

# State of Minnesota



## Office of the State Auditor

Julie Blaha  
State Auditor

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### **Tax Increment Financing Legislative Report**

TIF Reports for the Year Ended December 31, 2020  
TIF Reviews Concluded for the Year Ended December 31, 2021

## **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 100 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 of 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 Minnesota’s local 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 Employees 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, 2020  
TIF Reviews Concluded for the Year Ended December 31, 2021



**Office of the State Auditor**

**February 14, 2022**

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# TAX INCREMENT FINANCING LEGISLATIVE REPORT

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**APPENDIX B**

Office of the State Auditor Initial Notice of Noncompliance – City of Dassel  
Response to the Initial Notice of Noncompliance – City of Dassel  
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**APPENDIX C**

Office of the State Auditor Initial Notice of Noncompliance – City of Ironton  
Office of the State Auditor Final Notice of Noncompliance – City of Ironton

# EXECUTIVE SUMMARY

## Highlights and Trends

- In 2020, approximately \$260 million of tax increment revenue was generated statewide, which is an increase of almost seven percent from 2019 and the largest total over the past ten years. (Pages 16 - 19)
- In 2020, 394 development authorities submitted reports to the OSA for 1,661 TIF districts. The number of districts over the last five years has largely remained constant at between 1,648 and 1,665 districts. (Pages 9 - 12)
- In 2020, 76 new TIF districts were certified, 21 fewer than the 97 new districts certified in 2019. In 2020, the number of districts decertified increased to 100, an increase of 52 percent from 2019. New certifications have largely been more steady over the last ten years, while decertifications have been more variable. (Pages 13 - 15)
- In the latest five-year period, redevelopment and economic development districts saw significant jumps in their rates of early decertification (i.e., prior to the statutory maximum duration of the district) compared to rates reported in previous years. Respectively, they decertified early 70 percent and 37 percent of the time during this period. The rate of early decertification for housing districts has stayed consistently close to 80 percent and was 78 percent for this period. (Page 16)
- In 2020, development authorities returned \$8,388,322 in tax increment revenue to county auditors for redistribution as property taxes to cities, counties, and school districts. (Page 20)
- In 2020, there was a total of nearly \$1.7 billion of outstanding debt associated with TIF districts. Pay-As-You-Go (PAYG) obligations were the predominant type of debt, making up 66 percent of the debt reported (up from 64 percent in 2019). General Obligation (GO) bonds comprised about 16 percent of the total debt. Interfund loans (mostly from non-tax increment accounts) made up 12 percent of total debt. (Page 22)

## SCOPE AND METHODOLOGY

In 1995, the Minnesota Legislature assigned legal compliance oversight for TIF to the OSA.<sup>1</sup> The OSA's oversight authority extends to examining the use of TIF by political subdivisions, as authorized by the Minnesota Tax Increment Financing Act (TIF Act).<sup>2</sup>

The TIF Act requires development authorities to file with the OSA annual financial reports for each of their TIF districts. Reports must be submitted on or before August 1 of each year, starting the year in which a district is certified.<sup>3</sup> Reporting continues until the year following the year in which the district is both decertified and all remaining revenues derived from tax increment have been expended or returned to the county auditor.<sup>4</sup> Because new certifications and decertifications are not always reported in a timely manner, the data for prior years contained in this Report may differ from data presented in previous reports.

This 26th Annual Legislative Report (Report) was compiled from information reported by 394 development authorities currently exercising tax increment financing (TIF) powers in Minnesota. The Report summarizes information reported by these development authorities for 1,661 districts for the calendar year ended December 31, 2020.<sup>5</sup> An additional five authorities were required but failed to submit reports on six districts for the period; accordingly, data for those districts is not reflected in this Report.<sup>6</sup>

The Report also provides a summary of any violations cited in the limited-scope reviews conducted by the Office of the State Auditor (OSA) in 2021. This Report is provided annually to the chairs of the legislative committees with jurisdiction over TIF matters.<sup>7</sup>

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<sup>1</sup> 1995 Minn. Laws, ch. 264, art. 5, § 34. The OSA's oversight of TIF began in 1996.

<sup>2</sup> The TIF Act can be found at: Minn. Stat. §§ 469.174 through 469.1799 inclusive, as amended. The OSA's oversight authority can be found at: Minn. Stat. § 469.1771.

<sup>3</sup> Minn. Stat. § 469.175, subd. 6.

<sup>4</sup> Minn. Stat. § 469.175, subd. 6b.

<sup>5</sup> The summarized information reflects reported activity as of the end of calendar year 2021. Late and resubmitted reports may result in slight changes. Likewise, prior year data in some of the tables and charts may have changed slightly from previously published reports.

<sup>6</sup> Lakeland failed to report for both of its districts. Ironton, Morton, Orono, and St. Clair each failed to report for their single districts. Ironton and St. Clair have outstanding reports for previous years. The TIF Act provides for tax increment to be withheld when reports are not filed.

<sup>7</sup> Minn. Stat. § 469.1771, subd. 1(c).

# TAX INCREMENT FINANCING LEGISLATIVE REPORT

## BACKGROUND

Tax increment financing (TIF) is a financing tool established by the Legislature to support local economic development, redevelopment, and housing development. As its name suggests, TIF enables development authorities to finance development activities using the incremental property taxes, or “tax increments,” generated by the increased taxable value of the new development.

TIF is not a tax reduction; taxes are paid on the full taxable value of the property. The original taxable value continues to be part of the tax base that supports the tax levies of the city, county, school district, and other taxing jurisdictions.<sup>8</sup> The new, additional value from development activity is “captured” from the tax base; tax increments are the taxes paid on the captured value. Tax increments are reserved and used to finance qualifying costs that make the new development possible.

TIF districts are comprised of the land parcels on which development activity occurs. In order for a municipality to finance development with TIF, it must find that, without the use of TIF, the development would not be expected to occur.<sup>9</sup>

The expenditures that qualify to be paid from tax increment 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. Examples of qualifying costs include: land and building acquisition, demolition of structurally substandard buildings, removal of hazardous substances, site preparation, installation of utilities, and road improvements.

A TIF district is created by a development authority. A development authority can be a city, an entity created by a city, or an entity created by a county.<sup>10</sup> Development authorities derive their authority to use TIF and assist projects from various development acts that underlie and are incorporated into the TIF Act by reference: the Housing and Redevelopment Authorities (HRA) Act, the Port Authorities Act, the Economic Development Authorities (EDA) Act, the City Development District Act, and the Rural Development Financing Authorities Act.<sup>11</sup> These acts govern the development projects, whereas the TIF Act governs the use of tax increments. Project areas can be larger than a TIF district and can contain multiple TIF districts.

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<sup>8</sup> A hazardous substance subdistrict may capture original value due to the higher expense involved in cleaning up hazardous substances. Minn. Stat. §§ 469.174, subs. 7(b) and 23; 469.175, subd. 7.

<sup>9</sup> Minn. Stat. § 469.175, subd. 3(b)(2). This is often referred to as the “But-For Test,” (i.e. development would not happen but for the use of TIF).

<sup>10</sup> Counties and towns may also be development authorities in certain instances.

<sup>11</sup> Minn. Stat. § 469.174, subd. 2 (listing the statutory citations for the various development acts).



