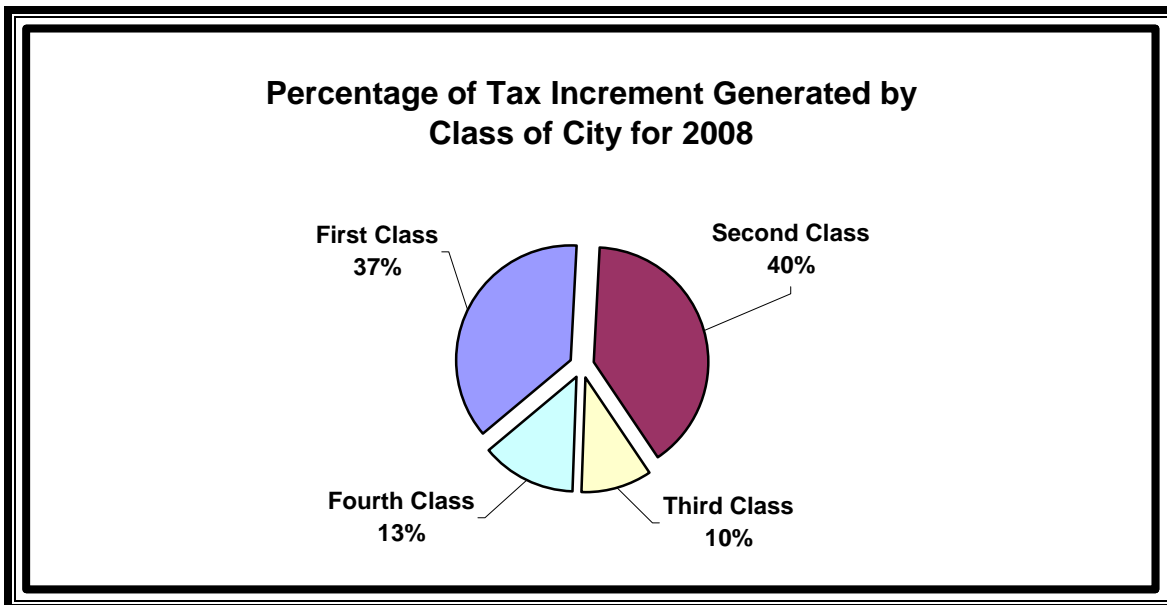


Figure 8 shows that approximately 77% of the tax increment generated for 2008 was generated from districts located within first- and second-class cities.³⁰

Figure 9 identifies TIF districts by Regional Development Commission (RDC). TIF districts are concentrated in the central and southern development regions of the state, with the largest concentration of districts located in Region 11, which is the Metro Area.

Figure 9.

TIF District Type by Region for Calendar Year 2008									
Regional Development Commission	Region	Total Districts	Pre-1979	Redevelopment	Renewal & Renovation	Housing	Economic Development	Soils Condition	Uncodified
Northwest RDC	1	42	1	15	0	22	4	0	0
Headwaters RDC	2	18	0	5	0	11	2	0	0
Arrowhead RDC	3	99	5	47	0	30	15	2	0
West Central Initiative Fund	4	180	1	75	0	59	45	0	0
Region 5 RDC	5	143	0	54	1	44	44	0	0
Mid-Minnesota Valley RDC	6E	62	0	23	0	15	24	0	0
Upper Minnesota Valley RDC	6W	41	1	23	0	6	11	0	0
East Central RDC	7E	83	1	34	3	22	23	0	0
Region 7W	7W	209	2	81	2	39	85	0	0
Southeast RDC	8	80	2	40	1	25	12	0	0
Region 9 RDC	9	163	3	71	2	45	42	0	0
Region 10	10	257	2	98	0	85	71	1	0
Metropolitan Council	11	671	29	384	16	142	76	17	7
Total		2,048	47	950	25	545	454	20	7

Tax Increment Revenue by Type of District

The amount of tax increment revenue generated from within a TIF district depends, in part, on the type of the district, the development activity occurring within the district, the length of its term, and the location of the district.

³⁰ The amount of tax increment generated by a development authority within each class of city is an estimate based on the data available to the Office of the State Auditor.

In 2008, redevelopment districts made up 47% of the TIF districts in the state, but generated 65% of the state's tax increment revenues. Economic development districts made up 22% of the state's TIF districts, but generated only 5% of its tax increment revenues.

As shown in Figure 10 below, redevelopment and pre-1979 districts account for 85% of the tax increment generated in 2008. Pre-1979 districts can no longer receive tax increment revenues.

Figure 10.

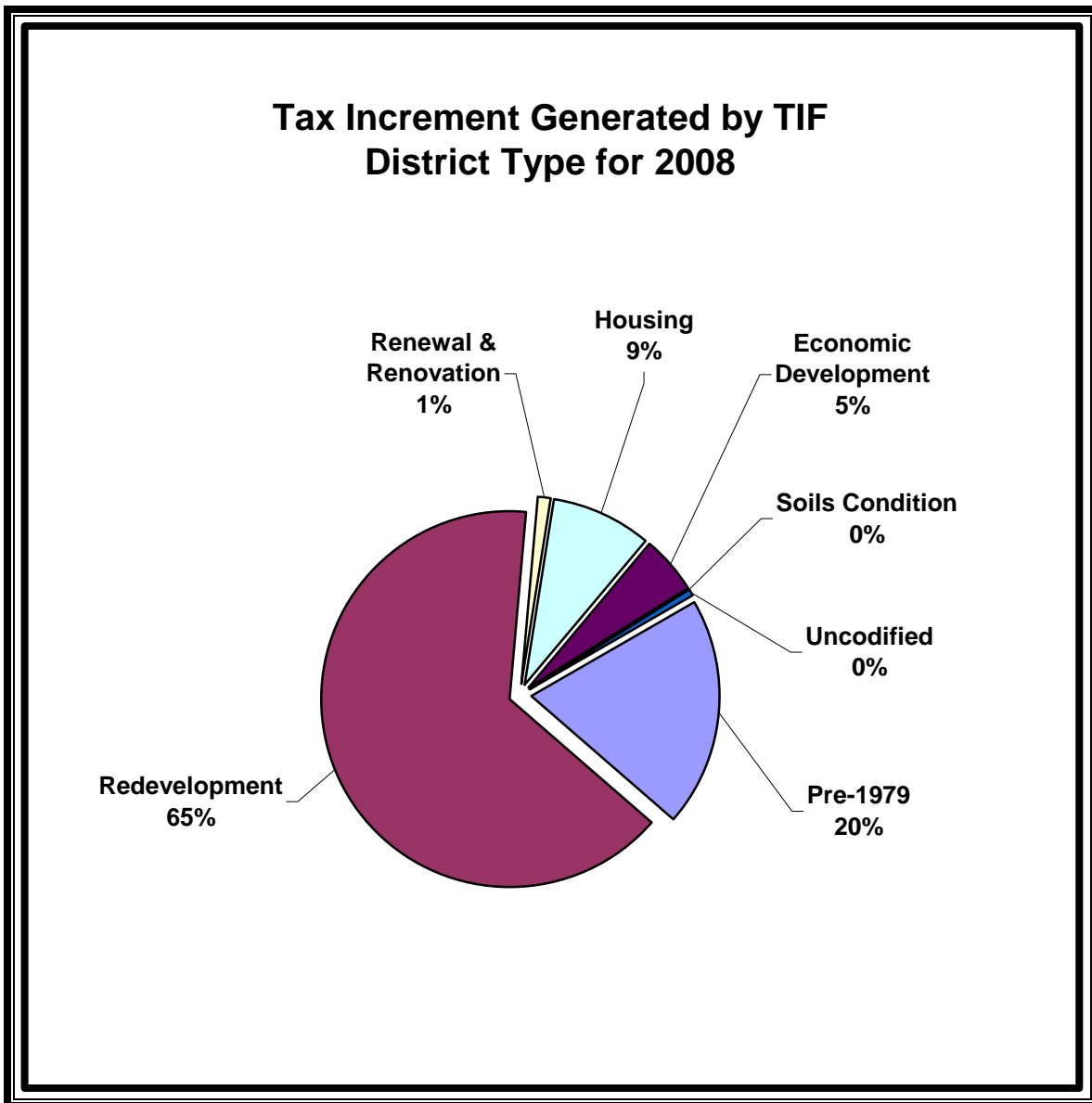


Figure 11.

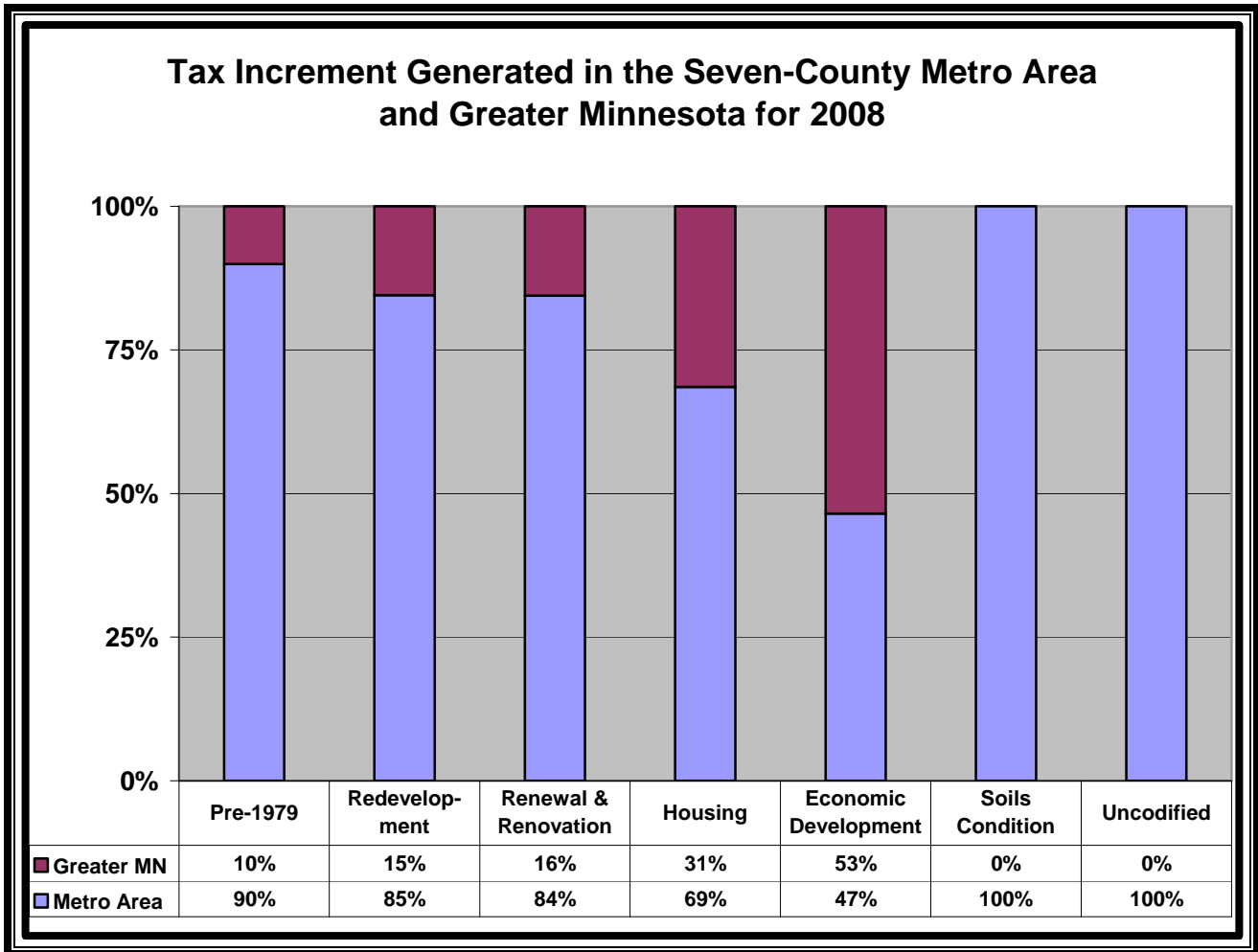


Figure 11 above shows the tax increment generated by district type as a percentage of the total tax increment in the Metro Area and Greater Minnesota. The largest percentage of tax increment generated in economic development districts is generated from districts located in Greater Minnesota. In 2008, 33% of the total number of TIF districts were located in the Metro Area; 67% were located in Greater Minnesota. However, 82% of the tax increment generated in 2008 was from districts located within the Metro Area.

