

## TIF Duration Extensions to Offset Deficits

### *Tax reform reduced increments, making some districts unable to pay their debt in full*

The 2001 property tax reform reduced the increments of tax increment financing (TIF) districts. In some cases, these reductions were sufficiently large that some TIF districts no longer generated enough increments to pay their obligations (bonds or development contracts). The 2001-02 legislature provided a variety of tools to help address these deficits or shortfalls. (See House Research, [TIF: Deficit Reduction Provisions](#), January 2008, for the general description of these mechanisms.)

### *The 2003 Legislature authorized extensions to offset deficits*

In 2003, the legislature authorized development authorities and cities to extend the duration of TIF districts beyond the normally applicable legal duration limits. This will permit the development authority (e.g., an HRA or EDA) to collect increments for a longer period of time, providing more increment to pay the TIF obligations. This additional increment, of course, will not be received until after the end of the normal duration of the district and, thus, cannot help to pay current debt service obligations. But if an extension can be combined with a refinancing of the TIF debt, it may enable current debt obligations to be met.

### *Which districts qualify to be extended?*

To qualify for an extension, a district must meet three tests:

- Certification of the district must have been requested before August 1, 2001 (i.e., before enactment of the 2001 property tax reform).
- The district's increments must be pledged to pay bonds, interfund loans (i.e., loans made by the city or authority from one of its non-TIF funds), or developer agreements that were entered before August 1, 2001.
- The authority must have used all of the other available deficit reduction measures to eliminate the deficit including:
  - Uncapping the original tax rate;
  - Switching fiscal disparities options; and
  - Transferring (or pooling) available increments from other districts.

### *How long is the permitted extension?*

The length of the permitted duration extension is determined under a formula that is an estimate of the reduction in the increment that was caused by the 2001 property tax reform. The formula extension is computed by comparing the tax paid by the district's original net tax capacity in 2001 with its average tax paid in 2002 and 2003. (The state general tax and market value taxes are ignored in these computations, since they do not affect increment computations.) The percentage reduction is multiplied by the remaining duration of the district (as of December 31, 2001) to determine the permitted extension (rounded up to the nearest whole

number of years for fractional amounts greater than one-third). For example, a district with nine years remaining that experienced a 25-percent drop in taxes on its original net tax capacity would qualify for a two-year extension (9 years x 25% = 2.25 years or rounded to two years). The maximum extension cannot exceed four years, in any case.

***DOR may grant an additional extension***

If the city estimates that the formula extension will not provide enough additional increment to pay the obligations in full, it may apply to the Department of Revenue (DOR) for an additional extension of up to two years. DOR received an application for an extension in 2004, which it approved. That is the only request it has received.

***Special rules for developer or “pay-as-you-go” obligations***

The extension authority was primarily intended to help the development authority or municipality to pay its own obligations—i.e., the reduction created a shortfall, relative to the authority’s legal obligation to pay. This situation generally does not occur with developer obligations (commonly referred to as “pay-as-you-go” obligations). Under pay-as-you-go contracts, the authority’s obligation is limited to the amount of its available increment. Thus, from the authority’s perspective, even though increments may have dropped substantially, there isn’t a deficit; the authority is only obligated to pay over whatever increments it receives. However, the developer expected to receive higher payments based on the pre-2001 property tax system and, thus, often will not receive payments that are large enough to cover the costs identified in the agreements with the city or authority. In some instances, these obligations or notes were sold to third-party investors who now suffer the loss. To provide some relief for these developers and investors, the extension law allows the authority to treat a pay-as-you-go obligation as a qualified obligation. If it does so, the maximum extension is one-half the regular formula amount (e.g., it cannot exceed two years). Also, application may not be made to DOR for an additional two-year extension.

***Restrictions applicable to extended districts***

If an authority elects to extend the duration of a district, after approval of the extension it can only use increments from the district to pay pre-existing obligations (i.e., those issued before August 1, 2001). The purpose of this restriction is to prevent the use of increments from the extension to fund new costs. During the extension period, increments may only be used to pay qualifying obligations (i.e., pre-2001 bonds, interfund loans, and pay-as-you-go notes). If increments from multiple districts are pledged to pay the qualifying obligations, then all of these districts (even if their terms have not been extended) are subject to this limit on the use of increments.

**For more information:** Contact legislative analyst Joel Michael at 651-296-5057. Also see the House Research publication *TIF Deficit Reduction Provisions*, January 2008.

The Research Department of the Minnesota House of Representatives is a nonpartisan office providing legislative, legal, and information services to the entire House.