TIF districts are terminated, or decertified, when they reach the earliest of the following times: (1) the applicable maximum duration limit provided in the TIF Act for each type of TIF district; (2) a shorter duration limit established by the authority in the TIF plan; (3) upon defeasing, paying, or setting aside sufficient increment to pay all in-district obligations pursuant to the Six-Year Rule; or (4) upon written request by the authority to the county auditor to decertify the district.<sup>12</sup> Decertification ends the collection of increment, but many districts remain active and continue to report until all remaining tax increment revenues have been expended or returned to the county auditor.

## **Development Authorities**

In 2020, there were 399 development authorities in Minnesota actively using TIF, which is seven less than the number active in 2019. Nine authorities became inactive and two inactive development authorities became active again.

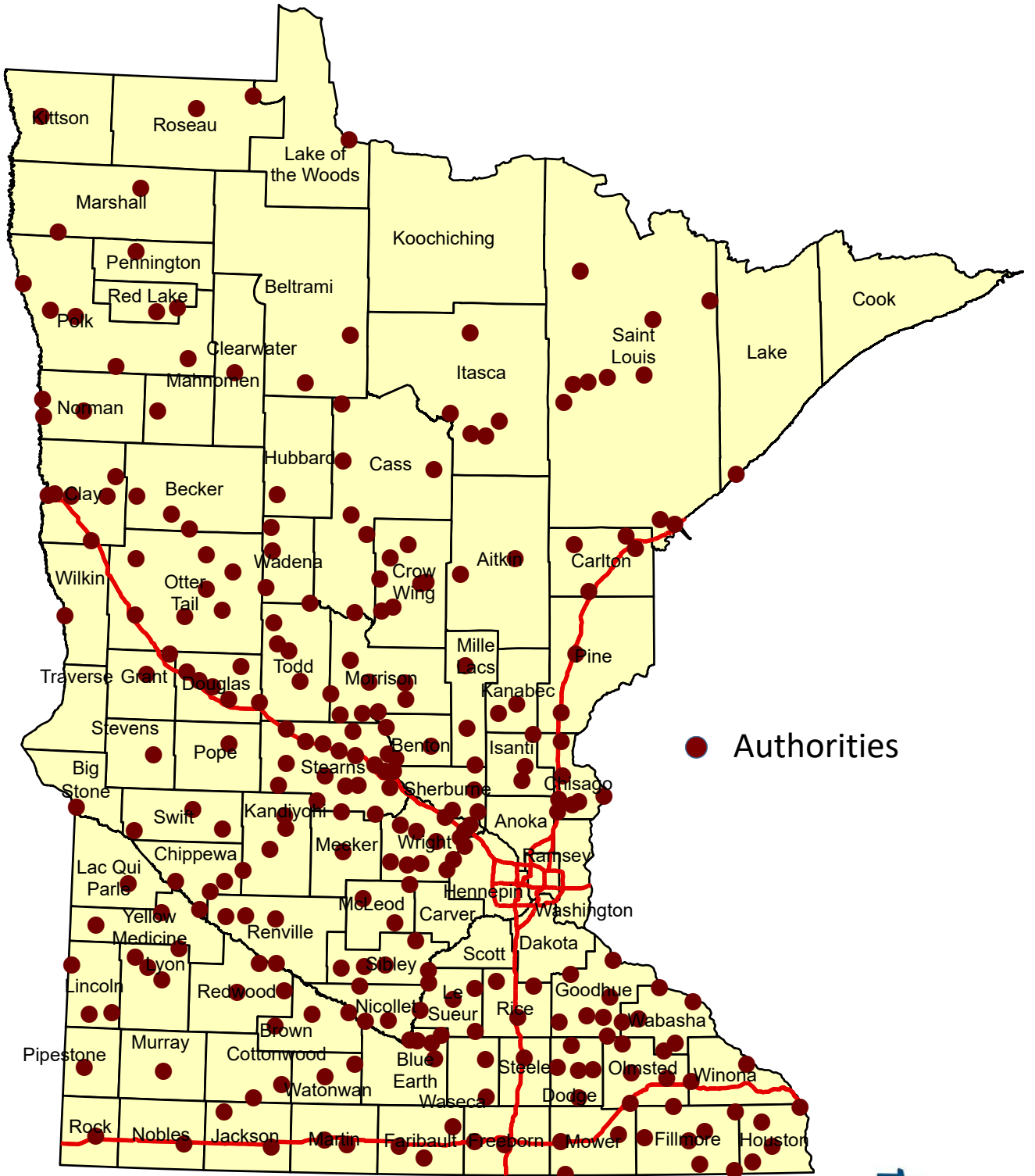
In 2020, of the 399 active development authorities, 297 were located in Greater Minnesota and 102 were located in the Seven-County Metropolitan Area (Metro Area). Maps 1 and 2 on the following pages show the locations of these authorities. Map 3 identifies counties that have a development authority using TIF.<sup>13</sup>

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<sup>12</sup> Minn. Stat. § 469.177, subd. 12.

<sup>13</sup> This map does not include the following joint authorities: Bluff Country HRA and Southeast Minnesota Multi-County HRA.

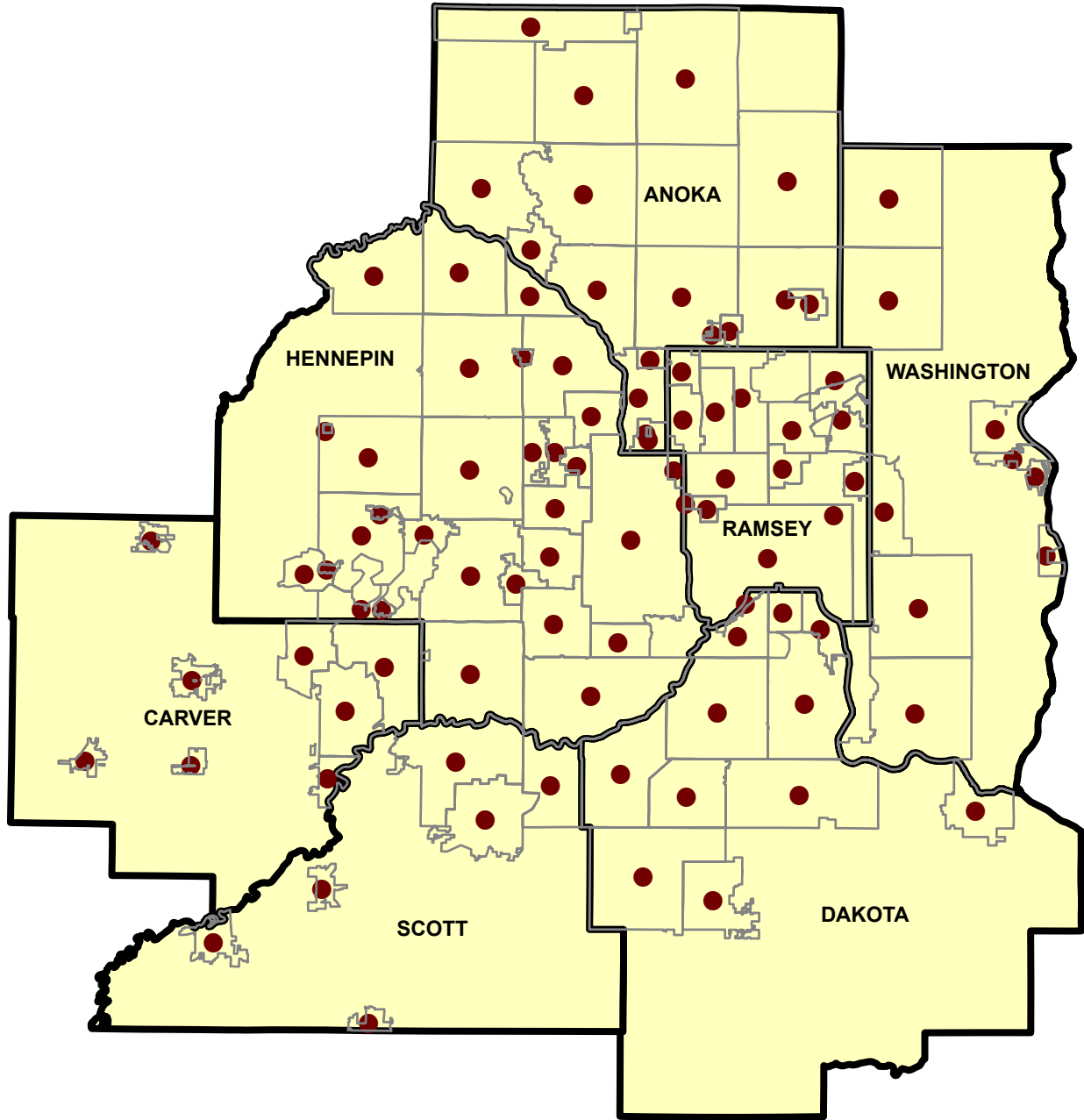
# Development Authorities in Greater Minnesota, 2020