Returned Tax Increment

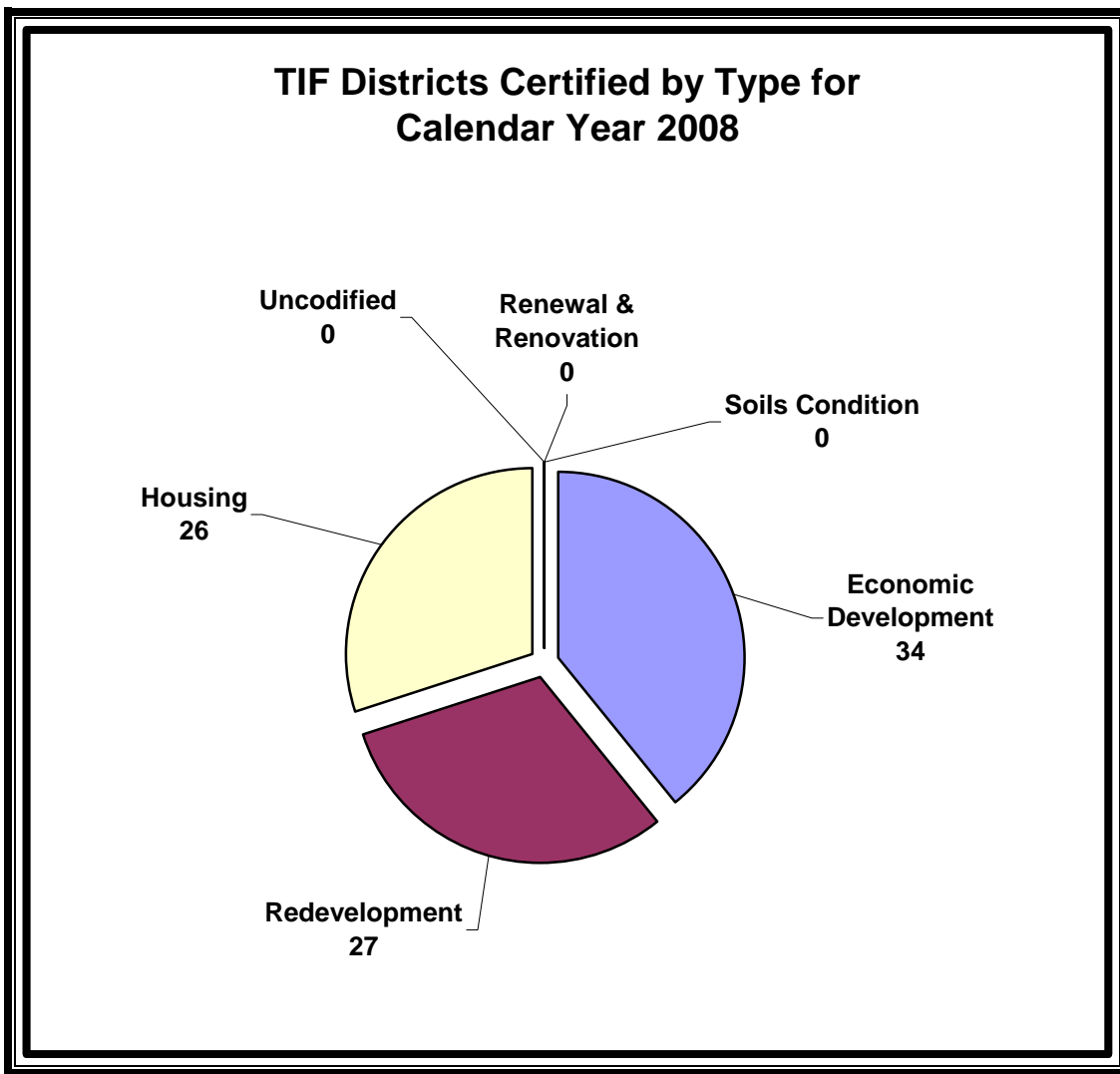
Tax increment revenues may be returned to the county auditor for redistribution to the city, county, and school district as property taxes. Some of the reasons tax increment is returned include receiving excess tax increment and improperly receiving tax increment. In calendar year 2008, development authorities returned \$10,971,913 of tax increment.

Tax increment is returned as a result of both the oversight work of the Office of the State Auditor and voluntary payments made by authorities. From January 1, 1996, to date, a total of more than \$84,228,742 has been paid or returned to county auditors who then redistributed to the cities, counties, and school districts.

Districts Certified for Calendar Year 2008

Once a municipality approves the creation of a TIF district, the county auditor certifies the original net tax capacity.³¹ From the date it is *certified*, the increase in property taxes generated by new development is sent to the TIF authority to pay qualifying development costs. Figure 12 shows TIF district certification by type in 2008.

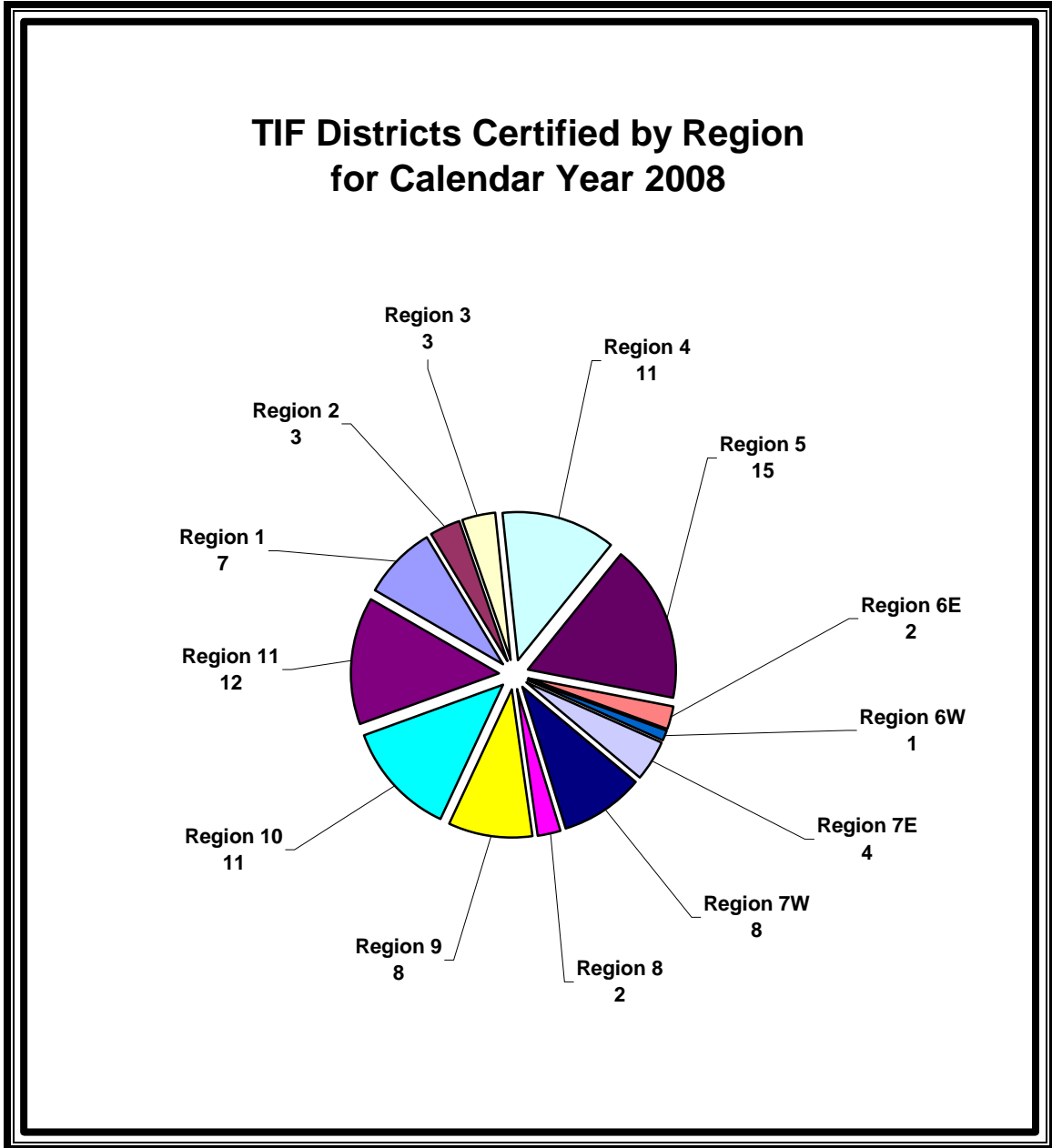
Figure 12.



³¹ Minn. Stat. § 469.177, subd. 1.

Figure 13 below shows that the largest number of new TIF district certifications in 2008 occurred in Region 5.

Figure 13.



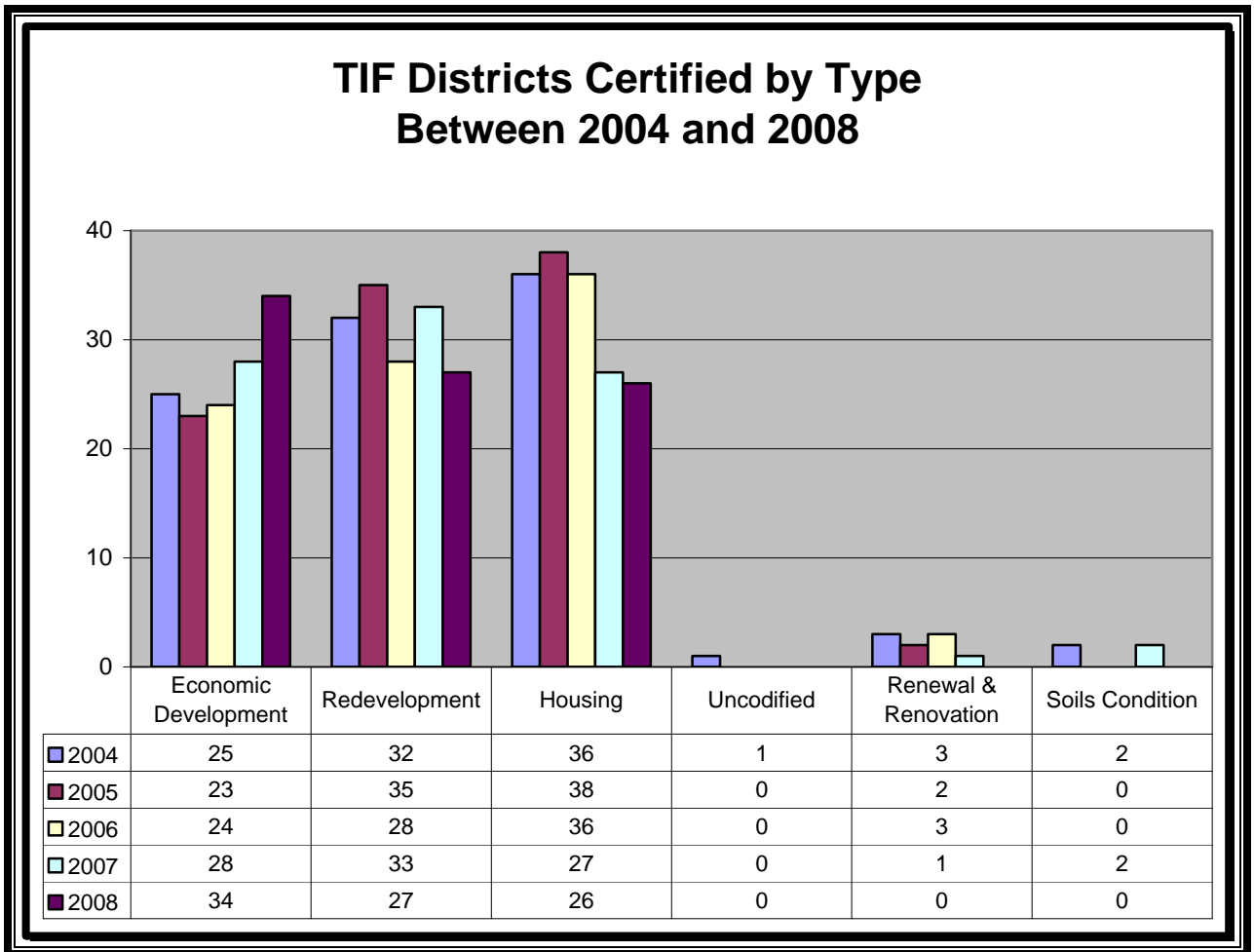
Certification Trends – Five Years

The total number of TIF districts certified between 2004 and 2008 decreased by 14%. The number of economic development districts certified increased by 36% between 2004 and 2008, but increased by 48% between 2005 and 2008. Certification of housing

districts decreased by 28% between 2004 and 2008, and by 32% between 2005 and 2008. The number of redevelopment districts certified decreased 16% overall between 2004 and 2008, with a decrease of 23% between 2005 and 2008.

Figure 14 below compares the TIF districts certified by type since 2004. When examining trends over the five-year period between 2004 and 2008, the number of economic development districts increased, while the number of housing districts declined. Over the same period, redevelopment districts showed no consistent trend.

