Prepared by the North Dakota Legislative Council staff for the Taxation Committee
February 2010

TAX INCREMENT FINANCING TO DEVELOP PROPERTY

Cities are allowed to utilize tax increment financing (TIF) under the urban renewal law in North Dakota Century Code Chapter 40-58 as an economic development tool for a development or renewal area.

According to a September 2000 article in *Economic Development Digest* (National Association of Development Organizations Research Foundation publication), the TIF concept began in the 1940s and was originally conceived to provide an alternative method of public financing for development of blighted and substandard areas. However, TIF programs in a number of states were expanded to finance a wider range of projects even in "nondistressed" areas. This expanded use was met with criticism and legislative action in several states. For example, 1999 Illinois legislation clarified the definition of blighted area, required multigovernmental review boards for TIF projects, prohibited TIF development of projects such as golf courses and municipal buildings, and required TIF programs that focus on residential housing to reimburse school districts for added costs resulting from TIF development of an area.

Creation of a TIF district "freezes" property valuations in that district for any political subdivision except the city. A pool of money from existing funds or issuance of bonds is created to finance improvements within the TIF district. As property valuation from development within the TIF district increases, the amount of valuation exceeding the "frozen" valuation is subject to taxation only by the city and the tax revenues from this incremental valuation are segregated in a special fund to repay the bonds or other financing for the TIF project. Other taxing districts, such as a school district, continue to collect property taxes on property in the TIF district, but only up to the amount of the "frozen" valuation of the property.

It appears that some cities across the country have used TIF financing as an alternative to levying special assessments to pay for street, sewer, and water projects. The apparent concern of school districts with this approach, if the area incorporates residential property, is that the school district will receive the same property tax revenue from the property for many years while facing increased costs to provide services for additional students.

North Dakota law on TIF was first enacted in 1973 and is contained in Chapter 40-58, which is the chapter on urban renewal. As a result of an interim study by the Jobs Development Commission, the TIF law was amended in 1989 to make this vehicle available to develop industrial or commercial property.

Section 40-58-20 requires approval of a development or renewal plan for a development or renewal area. Under Section 40-58-01.1, "development or renewal area" is defined as "industrial or commercial property, a slum or blighted area, or a combination of these properties or areas that the local governing body designates as appropriate for a development or renewal project." Section 40-58-01.1 also defines "blighted area" as an "area other than a slum area which by reason of the presence of a substantial number of slums, deteriorated or deteriorating structures, predominance of defective or inadequate street layout, . . . unsanitary or unsafe conditions, deterioration of site or other improvements, diversity of ownership, tax or special assessment delinquency exceeding the fair value of the land, defective or unusual conditions of title, improper subdivision or obsolete platting, or the existence of conditions which endanger life or property by fire and other causes, or any combination of these factors, substantially impairs or arrests the sound growth of a municipality, . . . and is a menace to the public health, safety, morals, or welfare in its present condition and use." Whether these conditions exist in the area in question appears to be a question of fact that must be answered by the city governing body.

In 2001 the city of Fargo designated a TIF district for development of land bordered by Interstate Highway 94, Interstate Highway 29, 45th Street, and 32nd Avenue South. The property in question is located in the city of Fargo but within the West Fargo School District. West Fargo School District officials were very upset with the decision of the city of Fargo (see attached *The Forum* newspaper article). The reason for their frustration was that development of the property in question would generate no new property tax revenue for the West Fargo School District but the additional residential property would increase the number of students to be educated by the West Fargo School District.

The property in question in Fargo was predominately open land area previously used only for agricultural purposes. The Fargo City Commission apparently concluded that open land could be considered a "blighted area" under the TIF financing laws. Senator Judy Lee of West Fargo took exception to the decision of the Fargo City Commission and introduced Senate Bill No. 2165 (2003) to amend the definition of "blighted area" in Section 40-58-01.1 to add language stating that "blighted area" does not include predominately open land area that has been developed only for agricultural purposes. The bill also would have required establishment of a joint review board to review city creation of a development or renewal area. The joint review board would have consisted of one representative from the governing body of each city, county, school district, and other political subdivision with taxing authority over the property in question. The bill failed to pass.

The question of whether "blighted area" for purposes of TIF can be considered to include agricultural property appears to be a matter of opinion. Governing bodies and city attorneys in some cities in the country have taken a very expansive view of what kind of property may constitute a TIF district. Other city governing bodies and attorneys have taken a narrower view of what constitutes a blighted area. The North Dakota Legislative Assembly had an opportunity in 2003 to exclude open land used for agricultural purposes from TIF district development but did not enact the legislation.

Another area of concern with TIF is the indefinite length of time a city may hold property in tax increment status. As an alternative to sale of bonds to be paid with tax increments, the city may grant the project developer a property tax exemption for up to 15 years. However, if bonds are issued, the only limitation on the length of time the TIF tax status exists is until the cost of the project and all bonds or other obligations related to the project have been paid. Because projects may be financed and refinanced indefinitely, it appears there is no limit that can be identified to the length of time property may be held in tax increment status.

ATTACH:1