● Authorities



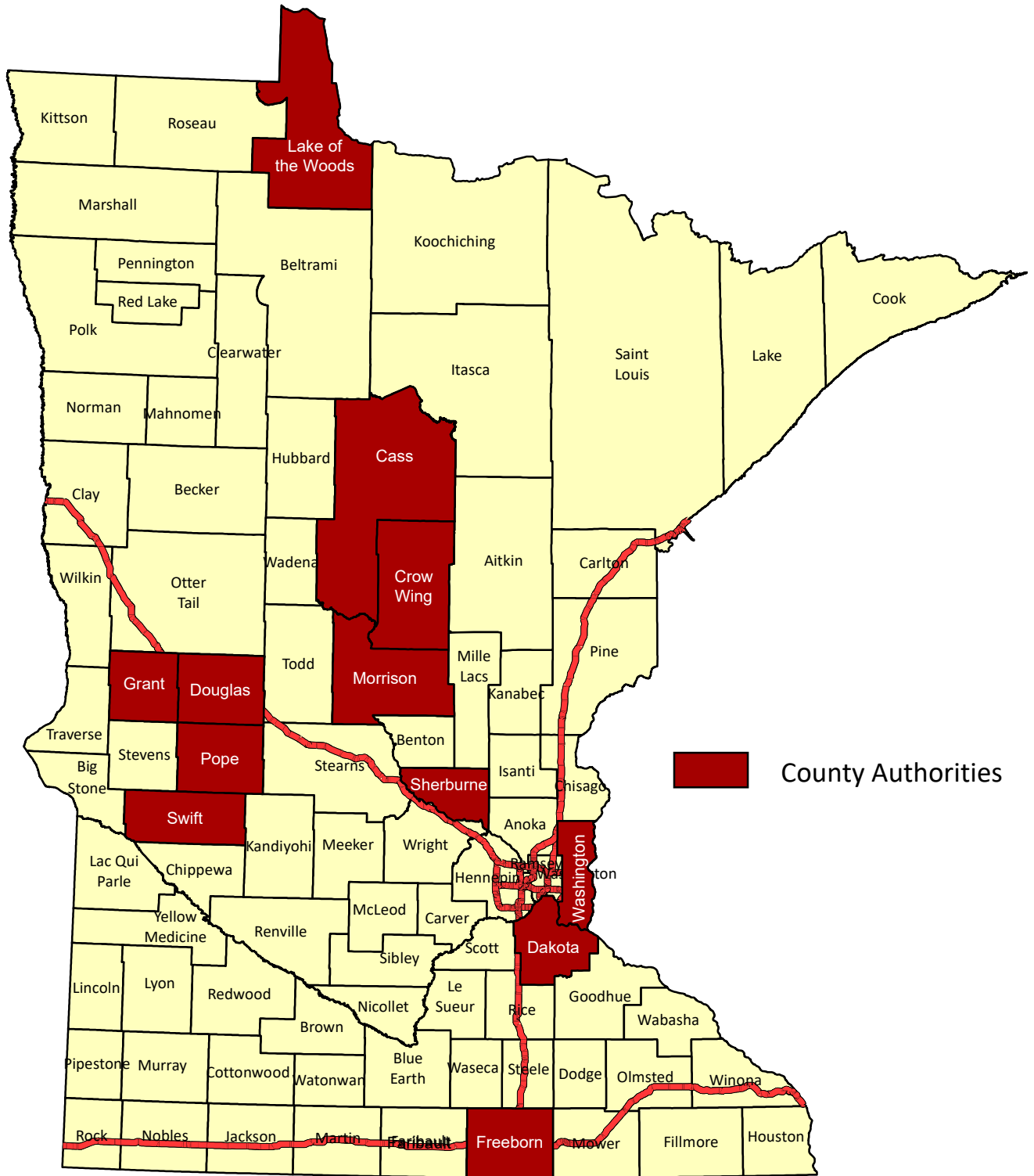
# Development Authorities in Metro Area, 2020



● Authorities



# County Development Authorities, 2020



## Creation of TIF Districts

The first step a development authority takes in creating a TIF district is to adopt a TIF plan. The TIF plan outlines the development activity to be funded with tax increment.<sup>14</sup>

A development authority must obtain approval of the TIF plan from the governing body of the municipality in which the TIF district is to be located. Approval of the TIF plan authorizes the use of tax increment to pay TIF-eligible project costs. Before approving a TIF plan, the municipality must publish a notice and hold a public hearing.<sup>15</sup> 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.<sup>16</sup>

Before the notice for a public hearing is published, the development authority must provide a copy of the proposed TIF plan to the county auditor and the clerk of the school board who, in turn, must provide copies of these documents to the members of the county board of commissioners and the school board.<sup>17</sup> The county board and school board may comment on the proposed district, but cannot prevent its creation.<sup>18</sup>

## Types of TIF Districts

Five different types of TIF districts are currently authorized by the TIF Act:

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

There are two other general types of districts: districts created prior to the enactment of the TIF Act ("pre-1979 districts") and districts created by special law ("uncodified districts"). There is also one type of subdistrict that can be created within a TIF district, a hazardous substance subdistrict.

Each type of TIF district has different requirements for its creation, different restrictions on the use of tax increment revenue, and different maximum duration limits.

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<sup>14</sup> Minn. Stat. § 469.175, subd. 1.

<sup>15</sup> Minn. Stat. § 469.175, subd. 3.

<sup>16</sup> In many cases, the commissioners of the TIF authority include some or all of the council members.

<sup>17</sup> Minn. Stat. § 469.175, subd. 2.

<sup>18</sup> When the county is the municipality that must approve the TIF plan, the county board may prevent the creation of a TIF district.