Figure 14.



Districts Decertified for Calendar Year 2008

After the TIF district’s statutory time expires and the development costs are paid, the district is *decertified*, and all future taxes are redirected to the county, city, and school district as property taxes, thereby increasing the local tax base. As Figure 15 on the following page shows, of the districts decertified in 2008, most were economic development districts.

Figure 15.

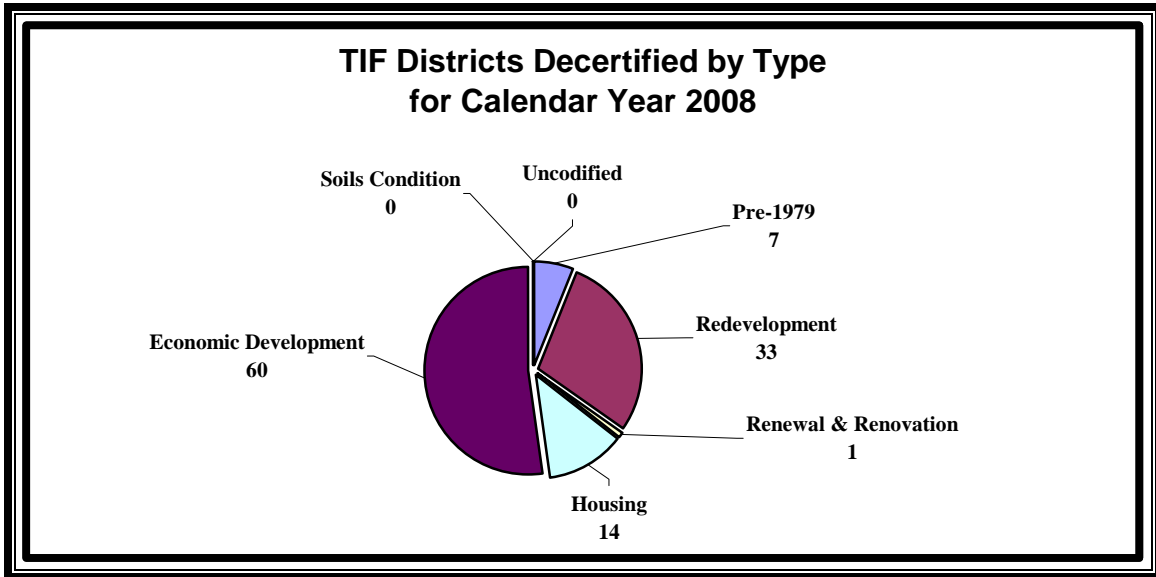
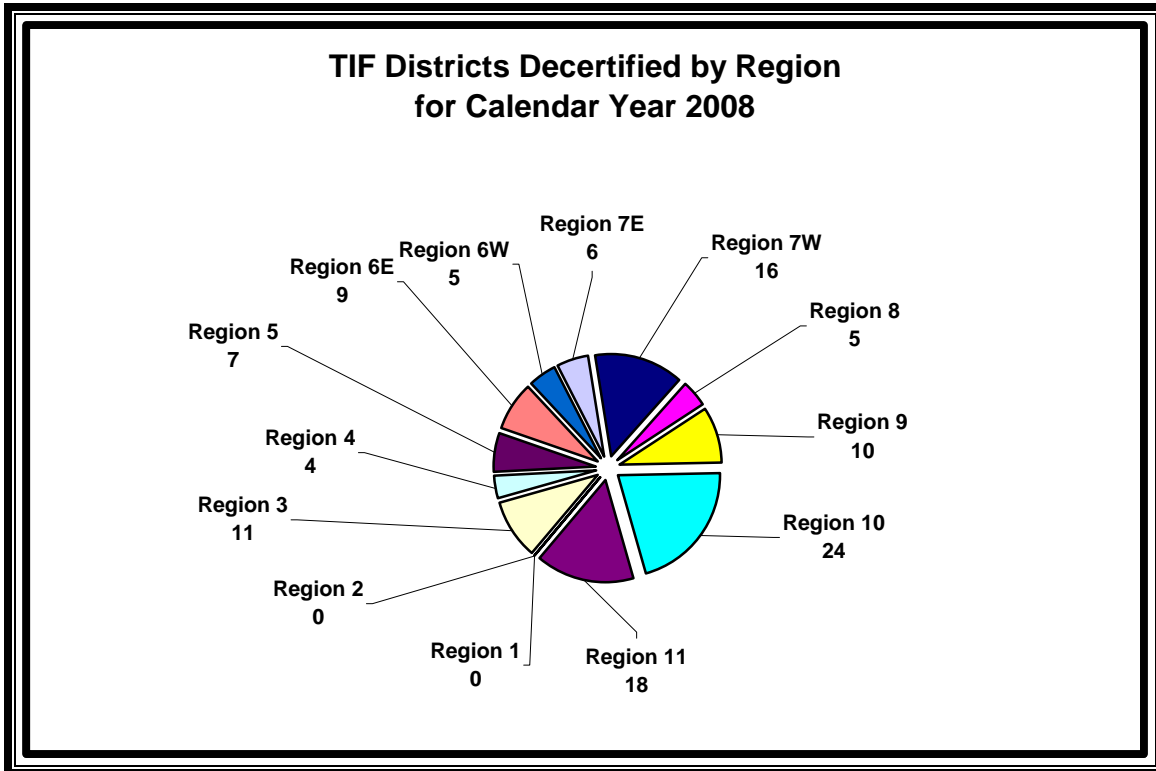


Figure 16 shows that the TIF districts decertified in 2008 were spread evenly among the various regions of the state, with the largest number of decertifications in Region 10.

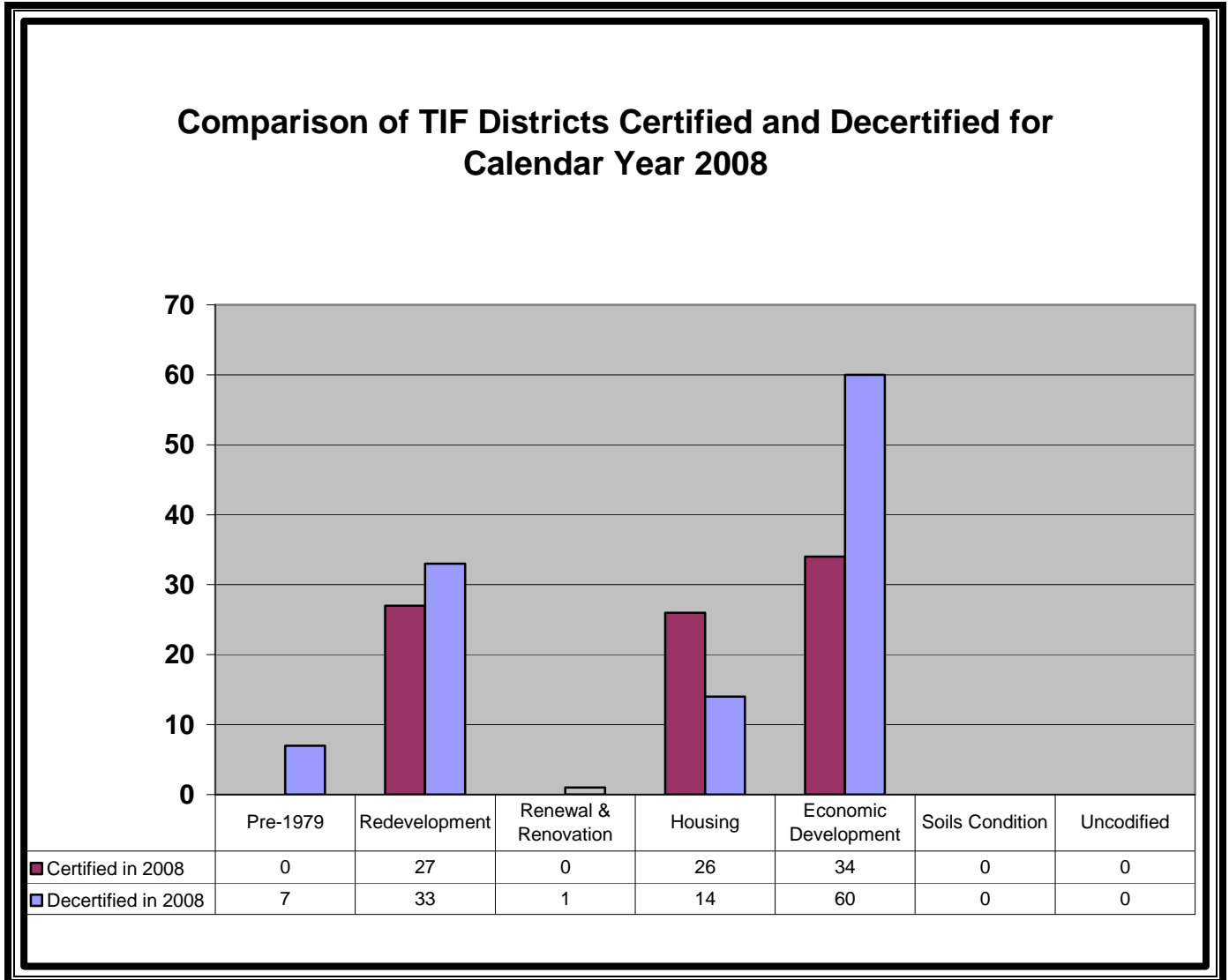
Figure 16.



Comparison of TIF Districts Certified and Decertified

Eighty-seven TIF districts were certified in Minnesota during calendar year 2008. One hundred fifteen TIF districts were decertified during the same year. Figure 17 compares the number of districts certified and the number of districts decertified in 2008 by type of TIF district.

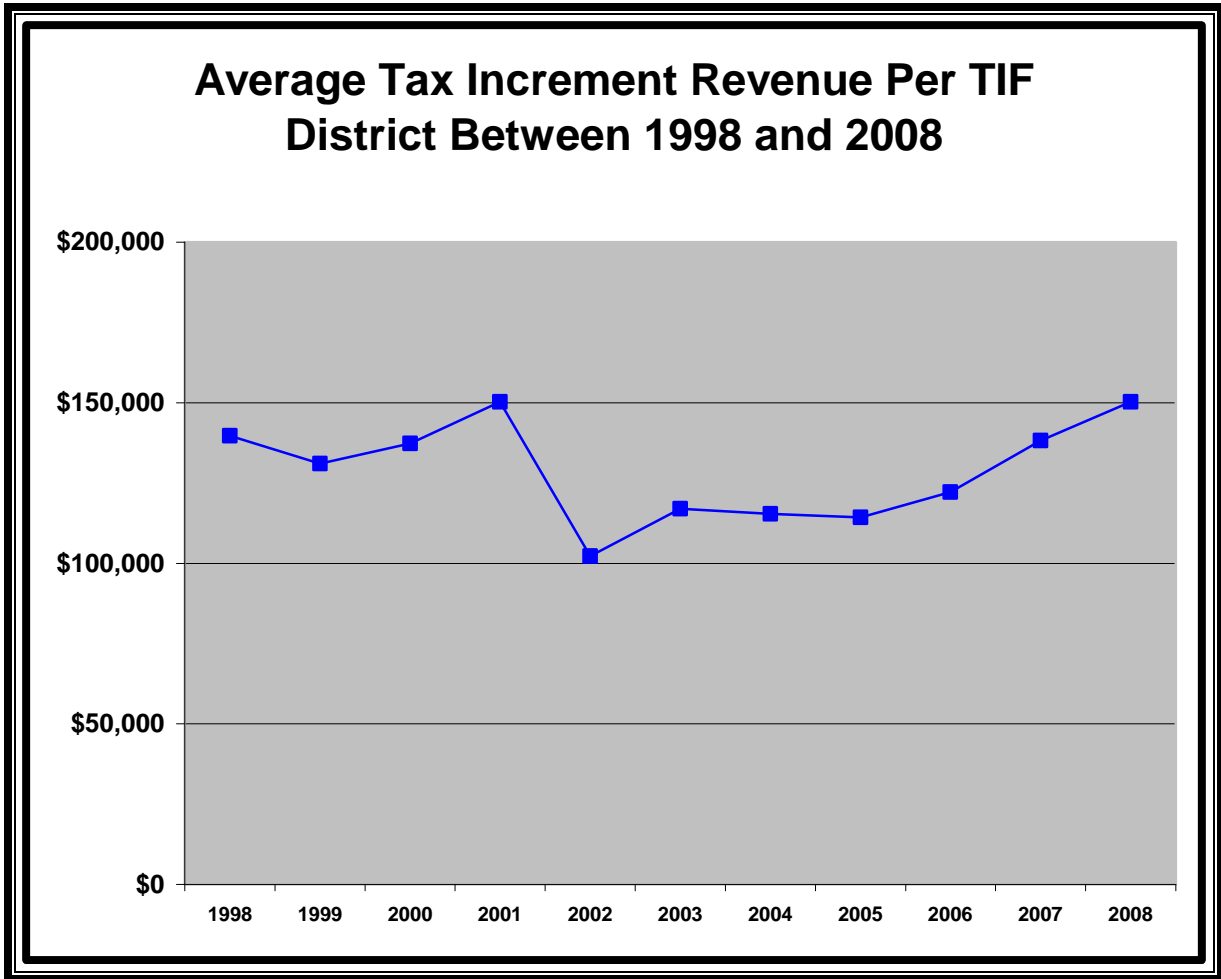
Figure 17.



Ten-Year Trends

Figure 18 shows the average amount of tax increment revenue per TIF district over the ten-year period of 1998 through 2008.

Figure 18.



In 2002, tax increment revenues declined sharply. The decline was likely the result of the 2001 Tax Reform Act, in which the property taxes from the commercial and industrial property taxes portion of the school district were redirected to the state. These property taxes were no longer available for use by development authorities. Other factors, such as the decertification of large, pre-1979 districts, may have also played a role starting in 2001. However, after about three years of slow growth, tax increment revenues appear to be on the rise. The increase in local property taxes could be a factor in the increase of tax increment generated.

As shown in Figure 19 below, the total number of TIF districts was on the rise until 2004, when a decline began. The reasons for the decline in the number of TIF districts could be the result of the decertification of older districts and the declining number of districts certified each year.

Figure 19.

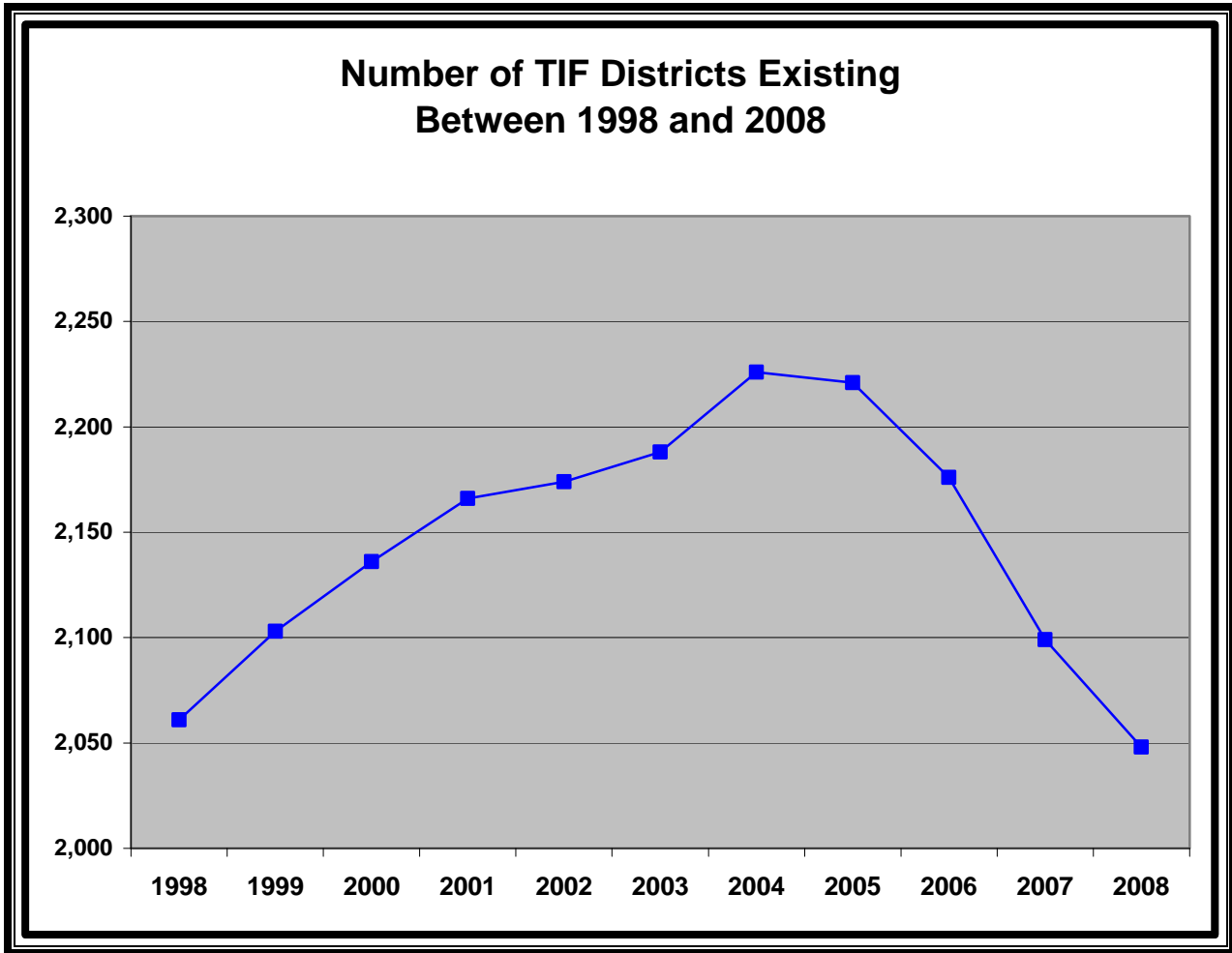
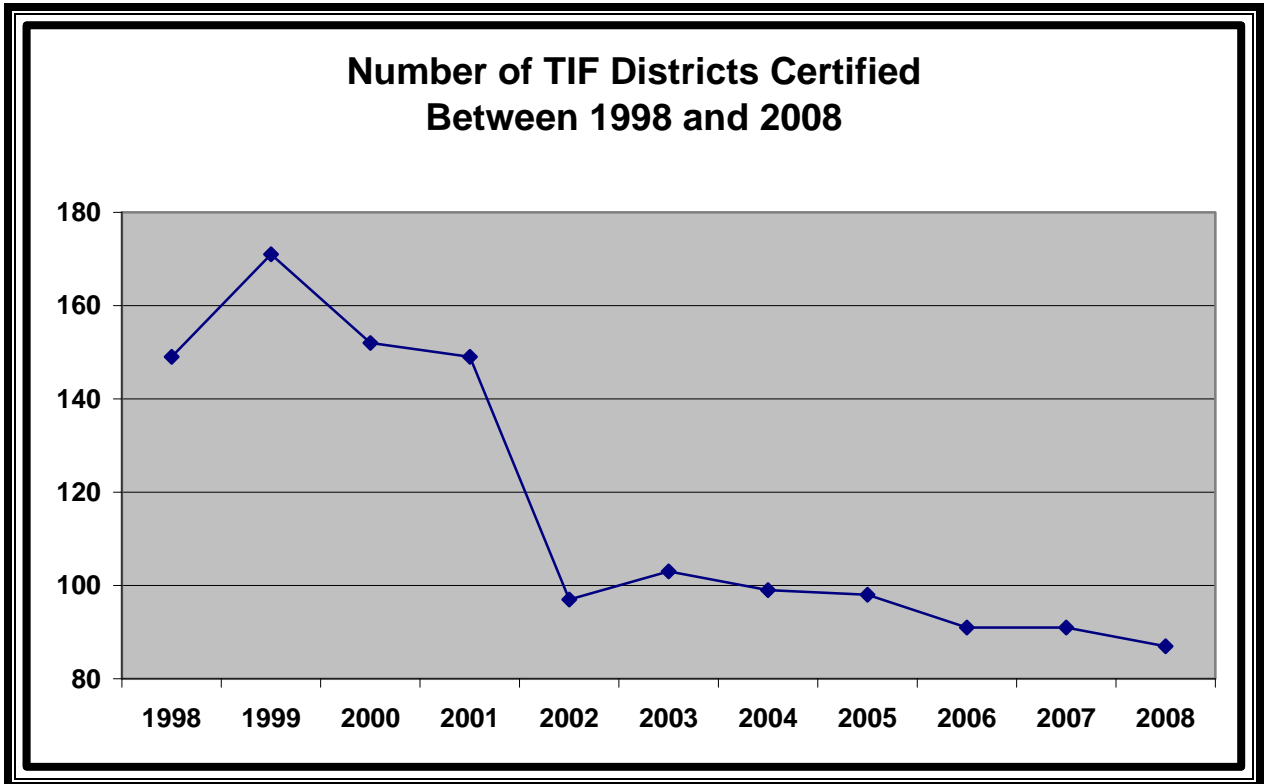


Figure 20 on the following page shows the number of TIF districts certified over the last ten years. The number of districts certified dropped sharply from 2001 to 2002. The sharp drop was likely due to the 2001 changes to the property tax laws. Because the new laws made less money available, fewer districts were certified. While there was a slight increase in 2003, the number of districts certified has continued to decrease. Over the ten-year period covering 1998 through 2008, the number of districts certified has declined approximately 42%.

Figure 20.



2008 REVENUES

Development authorities receive revenues from a variety of financing sources. Revenues may include, among other funding sources: (i) local, state, and federal grants; (ii) special assessments; (iii) loans; (iv) bond proceeds; (v) interest earned on invested funds; (vi) sales and lease proceeds; (vii) market value homestead credits; and (viii) tax increment revenues.³²

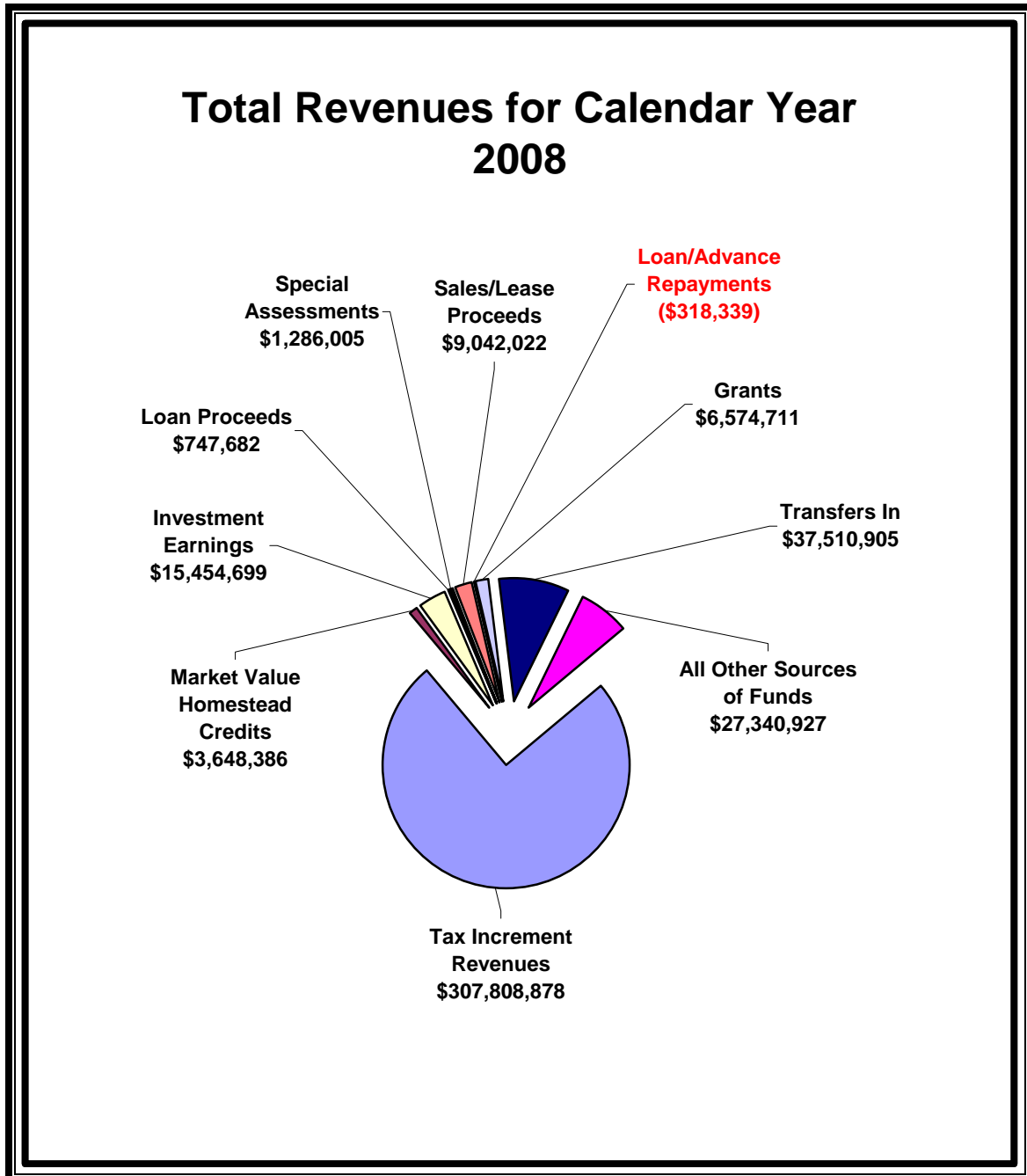
The way in which revenues are reported can be confusing. The nature of generally accepted accounting principles results in some revenues of a project being accounted for twice. For example, a bond may be issued to pay for the authorized costs of a project, and tax increment revenue is then used to pay the principal and interest payments on the bond, and both appear in the TIF reports. To identify revenues without accounting for both bond proceeds and the expenditure of tax increment revenues for payment of bonded indebtedness, bond proceeds have been removed from Figure 21.