**Redevelopment Districts** – The purpose of a redevelopment district is to eliminate certain blighted conditions.<sup>19</sup> Redevelopment districts are designed to conserve the use of existing utilities, roads, and other public infrastructure, and to discourage urban sprawl. Qualifying tax increment expenditures include: acquiring sites containing substandard buildings, streets, utilities, parking lots, or other similar structures; demolishing and removing substandard structures; eliminating hazardous substances; clearing the land; and installing utilities, sidewalks, and parking facilities. These TIF-financed activities are generally considered a means to “level the playing field” so that blighted property can compete with bare land for development. These districts have a statutory maximum duration limit of 25 years after first receipt of tax increment.<sup>20</sup>

**Economic Development Districts** – The purpose of an economic development district is to: (1) discourage commerce, industry, or manufacturing from moving to another state or city; (2) increase employment in the state; (3) preserve and enhance the tax base; or (4) satisfy requirements of a workforce housing project.<sup>21</sup> Tax increment revenue from economic development districts is used primarily to assist manufacturing, warehousing, storage and distribution, research and development, telemarketing, and tourism, but can also be used for workforce housing projects (as of 2017 and sunset in 2027).<sup>22</sup> Use of tax increment in these districts for commercial development (retail sales) is excluded by law, except in “small cities.”<sup>23</sup> Economic development districts are short-term districts with a limit of eight years after first receipt of tax increment.<sup>24</sup>

**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. Tax increment revenue can be used in the construction of low- and moderate-income housing and to acquire and improve the housing site. These districts have a statutory maximum duration limit of 25 years after first receipt of tax increment.<sup>25</sup>

**Renewal and 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

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<sup>19</sup> Minn. Stat. § 469.174, subd. 10(a).

<sup>20</sup> Minn. Stat. § 469.176, subd. 1b(a)(4). Note that a duration of 25 years *after* first receipt of tax increment permits 26 years of collection.

<sup>21</sup> Minn. Stat. § 469.174, subd. 12.

<sup>22</sup> Minn. Stat. § 469.176, subd. 4c, identifies allowable purposes. Minn. Stat. § 469.175, subd. 3(g), contains the sunset, barring districts from being certified for requests made after June 30, 2027.

<sup>23</sup> Minn. Stat. § 469.174, subd. 27 (defining small cities as, generally, those with a population of 5,000 or less located ten miles or more from a city of 10,000 or more), and Minn. Stat. § 469.176, subd. 4c.

<sup>24</sup> Minn. Stat. § 469.176, subd. 1b(a)(3). Note that a duration of eight years *after* first receipt of tax increment permits nine years of collection.

<sup>25</sup> Minn. Stat. § 469.176, subd. 1b(a)(4). Note that a duration of 25 years *after* first receipt of tax increment permits 26 years of collection.

the development activity relates more to inappropriate or obsolete land use. The statutory maximum duration limit for these districts is 15 years after first receipt of tax increment.<sup>26</sup>

**Soils Condition Districts** – The purpose of a soils condition district is to assist in the redevelopment of land which cannot otherwise be developed due to the presence of hazardous substances, pollutants, or contaminants. The estimated cost of the proposed removal and remediation must exceed the fair market value of the land before the remediation is completed.<sup>27</sup> The statutory maximum duration limit for these districts is 20 years after first receipt of tax increment.<sup>28</sup>

**Pre-1979 Districts** – These districts were created prior to the 1979 TIF Act and have all been decertified.<sup>29</sup>

**Uncodified Districts** – Special laws have been enacted to address unique issues and permit the use of TIF for geographic areas that do not meet the statutory qualifications for the main statutory types of TIF districts. They are referred to as an “uncodified” districts. Examples of uncodified districts are housing transition districts for the cities of Crystal, Fridley, Minneapolis, and St. Paul, and a district addressing distressed rental properties in Brooklyn Park.

**Hazardous Substance Subdistricts** – The purpose of a hazardous substance subdistrict (HSS) is to finance the cleanup of hazardous substance sites within a TIF district so that development or redevelopment can occur.<sup>30</sup> The subdistrict may be established at the time of approval of the TIF plan, or added later by modification, and requires certain findings and a development response action plan approved by the Minnesota Pollution Control Agency (PCA).<sup>31</sup> The HSS captures additional increment by reducing the original net tax capacity (ONTC) by the estimated costs of the removal actions.<sup>32</sup> The payment of these costs comes from what would normally be the frozen property tax base of the district and yields immediate increment without requiring any increase in property value. The additional increment may be used only to pay or reimburse specified costs, such as removal or remedial actions, pollution testing, purchase of environmental insurance, and related administrative and legal costs.<sup>33</sup> The statutory maximum duration limit for an HSS can extend beyond that of the overlying district and is 25 years from the date the extended period began or the period necessary to recover the costs specified in the development response plan, whichever occurs first.<sup>34</sup>

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<sup>26</sup> Minn. Stat. § 469.176, subd. 1b(a)(1). Note that a duration of 15 years *after* first receipt of tax increment permits 16 years of collection.

<sup>27</sup> Minn. Stat. § 469.174, subd. 19.

<sup>28</sup> Minn. Stat. § 469.176, subd. 1b(a)(2). Note that a duration of 20 years *after* first receipt of tax increment permits 21 years of collection.

<sup>29</sup> Minn. Stat. § 469.176, subd. 1c. Princeton’s TIF 1 Downtown Redevelopment District is the last pre-1979 district reporting.

<sup>30</sup> Minn. Stat. § 469.174, subs. 16 and 23; Minn. Stat. § 469.175, subd. 7.

<sup>31</sup> Minn. Stat. § 469.174, subd. 17.

<sup>32</sup> Minn. Stat. § 469.174, subd. 7(b).

<sup>33</sup> Minn. Stat. § 469.176, subd. 4e.

<sup>34</sup> Minn. Stat. § 469.176, subd. 1e.

## Special Legislation

The legislature has enacted special legislation allowing exceptions to the TIF Act for individual districts with some frequency. As of 2020, 115 TIF districts reported having special laws. The most common types of special legislation include: (1) extending the five-year deadline for entering into contracts or issuing bonds, (2) extending the duration limit of a TIF district, (3) creating an exception to requirements or findings needed to create a TIF district, and (4) creating an exception to the limitations on the use of tax increment.

## Number of TIF Districts

In 2020, 394 development authorities submitted reports to the OSA for 1,661 TIF districts. Of these districts, 1,045 (63 percent) were located in Greater Minnesota and 616 (37 percent) were located in the Metro Area.<sup>35</sup> (See Figure 1.)

**Figure 1.**

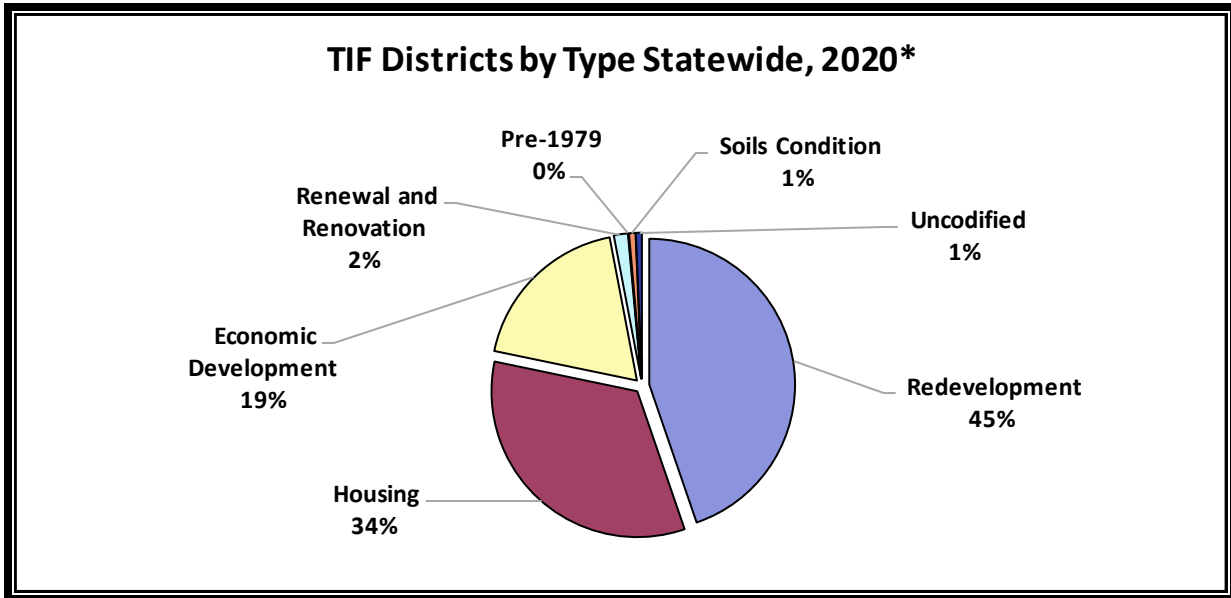
<b>TIF Districts by Type: Statewide, Greater MN, &amp; Metro Area; 2020</b>			
<b>Type of District</b>	<b>Statewide</b>	<b>Greater MN</b>	<b>Metro Area</b>
Redevelopment	743	404	339
Housing	557	377	180
Economic Development	311	250	61
Renewal and Renovation	26	9	17
Pre-1979	1	1	0
Soils Condition	12	4	8
Uncodified	11	0	11
<b>Total</b>	<b>1,661</b>	<b>1,045</b>	<b>616</b>
Hazardous Substance Subdistricts	22	2	20

In 2020, redevelopment districts made up 45 percent of all TIF districts statewide, followed by housing districts at 34 percent and economic development districts at 19 percent. Combined, these three types made up 97 percent of all districts. (See Figure 2.)

<sup>35</sup> The number of districts being reported includes districts that are decertified but must continue to report due to remaining tax increment assets.



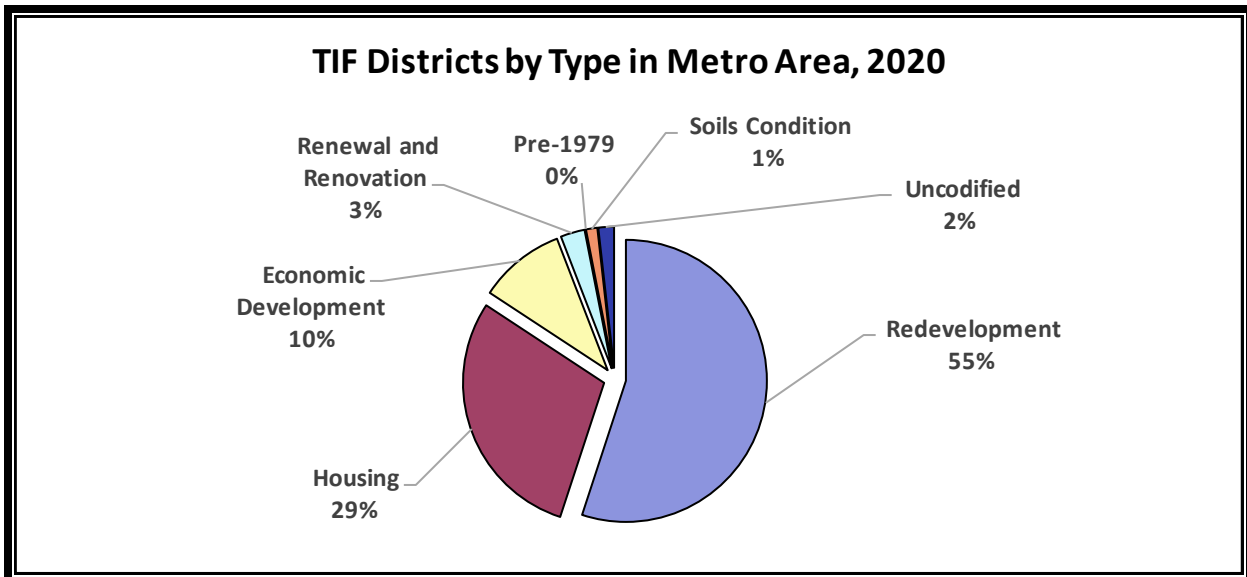
Figure 2.



\*Due to rounding, the sum of the percentages does not equal 100 percent.

In the Metro Area, redevelopment districts made up over half (55 percent) of all districts, followed by housing districts at 29 percent and economic development districts at ten percent. (See Figure 3.)

Figure 3.



In Greater Minnesota, redevelopment districts were also the largest type of district, again followed by housing and economic development districts. However, redevelopment districts made up a smaller portion compared to the Metro Area, and housing and economic development districts each made up much larger portions. (See Figure 4.)

Figure 4.