Three other categories listed in Figure 14, loan proceeds, loan/advance repayments, and transfers in, include forms of indebtedness for which tax increment revenues were expended for repayment, resulting in revenues being accounted for twice. Because it is

³² Interest earned on invested funds, sales and lease proceeds, and market value homestead credits are often characterized as tax increment revenues.

not possible to ascertain from the reports the extent to which tax increment revenues were expended to repay such indebtedness, these three categories were not removed from Figure 21.

Figure 21.³³



³³ The negative amount listed for loan/advance repayments was due to a detailed and well-documented re-classification of revenue by the Duluth Seaway Port Authority in 2008.

Revenue by Region

Figure 22 shows the amount of tax increment generated by region. A substantial share is generated in the Metro Area. Minneapolis and St. Paul are the most fully-developed and densely-populated cities in the state. The Metro Area (Region 11) generates the largest amount of tax increment per district, due in large part to the higher property tax values, density, and size of development.

Figure 22.

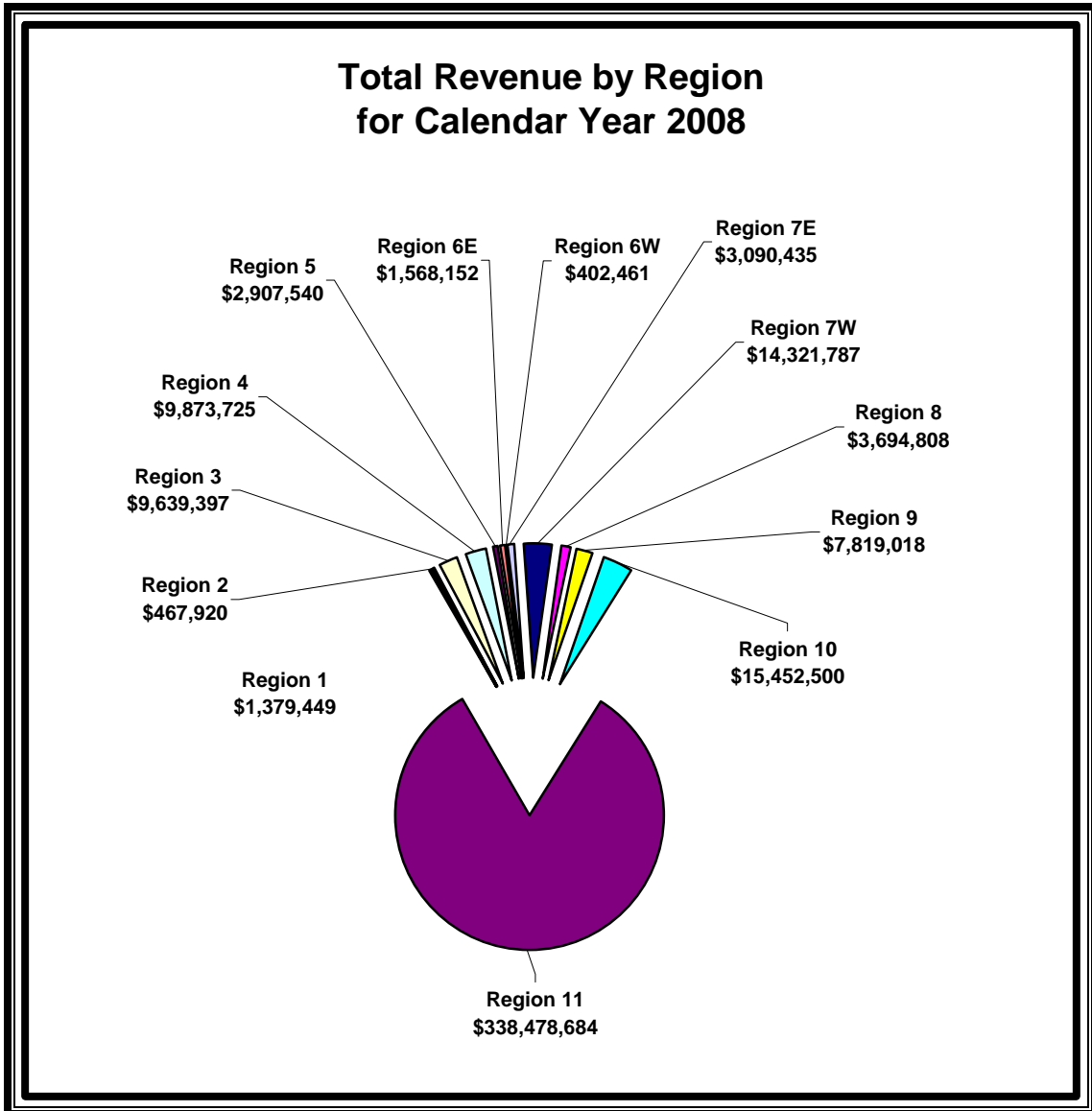
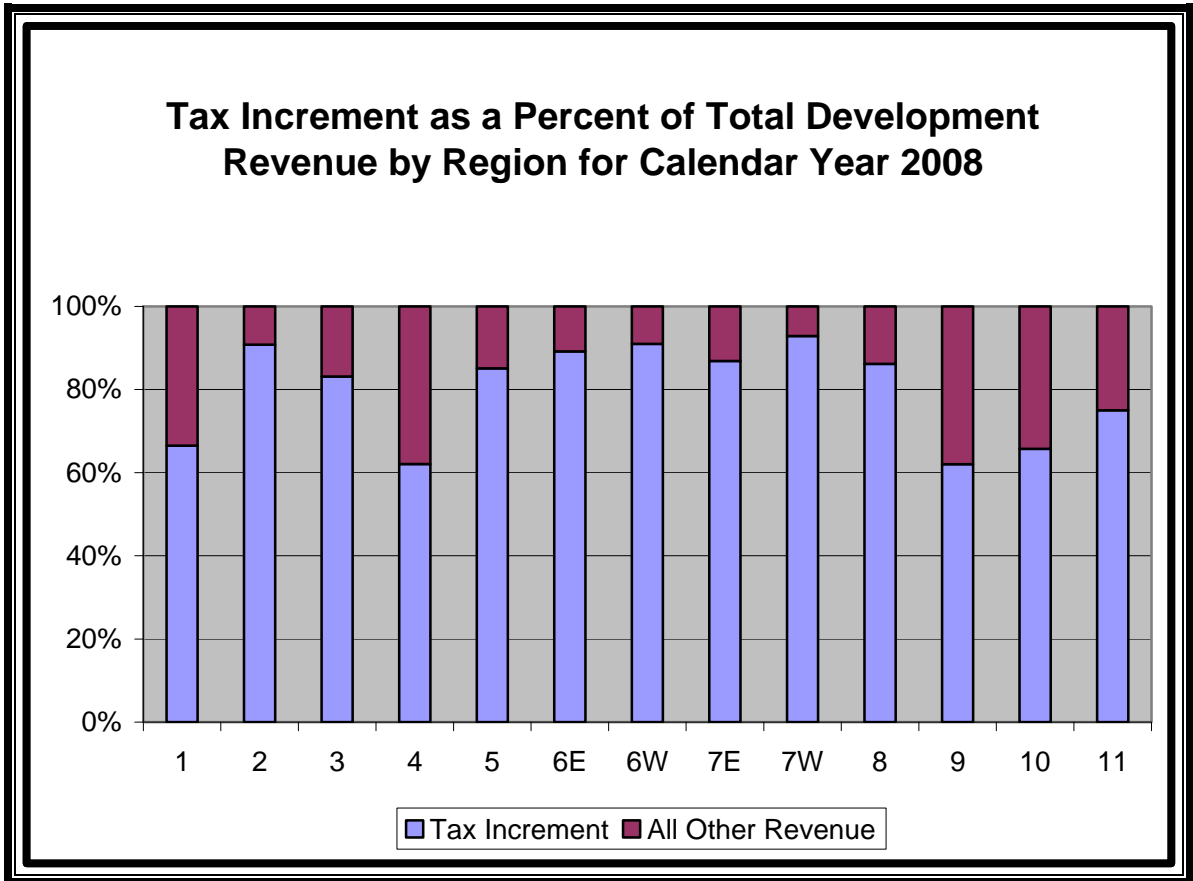


Figure 23 illustrates tax increment revenues generated in calendar year 2008 as a percent of total revenues.

Figure 23.



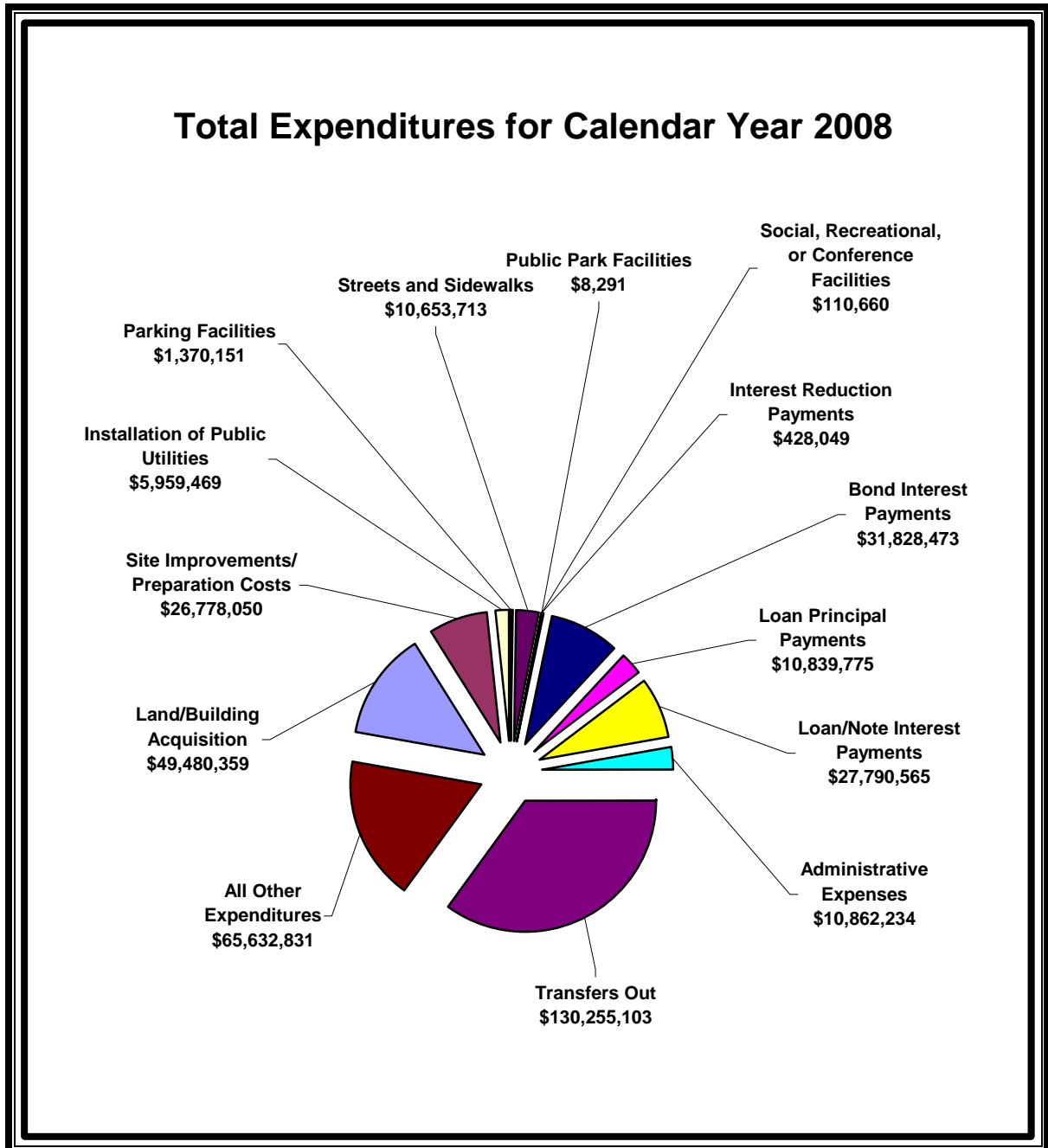
2008 EXPENDITURES

Expenditures for development activity must be made within limits set by state law. Tax increment revenues must be expended only as permitted in the underlying development authority and in the TIF Act.

As with revenues, the way in which expenditures are reported can be confusing. The nature of generally accepted accounting principles results in some costs of a project being accounted for twice. The information contained in the TIF reports includes both the authorized costs of a project and the costs associated with debt service (principal and interest). To identify expenditures without accounting for both the costs of the development activity and the costs associated with debt incurred to cover the costs of the development activity, bond principal payments have been removed from the table above and the two charts that follow. Two other categories listed in Figure 24 -- loan principal payments and transfers out -- include substantial indebtedness for which tax increment revenues were expended for repayment. Since it is not possible to ascertain from the reports the extent to which tax increment revenues were expended to repay such indebtedness, those two categories were not removed.

Figure 24 below identifies the type of expenditures made by development authorities for calendar year 2008.³⁴

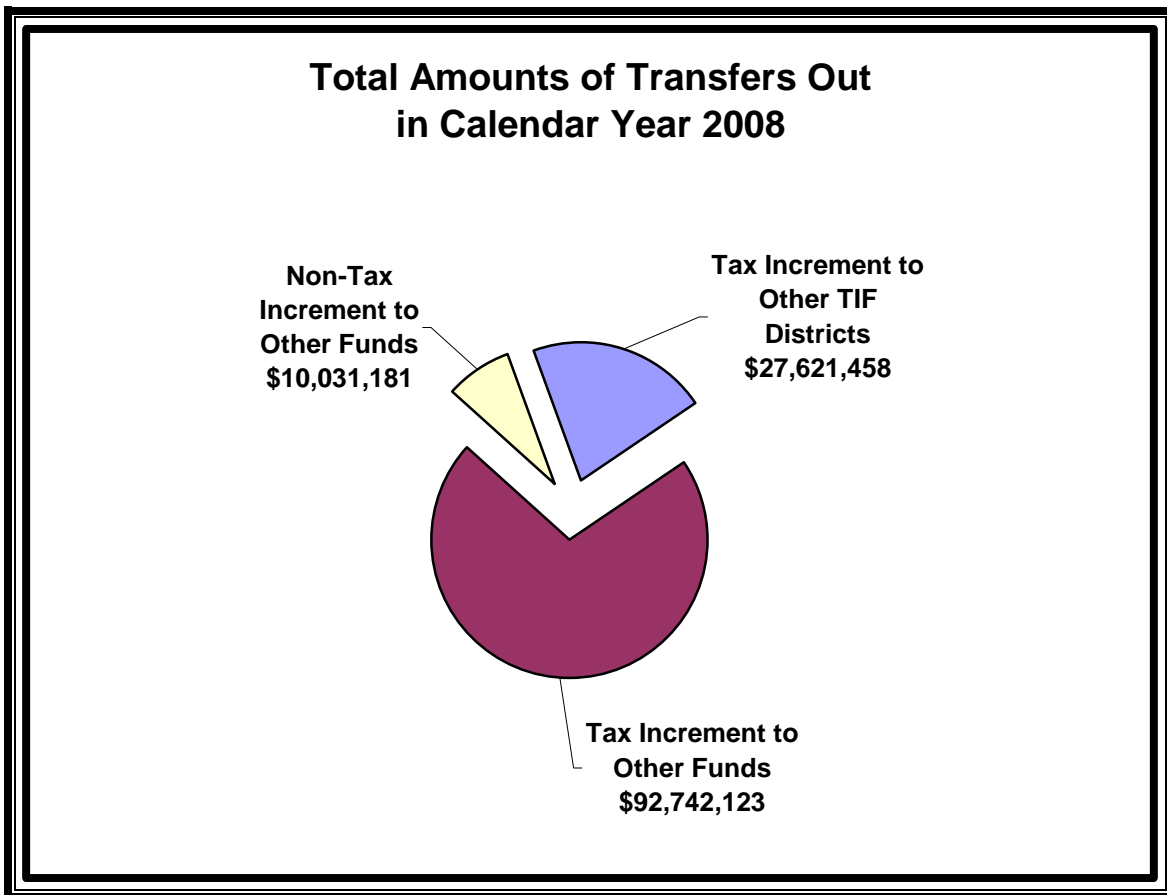
Figure 24.



³⁴ Expenditures for public park facilities and public social, recreational, or conference facilities are no longer an authorized use of tax increment. However, there are some obligations that were incurred when the use of tax increment was authorized for these purposes that remain outstanding.

As noted in Figure 24, the largest expense in 2008 was for transfers out of the TIF districts. Transfers out can be divided into three categories: transfers of tax increment to other funds, transfers of tax increment to other TIF districts, and transfers of non-tax increment to other funds. Figure 25 below identifies the amounts transferred out of the TIF districts by category.

Figure 25.



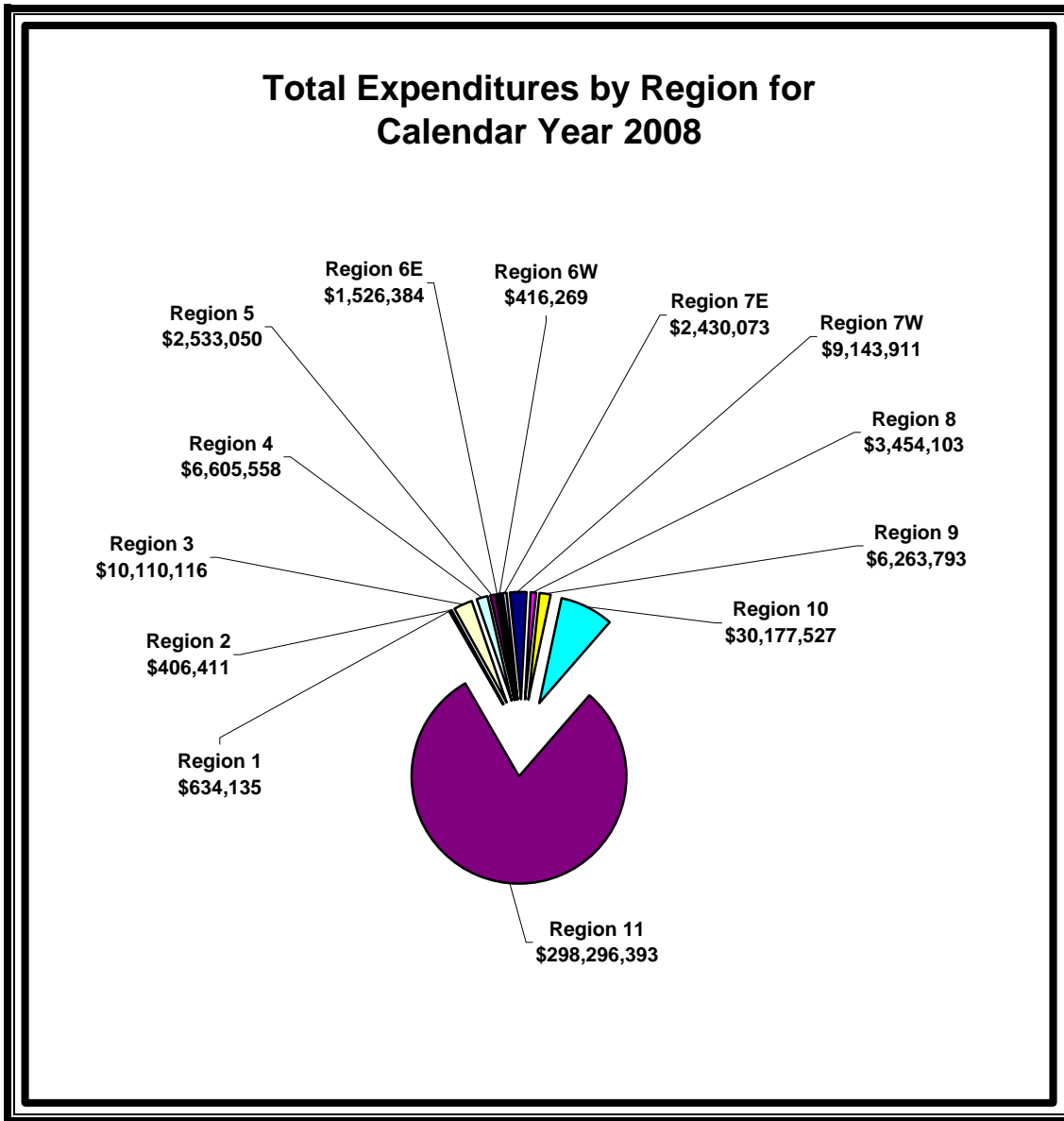
The amount of tax increment transferred to other TIF districts accounted for approximately 21% of the total \$130,394,762 transferred out in calendar year 2008. Very often, these transfers were made to offset deficits in the receiving TIF district(s), or to assist in paying outstanding expenses in the receiving TIF district(s).

The amount of tax increment transferred out to other funds was 71% of the total. The vast majority of these transfers were made to make debt service payments on outstanding debt. For example, Minneapolis accounted for 72% of the \$92,742,123 of tax increment transferred to other funds. Minneapolis transferred tax increment for debt service payments.

The final eight percent of the transfers out were transfers of non-tax increment revenue to other funds. The non-tax increment revenue includes revenue from such things as special assessments and grants.

Figure 26 below shows the total expenditures by region.

Figure 26.



THE TIF ACT AND COMPLIANCE SUPPORT

The TIF Act has been amended frequently since its creation in 1979. Changes in the law have created an added layer of complexity. A TIF district is usually governed by the laws in effect in the year in which the request for certification of the district was made.

The Office of the State Auditor holds annual TIF training sessions and workshops to assist development authorities and municipalities with TIF Act compliance issues. Figure 27 shows the TIF training events held by the Office of the State Auditor in 2009.

Figure 27.

TIF Training Events Held in 2009			
<u>Location</u>	<u>Type</u>	<u>Date</u>	<u>Registered Participants</u>
Lyon County	Workshop	June	20
Clearwater County	Workshop	June	27
Duluth	Workshop	June	33
Fillmore County	Workshop	June	22
Arden Hills	Workshop	July	46

FINDINGS AND RESPONSES

The Office of the State Auditor conducts informal reviews and limited audits of development authorities. After the completion of a TIF audit, if an authority is not in compliance with the TIF Act, an initial notice of noncompliance (Initial Notice) is sent to the governing body of the municipality that approved the TIF district in which the violation arose. The Initial Notice provides the findings, the basis for the findings, and describes the possible consequences of the noncompliance.

The municipality is required by law to respond in writing within 60 days after receiving the Initial Notice. In its response (Response), the municipality must state whether it accepts the findings, in whole or in part, and indicate the basis for any disagreement with the findings. After consideration of the municipality's Response, the Office of the State Auditor submits its final notice of noncompliance (Final Notice) to the municipality. The Office of the State Auditor forwards information regarding unresolved findings of noncompliance to the appropriate county attorney who may bring an action to enforce the TIF Act.³⁵

If the county attorney does not commence an action against the authority within one year after receiving a referral of a Final Notice, and the matter is not otherwise resolved to the Office of the State Auditor's satisfaction, the Final Notice is referred to the Attorney General. If the Attorney General finds that the authority violated a provision of the TIF Act, and the violation was substantial, the Attorney General will commence an action in the tax court to suspend the use of TIF by the authority. Before commencing the action in the tax court, however, the Attorney General must attempt to resolve the dispute using

³⁵ All information and communications remain confidential until the Final Notice is submitted. Minn. Stat. § 6.715.

appropriate alternative dispute resolution procedures. If the Attorney General commences an action and the tax court finds that the authority violated the TIF Act, and the violation was substantial, the tax court may suspend the use of TIF by the authority for a period of up to five years.³⁶

Summary of Findings and Responses

State law requires the Office of the State Auditor to provide a Summary of the Responses it received from the audited municipalities and copies of the Responses themselves to the chairs of the legislative committees with jurisdiction over tax increment financing.³⁷ This section of the report summarizes the various TIF legal compliance audits and investigations concluded as of December 31, 2009. Audits were completed, and Initial Notices and Final Notices were sent to the following municipalities:

1. St. Paul Port Authority – An Initial Notice was sent on September 22, 2009. A Final Notice was sent on November 25, 2009.
2. City of West St. Paul – An Initial Notice was sent on July 13, 2009. A Final Notice was sent on September 25, 2009.

Complete copies of the Initial Notices and Final Notices and the municipalities' Responses are provided at the end of this report.

Improper Expenditures of Tax Increment

City of West St. Paul

TIF District 3

In the Initial Notice, the Office of the State Auditor found that the City spent \$3,440.05 of tax increment in violation of the TIF Act. In its Response, the City stated it did not agree with the finding, but felt the amount was not significant. The City has returned \$3,440.05 to Dakota County. In the Final Notice, the Office of the State Auditor considered this finding resolved.