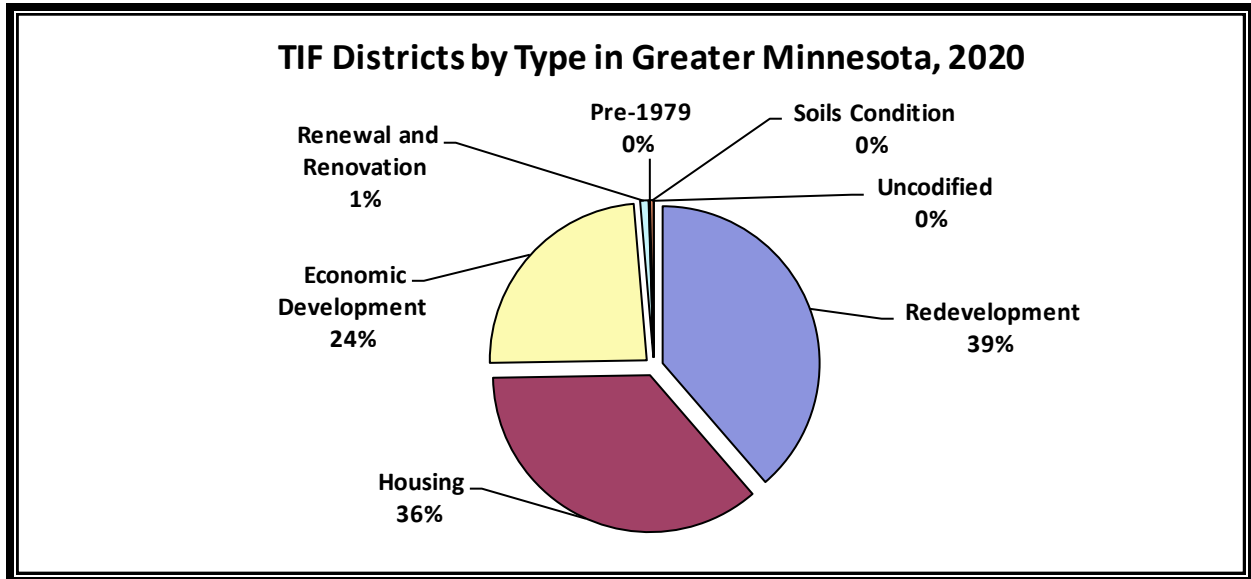
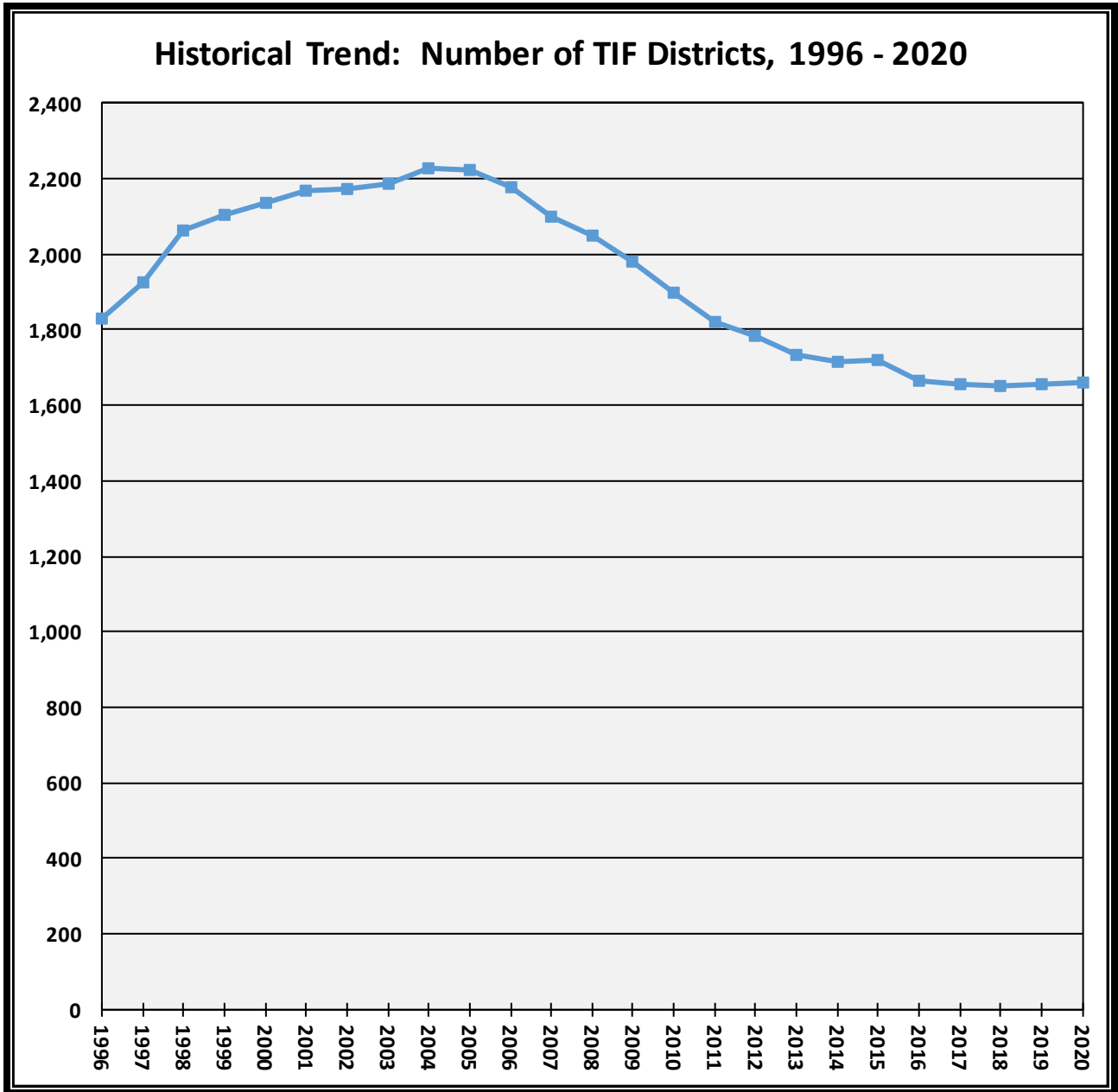


Figure 5 shows the total number of districts reporting to the OSA for each year since 1996, which is when the OSA began oversight of TIF. Between 1996 and 2004, the number of TIF districts increased each year. From 2004 to 2016, the total number has declined each year, except for a very slight increase of two districts in 2015. This decline reflected, among other things, large numbers of older districts created prior to moderating reforms in 1990 reaching their statutory duration limits. As the majority of pre-1990 districts have decertified, the number of districts over the last five years has largely remained constant at between 1,648 and 1,665 districts. The 1,661 districts reporting for 2020 is up less than one percent from the 1,648 reporting in 2019.

Figure 5.



## New Districts Certified

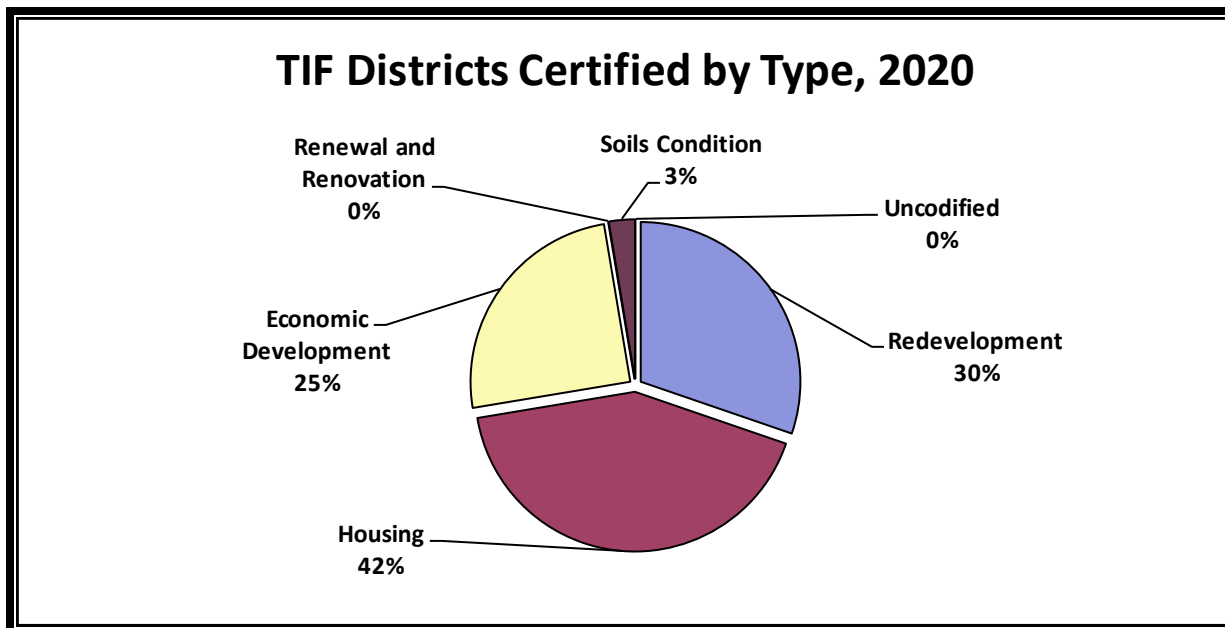
In 2020, 76 new TIF districts were certified, 21 fewer than the 97 new districts certified in 2019. Figure 6 shows new district certifications by type over the past five years. The number of certifications in 2020 was closer to the recent low reported in 2016 and follows three years of significantly higher numbers of certifications. The trends among types of districts are varied, with housing district creation remaining higher and economic development districts being the most variable.

Figure 6.

Number of TIF Districts Certified by Type, 2016 - 2020					
	2016	2017	2018	2019	2020
Redevelopment	29	34	32	28	23
Housing	18	29	35	34	32
Economic Development	21	27	24	31	19
Renewal and Renovation	3	1	2	1	0
Soils Condition	1	0	2	1	2
Uncodified	1	0	1	2	0
<b>Total</b>	<b>73</b>	<b>91</b>	<b>96</b>	<b>97</b>	<b>76</b>

In 2020, housing districts accounted for the largest portion of all new districts at 42 percent, with redevelopment districts following at 30 percent. Economic development districts made up 25 percent, with soils condition making up the remainder. (See Figure 7.)

Figure 7.



### Districts Decertified

Unlike the full discretion involved in creating new districts, decertifications are more often the result of duration limits (either statutory or plan-specified), or the Six-Year Rule, which requires decertification once all in-district obligations have been satisfied.<sup>36</sup>

In 2020, the number of districts decertified increased to 100, an increase of 52 percent from 2019, which had seen a significant decrease. Figure 8 shows the number of decertifications by type of district for the last five years.

**Figure 8.**

<b>Number of TIF Districts Decertified by Type, 2016 - 2020</b>					
	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>
Redevelopment	60	36	40	27	37
Housing	33	12	23	23	26
Economic Development	25	28	29	14	35
Renewal and Renovation	1	1	1	1	2
Soils Condition	0	0	0	1	0
Uncodified	0	0	0	0	0
Pre-1979	0	0	0	0	0
<b>Total</b>	<b>119</b>	<b>77</b>	<b>93</b>	<b>66</b>	<b>100</b>

The variability of 2017 to 2020 decertifications is not readily explainable. The drops in 2017 and 2019 had not been too surprising given that maximum durations would likely be reached for districts created during past periods of reduced certifications.<sup>37</sup> The increases for 2018 and 2020 might just reflect the increasing prevalence of less-predictable early decertifications under the Six-Year Rule.

In 2020, 37 percent of decertified districts were redevelopment districts, 35 percent were economic development districts, and 26 percent were housing districts. (See Figure 9.)

<sup>36</sup> In-district obligations are determined pursuant to the Five-Year Rule (Minn. Stat. § 469.1763, subd. 3), which generally limits “in-district” obligations to those established in the first five years. The Six-Year Rule (Minn. Stat. § 469.1763, subd. 4), generally requires that beginning in the sixth year, an authority must use a certain portion of increment to pay, or set aside to pay, the in-district obligations, and to decertify when the in-district obligations are paid or when enough increment has been set aside for their payment.

<sup>37</sup> The level of new district certifications following 1990 reforms was less than prior years, and the redevelopment and housing districts created during those years would be reaching their maximum durations around this time period and make lower levels of decertifications likely. Figure 10 supports this idea, where decertifications for the last four years are less than those seen in the previous six years. In addition, the reduced number of economic development districts created during the great recession years of 2009 and 2010 would also be reaching their maximum durations in the last year or two (as was seen in 2019’s lower number).

Figure 9.

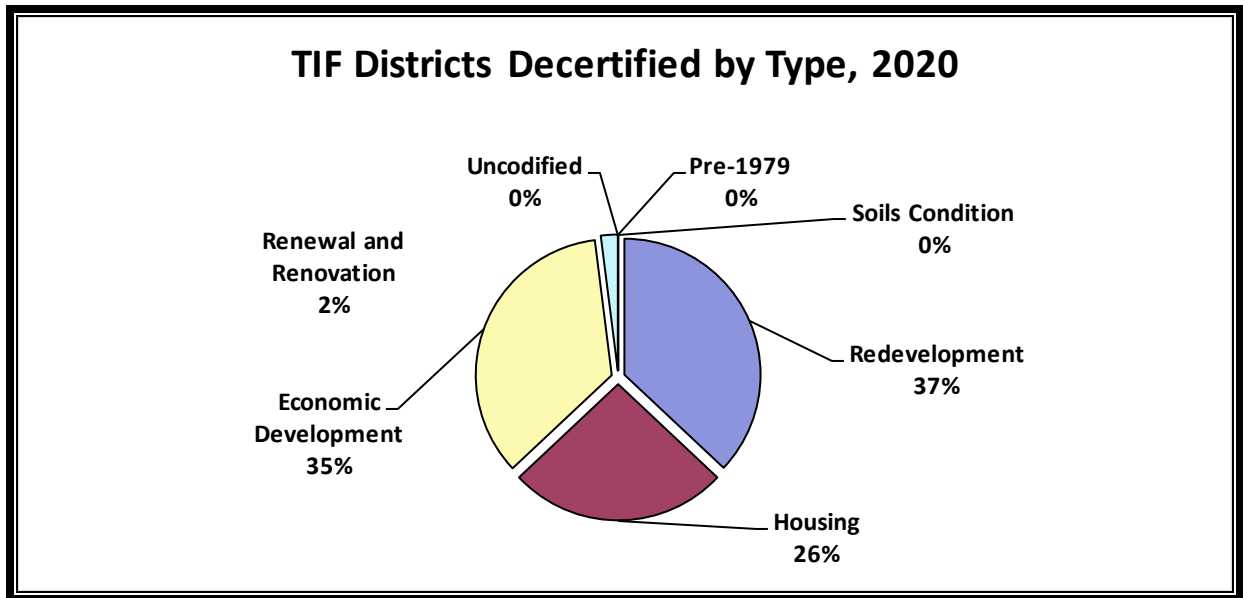
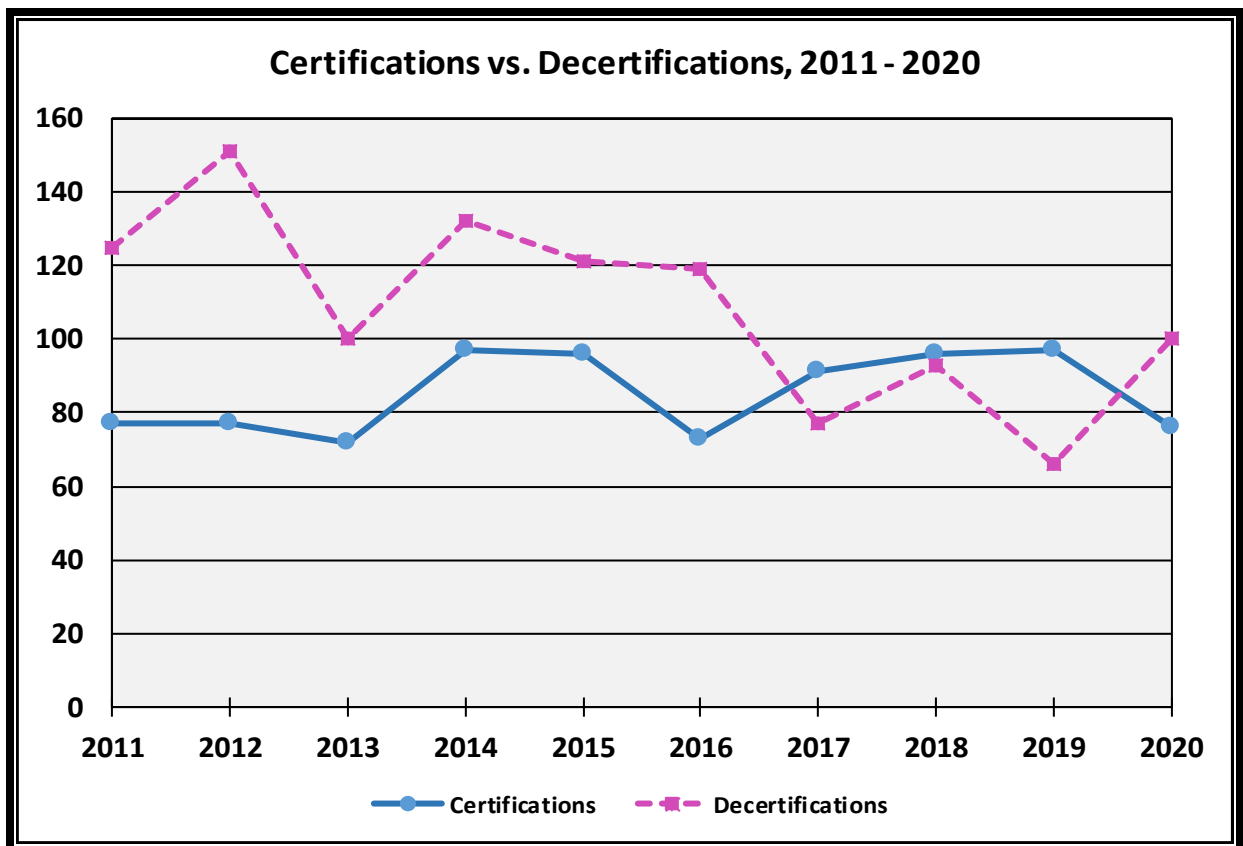