³⁶ Minn. Stat. § 469.1771, subd. 2b(c).

³⁷ Minn. Stat. § 469.1771, subd. 1(c).

Failure to Comply with Special Legislation

St. Paul Port Authority

Williams Hill TIF District

In the Initial Notice, the Office of the State Auditor found that the Port Authority failed to comply with Section 469.1782, subdivision 2 and, therefore, the maximum two-year extension of the duration limit was deemed disapproved.

In its Response, the City agreed with the finding, stating, “the mechanism to implement the special legislation was inadvertently not followed by the Saint Paul Port Authority, and as such, did not become effective.” The City stated it was working with the county to verify the initial tax payments to the district related to the Hazardous Substance Subdistrict (HSS). This reclassification of the initial tax payments should result in no need for the special legislation.³⁸

In the Final Notice, the Office of the State Auditor reiterated its finding that the maximum two-year duration limit extension authorized in the special legislation was disapproved. The Office of the State Auditor agreed that, if the initial tax payments are classified as HSS increment, the special legislation is no longer needed. No further action was required.

Failure to Comply with Public Hearing Requirements

St. Paul Port Authority

Williams Hill TIF District

In the Initial Notice, the Office of the State Auditor found that the Port Authority failed to comply with the public hearing requirements when trying to add property to the district and hazardous substance subdistrict.

In its Response, the City stated that, based upon the information subsequently provided to the Office of the State Auditor, it was the City’s understanding that the issue had been resolved.

In the Final Notice, the Office of the State Auditor acknowledged receipt of additional information in which it appeared that the parcel issue had resulted from a scrivener’s error, and no additional area was added to the District or HSS. Therefore, this finding was considered resolved.

³⁸ Minn. Stat. § 469.176, subd. 1b(d).

APPENDIX A

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REBECCA OTTO
STATE AUDITOR

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state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

September 22, 2009

The Honorable Chris Coleman, Mayor
The Honorable Dan Bostrom, Council Member
The Honorable Melvin Carter, Council Member
The Honorable Patrick Harris, Council Member
The Honorable Lee Helgen, Council Member
The Honorable Kathy Lantry, Council Member
The Honorable Russ Stark, Council Member
The Honorable Dave Thune, Council Member

City of St. Paul

15 Kellogg Blvd W, Rm 110
Saint Paul, MN 55102-1606

Re: Port Authority TIF District Williams Hill – Initial Notice

Dear Mayor Coleman and Council Members:

In May/June of 2009, the Office of the State Auditor (OSA) performed an examination of certain records of two tax increment financing districts (TIF Districts) of the Saint Paul Port Authority (PA) located in the City of St. Paul (City). The audit (Audit) covered the Energy Lane Business Center and the Williams Hill TIF Districts. Both districts are currently active.

The Audit examined, on a test basis, evidence supporting the PA's compliance with the TIF Act.¹ The OSA reviewed and/or tested the TIF Districts' reports filed with the OSA through the year ended December 31, 2007, TIF plans, general ledgers, invoices, and other supporting documents. No findings were made in the audit of the Energy Lane Business Center. The examination resulted in two findings of noncompliance with state law in the Williams Hill TIF District (the "District"). This Initial Notice of Noncompliance (Initial Notice) contains those two findings.

State law requires the City to respond in writing to the OSA within 60 days after receipt of this Initial Notice. The Response must state whether the City accepts the findings, in whole or in part, and must indicate the basis for any disagreement. At the conclusion of the Audit, if the findings remain unresolved, a Final Notice of Noncompliance (Final Notice) will be submitted to the City. If the OSA finds that the PA has violated a provision of the TIF Act for which a remedy is provided, the relevant information will be forwarded to the Ramsey County Attorney for review.²

¹ See Minn. Stat. §§ 469.174 to 469.1799, as amended.

² See Minn. Stat. § 469.1771, subdivision 1 (b).

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Mayor and Council, City of Saint Paul
September 22, 2009
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All data relating to this Audit, including this Initial Notice and the City's response (Response), are not public until the OSA has issued its final report.³

FINDING OF NONCOMPLIANCE

Findings of noncompliance regarding the District are as follows:

Finding 1. Failure to Comply with Special Legislation

The Laws of Minnesota for 1999, Chapter 243, Article 10, Section 20, City of Saint Paul (Special Legislation), reads:

Subdivision 1. **DELAY OF DEEMED COMMENCEMENT OF TAX INCREMENT FINANCING DISTRICT.** Notwithstanding Minnesota Statutes, section 469.176, or any other law to the contrary, the duration limit of the Williams Hill tax increment district in the city of St. Paul is determined as if the date of receipt of the first tax increment by the authority occurs when the aggregate of all tax increments received from the district reaches \$2,000. In no case may the duration limit of the district be extended by more than two years.

Subdivision 2. **EFFECTIVE DATE.** This section is effective upon approval by and compliance with Minnesota Statutes, sections 469.1782, subdivision 2, and 645.021, subdivision 3, by the governing body of the city of St. Paul.

Based on information submitted during the Audit, it was determined that the PA complied with Minn. Stat. § 645.021, subd. 3, as required by the Special Legislation. However, the PA did not comply with section 469.1782, subdivision 2, also required by the Special Legislation, and which reads as follows:

Local approval of special laws. (a) If a special law allows an extension of the duration limit of an existing tax increment financing district under section 469.176 or allows establishment of a new district with a longer duration limit than that permitted by general law, the "affected local government units," for purposes of section 645.021 and article XII, section 2, of the Minnesota Constitution, include the city or town, the school district, and the county in which the tax increment district is located. The town board may act to approve the special law.

(b) The chief clerical officer of the municipality must, as soon after the affected

³ See Minn. Stat. § 6.715 (During an audit, the information is confidential and/or nonpublic until the audit is complete); Minn. Stat. §13.03, subdivision 4 (c) (to the extent data is sent to another government entity, the data retains the same classification).

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local units have approved the special law allowing an extension, file with the secretary of state a certificate stating the essential facts necessary to valid approval, including a copy of each of the resolutions of approval by the city or town, the school district, and the county. The attorney general shall prescribe the form of the certificate and the secretary of state shall furnish copies. If the municipality fails to file a certificate of approval before the first day of the next regular session of the legislature, the extension of the duration is deemed to be disapproved, unless the special law allows a longer period for approval. If the law contains other provisions besides an extension of the duration and the municipality otherwise complies with section 645.021, the rest of the law takes effect.

The PA did not provide the OSA with the certificate or the resolutions of the school district and the county (County) evidencing compliance with subdivision 2 of the Special Legislation. According to discussions with the PA, it did not solicit the resolutions from the affected local government units.⁴ We find that the PA failed to comply with Section 469.1782, subdivision 2. The maximum two-year extension of the duration limit is deemed disapproved.

Finding 2. Failure to Comply with Public Hearing Requirements

The District and its hazardous substance subdistrict (HSS) can be enlarged only after there has been discussion, a public hearing, and findings, as required for approval of the original plan for the District.⁵

On July 10, 1997, the PA sent revised parcel lists to the County and stated that Parcel No. 31-29-22-14-0031 (Parcel 31) had been added to both the District parcel list and to the HSS parcel list. No evidence of notice, a public hearing or findings was provided to the OSA.

On February 5, 1999, a letter from the Property Records and Revenue Department of the County informed the PA that the original net tax capacity of Parcel 31, among other parcels, had been certified.

The PA did not provide the OSA with the required documentation evidencing a notice, a public hearing and findings made prior to the request of the PA to include Parcel 31 in the District and the HSS. We find that the PA failed to comply with the public hearing requirements.

4 It appears the first receipt of increment was in 1998 and, as such, the maximum duration limit of the Williams Hills TIF district is 12/31/2023 (1998 + 25 years).

5 Minn. Stat. § 469.175, subd. 4 (b) (1) (A public hearing is required for the enlargement of a tax increment district); Minn. Stat. § 469.175, subd. 7 (A public hearing is required for enlargement of a hazardous substance subdistrict).

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ADDITIONAL COMMENTS

In addition to the above findings, we are including comments of significance (Comments) to the Audit. Certain irregularities were noted during the Audit, but these concerns did not rise to the level of a finding. The following Comments are meant to inform the PA and the City of these concerns. The Response does not need to include written answers to the Comments.

Comment 1. Certification of the District and the HSS

On November 14, 1996, the PA requested certification of the District. On November 15, 1996, the PA requested certification of the HSS contained therein. According to the certification letters provided, Ramsey County certified only two parcels as being within the District. The two certified parcels were the only two parcels that did not have an HSS. The certification letter from the County asked that the PA “verify that the parcels on the attached list match the property that the Port Authority understands to be in the tax increment district.” No evidence was presented that the PA did verify. The list did not match the list in the TIF plan for the District.

We recommend, in the future, the PA review and verify the certification of parcels by the County. The 24 parcels certified in the HSS should also have been certified as being within the District. An HSS can not be created independently of a TIF district.⁶ Clearly, the District contained more than two parcels.

The reason this issue did not rise to the level of a finding is because the error in classification of parcels was made by Ramsey County. We did not attribute this error to the PA. Tax increment revenues generated from within the District and from within the HSS are subject to different expenditure rules.⁷ For example, tax increment revenues from the District can be used for acquisition of property whereas tax increment revenues from the HSS can not. Red flags would not have been raised about the use of tax increment from the HSS for acquisition of property if Ramsey County had correctly certified the parcels. To sort out which parcels were in the District and which parcels were in the HSS and to attribute the correct tax increment revenues to each, we had to rely on levy sheets subsequently provided to the OSA.

Comment 2. Payment of Tax Increment Prior to Certification of the District

The second comment involves the initial payment of tax increment by the County. The County took over two years (from November 1996 to February 1999) to certify the tax capacities and tax rates of the District and the HSS. Property taxes do not become reclassified as tax increment until after the

6 Minn. Stat. § 469.175, subd. 7.

7 Minn. Stat. §469.176, subd. 4j permits tax increments in a redevelopment district to be used to acquire property. Minn. Stat. § 469.176, subd. 4e does not permit tax increment from an HSS to be used for acquisition of property.

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date of certification of the District. The original net tax capacity and original local tax rate must be known and certified before tax increment can be calculated.⁸ Ramsey County paid tax increment to the PA in calendar year 1998, which was prior to the 1999 certification of the District and certification of the HSS. The payment of tax increment to the PA in 1998, however, started the clock for tolling the twenty-five year term of the District.⁹

Legislation enacted in 2008 now gives authorities the ability, up to a maximum of four years, to elect when it will receive its first tax increments.¹⁰ We recommend, in the future, the PA state in its TIF plans the year it elects to receive a district's first tax increment and communicate the election to Ramsey County.

CONCLUSION

As noted above, the City's Response to the findings must be submitted in writing to the OSA within 60 days after receipt of this Initial Notice. Our TIF Division staff is available to review and discuss the findings at any time during the preparation of the City's Response. After reviewing the Response, we will issue the Final Notice.

If you have any questions, please call me at (651) 296-7979. We look forward to receiving your Response.

Very truly yours,

/s/ Arlin Waelti

Arlin Waelti
Assistant State Auditor
TIF Division Director

cc: Louis F. Jambois, President
Laurie J. Hansen, Chief Financial Officer
Bruce Kessel, Controller

8 Minn. Stat. § 469.177, subdivision 1 and 1a (At the time of certification, the county auditor shall certify the original net tax capacity and original local tax rate. Until certification, these calculations are not known).
9 Laws of 1997, ch. 231, art. 10, section 6, effective for districts with CRDs after June 30, 1997 (No tax increment shall be paid for a redevelopment district after 25 years from the date of receipt of the first increment).
10 Minn. Stat. 469.175, subd. 1 (b), effective for districts, other than economic development districts, for which the request for certification is made after June 30, 2008.

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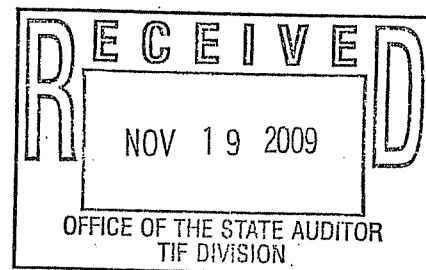
CITY OF SAINT PAUL
Christopher B. Coleman, Mayor

25 West Fourth Street
Saint Paul, MN 55102

Telephone: 651-266-6565
Facsimile: 651-228-3261

November 17, 2009

Arlin Waelti, Assistant State Auditor
TIF Division Director
Office of the State Auditor
Suite 500
525 Park Street
St. Paul, MN 55103-2139



RE: Port Authority TIF District Williams Hill – Initial Notice

Dear Ms. Waelti:

On September 22, 2009, your office sent the City of Saint Paul a letter regarding the Saint Paul Port Authority Williams Hill TIF District Initial Notice. The result of your audit and the initial notice identified two potential findings. This letter is a follow up to that letter.

Finding 1 related to failure to comply with special legislation in 1999. Based upon a review of the legislation and discussions with legal council, it appears that the mechanism to implement the special legislation was inadvertently not followed by the Saint Paul Port Authority, and as such, did not become effective. We will be working with Ramsey County to verify the initial tax payments related to the Hazardous Substance Subdistrict. The net impact of this should result in no need for the special legislation, nor the need for the same statutory decertification date of December 31, 2026 as previously reported.

Finding 2 related to a failure to comply with public hearing requirements. Based upon information that has subsequently been provided to your office, it is our understanding that this issue has been resolved and will no longer be reported as a finding.

It is our understanding that your office will be issuing a final public report that will take into account the above information, resulting in only your initial Finding 1 being reported. If you have any questions, feel free to contact the Port Authority or my office.

Sincerely,


Cecile Bedor
Director

cc: Louie Jambois

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
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(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

November 25, 2009

The Honorable Chris Coleman, Mayor
The Honorable Dan Bostrom, Council Member
The Honorable Melvin Carter, Council Member
The Honorable Patrick Harris, Council Member
The Honorable Lee Helgen, Council Member
The Honorable Kathy Lantry, Council Member
The Honorable Russ Stark, Council Member
The Honorable Dave Thune, Council Member

City of St. Paul

15 Kellogg Blvd W, Rm 110
Saint Paul, MN 55102-1606

Re: Port Authority TIF District Williams Hill – Final Notice of Noncompliance

Dear Mayor Coleman and Council Members:

On September 22, 2009, the Office of the State Auditor (OSA) sent to the City of St. Paul (City) an Initial Notice of Noncompliance (Initial Notice) regarding the Saint Paul Port Authority's (PA) Williams Hill TIF District (the "District"). The OSA received the City's response (City Response) on November 19, 2009, in a letter from Cecile Bedor, Director.

This letter is the Final Notice of Noncompliance (the "Final Notice") of the Office of the State Auditor. It summarizes the initial findings and the City Response, and provides the OSA's final conclusion regarding the issues raised by the review. A detailed discussion of the basis for the findings can be found in the Initial Notice.

FINDINGS OF NONCOMPLIANCE

Finding 1. Failure to Comply with Special Legislation-No Further Action Required

In the Initial Notice, the OSA found that the PA did not provide the OSA with the certificate or the resolutions of the school district and the county evidencing compliance with Minnesota Statute § 469.1782, subdivision 2, and, as such, the maximum two-year duration limit extension authorized in the Special Legislation was disapproved.

In the City's Response, the City agreed with the OSA's finding, stating "the mechanism to implement the special legislation was inadvertently not followed by the Saint Paul Port Authority,

OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Saint Paul
November 25, 2009
Page 2

and as such, did not become effective.” The City stated it was working with Ramsey County to verify the initial tax payments to the District related to the Hazardous Substance Subdistrict (HSS). This reclassification of the initial tax payments should result in no need for the special legislation.¹

Based on the City’s response, the OSA reiterates its finding that the maximum two-year duration limit extension authorized in the Special Legislation was disapproved. The OSA agrees that, if the initial tax payments are classified as HSS increment, the special legislation is no longer needed. No further action is required.

Finding 2. Failure to Comply with Public Hearing Requirements-Resolved

In the Initial Notice, the OSA found that the PA sent revised parcel lists to the County and stated that Parcel No. 31-29-22-14-0031 (Parcel 31) had been added to both the District parcel list and to the HSS parcel list. No evidence of notice, a public hearing or findings was provided to the OSA. The PA subsequently provided information demonstrating that no additional area was added to the District or HSS.²

In the City’s Response, the City stated that, based upon the information that was subsequently provided to the OSA, it is our understanding that this issue has been resolved.

Based on subsequent information provided to the OSA and the City’s Response, it appears the parcel issue resulted from a scrivener’s error and no additional area was added to the District or HSS. Accordingly, a public hearing was not required and the OSA considers this finding resolved.

CONCLUSION

If you have questions, would like additional information, or if we can be of assistance in the future, please do not hesitate to contact me. I can be reached at (651) 296-7979.

Very truly yours,

/s/ Arlin Waelti

Arlin Waelti
Assistant State Auditor
TIF Division Director

1 Minn. Stat. § 469.176, subd. 1b (d).

2 E-mail and attachments from Bruce A. Kessel, Controller, to Kurt Mueller, dated October 9, 2009.

OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Saint Paul

November 25, 2009

Page 3

cc: Louis F. Jambois, President
Laurie J. Hansen, Chief Financial Officer
Bruce Kessel, Controller
Cecile Bedor, Director

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APPENDIX B

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REBECCA OTTO
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state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

July 13, 2009

The Honorable John Zanmiller, Mayor
The Honorable Jim Englin, Council Member
The Honorable Ed Iago, Council Member
The Honorable Darlene Lewis, Council Member
The Honorable Aaron Van Moorlehem, Council Member
The Honorable Anthony Vitelli, Council Member
The Honorable David Wright, Council Member

City of West St. Paul

1616 Humboldt Ave
West St. Paul, MN 55118

Re: City of West St. Paul's TIF Districts—Initial Notice of Noncompliance

Dear Mayor Zanmiller and Council Members:

On May 5, 2009, the Office of the State Auditor (OSA) performed an on-site examination of the tax increment financing (TIF) district records of the City of West St. Paul's Economic Development Authority (City). The examination covered the following districts: TIF 1-1 South Robert Street, TIF 1-2 Walmart, TIF 1-3, and TIF 1-4 Lowes. The examination resulted in one finding that the City has not complied with state law governing the use of tax increment financing. This Initial Notice of Noncompliance (Notice) contains our finding and comments regarding the examination.

All data relating to the examination, including this Notice and the City's response (Response), are not public until the OSA has issued its final report.¹

State law requires the City send its Response in writing within 60 days after receipt of this Notice. The Response must state whether the City accepts the finding, in whole or in part, and the basis for any disagreement. After reviewing the Response, the OSA is required to forward information on any unresolved issues to the Dakota County Attorney for review.²

¹ Minn. Stat. § 6.715.

² Minn. Stat. § 469.1771, subd. 1.

OFFICE OF THE STATE AUDITOR

Mayor and Council, City of West St. Paul
July 13, 2009
Page 2

If the City pays to the County an amount equal to the amount in noncompliance indicated in this Notice, the OSA will consider the finding to be resolved. The City receives its proportionate share of the redistribution of the funds that have been returned to the County, if the City makes the payment within 60 days after the City receives this Notice.³

BACKGROUND

The OSA examined the following TIF districts in the City of West St. Paul.

TIF District Name	District Type	TIF-Plan Approval Date	Certification Request Date	Certification Date
TIF 1-1 South Robert Street	Renewal & Renovation	March 25, 2002	December 27, 2002	July 7, 2003
TIF 1-2 Walmart	Redevelopment	June 9, 2003	October 29, 2003	July 27, 2004
TIF 1-3	Redevelopment	September 27, 2004	May 5, 2005	August 4, 2005
TIF 1-4 Lowes	Renewal & Renovation	August 22, 2005	November 2, 2005	June 22, 2006

FINDING OF NONCOMPLIANCE

The OSA's finding of noncompliance regarding the City's TIF districts is as follows:

Finding. TIF District 3—Improper Expenditures of Tax Increment

In 2005, the City paid Top of the Line Lawn & Landscape, Inc., \$3,440.05 of tax increment for costs such as snow removal and lawn care. Snow removal and lawn care are maintenance expenses, not administrative expenses.⁴ Therefore, the City did not have authority to spend tax increment for these costs.

We find that the City spent \$3,440.05 of tax increment in violation of the TIF Act.

³ Minn. Stat. § 469.1771, subd. 5.

⁴ Minn. Stat. § 469.174, subd. 14.

OFFICE OF THE STATE AUDITOR

Mayor and Council, City of West St. Paul
July 13, 2009
Page 3

CONCLUSION

The Response to this finding must be submitted in writing to the Office of the State Auditor within 60 days after receipt of this notice. We are available to review and discuss the finding within this letter at any time during the preparation of the Response. After reviewing your response, the State Auditor will issue the Final Notice of Noncompliance.

If you have any questions, please call me at (651) 296-7979. We look forward to receiving your response.

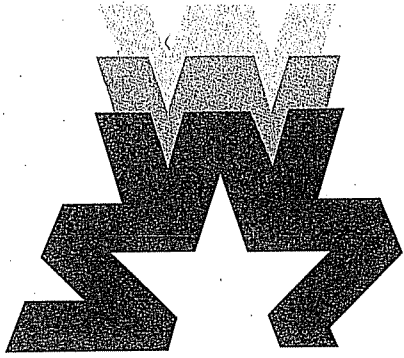
Very truly yours,

/s/ Arlin Waelti

Arlin Waelti
Assistant State Auditor
TIF Division Director

cc: John Remkus, City Manager
Sandy Christensen, Finance Director
Jim Hartshorn, Community Development Director

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CITY OF WEST ST. PAUL

1616 HUMBOLDT AVENUE, WEST ST. PAUL, MN 55118-3972

www.ci.west-saint-paul.mn.us

MUNICIPAL CENTER

Parks/Recreation/Public Works

Police

South Metro Fire

651-552-4100

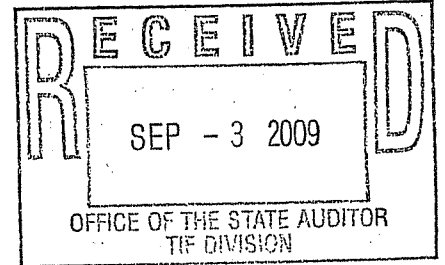
651-552-4150

651-552-4200

651-552-4176

FAX 651-552-4190

TDD 651-322-2323



September 1, 2009


Ms. Lisa McGuire
Office of the MN State Auditor
Tax Increment Financing Division
525 Park Street, Suite 500
St. Paul, MN 55103

Dear Ms. McGuire;

Enclosed please find a copy of the correspondence to the Dakota County Auditor regarding repayment of TIF funds that the City of West St. Paul was not eligible to receive. As noted in the findings of July 13, 2009, \$3,440.05 in invoices was determined to be in violation of the TIF Act. While the City noted in its initial response via Special Council Stephen Bubel that we are not in full agreement with the findings, we nevertheless feel that the amount is not significant. Therefore, the attached communication and check were sent to Dakota County of August 25th, 2009. If you require additional documentation to resolve the findings, please let me know.

Thank you for assisting us in insuring proper documentation and compliance.

Best regards,


Sandy Christensen
Finance Director

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

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September 25, 2009

The Honorable John Zanmiller, Mayor
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The Honorable Aaron Van Moorlehem, Council Member
The Honorable Anthony Vitelli, Council Member
The Honorable David Wright, Council Member
City of West St. Paul
1616 Humboldt Ave
West St. Paul, MN 55118

Re: City of West St. Paul's TIF Districts—Final Notice of Noncompliance

Dear Mayor Zanmiller and Council Members:

On July 13, 2009, the Office of the State Auditor (OSA) sent the City of West St. Paul (City) an Initial Notice of Noncompliance (Initial Notice) regarding the following tax increment financing (TIF) districts: TIF 1-1 South Robert Street, TIF 1-2 Walmart, TIF 1-3, and TIF 1-4 Lowes. The OSA received the City's response (City Response) on September 3, 2009, in a letter from Sandy Christensen, Finance Director.

This letter is the Final Notice of Noncompliance (the "Final Notice") of the Office of the State Auditor. It summarizes the initial finding and the City Response, and provides the OSA's final conclusion regarding the issue raised by the review. A detailed discussion of the basis for the finding can be found in the Initial Notice.

FINDING OF NONCOMPLIANCE

Only one finding of noncompliance was made.

Finding. TIF District 3—Improper Expenditures of Tax Increment—RESOLVED

In the Initial Notice, the OSA found that the City spent \$3,440.05 of tax increment in violation of the TIF Act. In the City's Response, the City stated they do not agree with the finding, but the amount is not significant. The City has returned \$3,440.05 to Dakota County. Therefore, the OSA considers this finding resolved.

OFFICE OF THE STATE AUDITOR

Mayor and Council, City of West St. Paul
September 25, 2009
Page 2

CONCLUSION

If you have questions, would like additional information, or if we can be of assistance in the future, please do not hesitate to contact me. I can be reached at (651) 296-7979.

Very truly yours,

/s/ Arlin Waelti

Arlin Waelti
Assistant State Auditor
TIF Division Director

cc: John Remkus, City Manager
Sandy Christensen, Finance Director
Jim Hartshorn, Community Development Director