Figure 10 shows ten-year trends for decertifications and new certifications. New certifications have largely been more steady over the period, while decertifications have been more variable.

Figure 10.



The impact of the Six-Year Rule is reflected, in part, in Figure 11, which compares, for districts that decertified from 2016 through 2020, the number of districts that decertified early versus those that ran for their full statutory maximum duration.

**Figure 11.**

<b>Decertifications 2016 - 2020: Full Duration vs. Early Decertification*</b>				
<b>District Type / (Max Duration)</b>	<b>Decertified Districts</b>	<b>Lasted Full Duration</b>	<b>Decertified Early</b>	
			<b>Percent</b>	<b>Average Years</b>
Redevelopment (25 years)	200	30%	70%	10
Housing (25 years)	117	22%	78%	10
Economic Development (8 years)	131	63%	37%	4
Renewal and Renovation (15 years)	6	100%	0%	0
Soils Condition (20 years)	1	0%	100%	6

\*Durations are measured by comparing "year of actual decertification" to "year of required decertification" reported by the authority and based on the maximum duration limit or an earlier final year identified in the TIF plan. Early decertifications may be voluntary or may be required by the Six-Year Rule.

From 2016 to 2020, 78 percent of housing districts decertified early. This rate has stayed consistently close to 80 percent since this metric was first included in the 2014 TIF Legislative Report. In this latest five-year period, redevelopment and economic development districts saw significant jumps in their rates of early decertification. Redevelopment districts decertified early 70 percent of the time, compared to the 63 percent rate reported a year ago and continuing a trend of rising rates of early decertification.<sup>38</sup> Economic development districts decertified early 37 percent of the time over this period, which is a second consecutive increase of seven percentage points.<sup>39</sup> For districts that decertified early, redevelopment and housing districts decertified ten years early on average, and economic development districts decertified an average of four years early.

**Tax Increment Revenue**

In 2020, approximately \$260 million of tax increment revenue was generated statewide. While most districts are located in Greater Minnesota, most tax increment revenue is generated in the Metro Area. Approximately \$219 million of tax increment, or 84 percent, was generated in the Metro Area in 2020. (See Figure 12.)

<sup>38</sup> While not displayed herein, the previous rates of early decertification have increased each year from a low of 48 percent in the 2015 TIF Legislative Report.

<sup>39</sup> While not displayed herein, the 2019 TIF Legislative Report identified a five-year rate of 30 percent for economic development districts, and in prior years, the rate ranged from 22 to 25 percent.

Figure 12.

Revenue Generated by Type: Statewide, Greater MN, & Metro Area; 2020			
Type of District	Statewide	Greater MN	Metro Area
Redevelopment	\$ 191,317,483	\$ 18,304,275	\$ 173,013,208
Housing	\$ 37,468,430	\$ 12,293,969	\$ 25,174,461
Economic Development	\$ 23,260,761	\$ 9,795,052	\$ 13,465,709
Renewal and Renovation	\$ 5,605,698	\$ 630,231	\$ 4,975,467
Pre-1979	\$ -	\$ -	\$ -
Soils Condition	\$ 494,455	\$ 85,705	\$ 408,750
Uncodified	\$ 1,630,619	\$ -	\$ 1,630,619
<b>Total</b>	\$ 259,777,446	\$ 41,109,232	\$ 218,668,214

Figures 13, 14, and 15 illustrate the mixes of tax increment revenue generated in 2020 by type of district for the whole state, the Metro Area, and Greater Minnesota, respectively. Statewide, while redevelopment districts made up 45 percent of the TIF districts, they generated 74 percent of total tax increment revenue. This is driven by districts in the Metro Area, where redevelopment districts generated 79 percent of the tax increment revenue despite representing only 55 percent of the districts. By contrast, the distribution of tax increment revenue in Greater Minnesota is more similar to the distribution of the number of districts.

Figure 13.

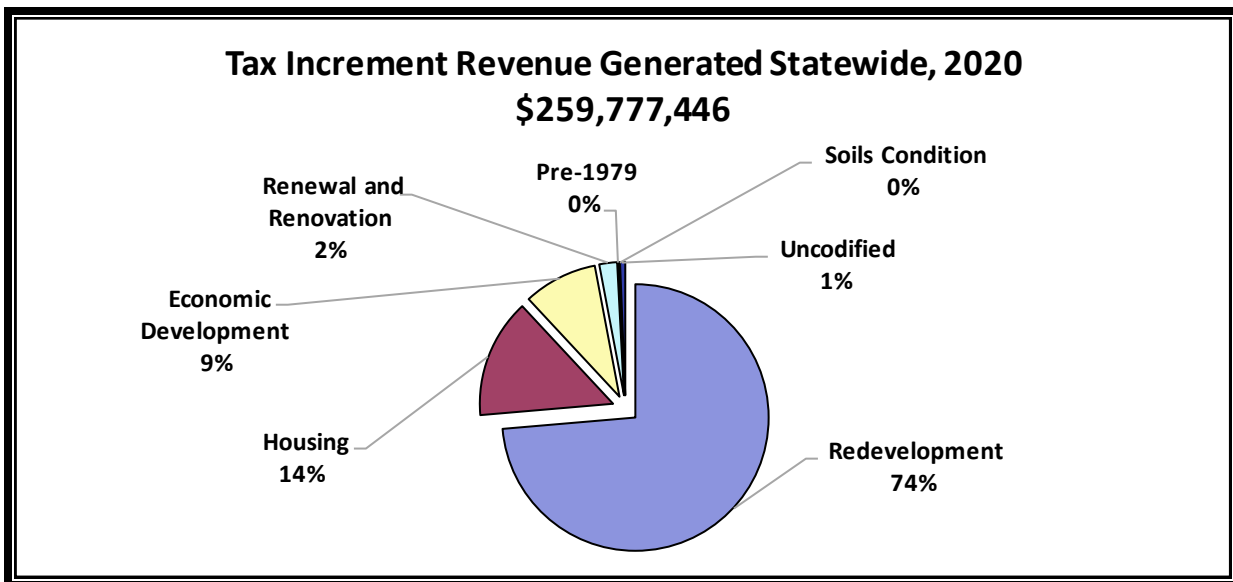




Figure 14.

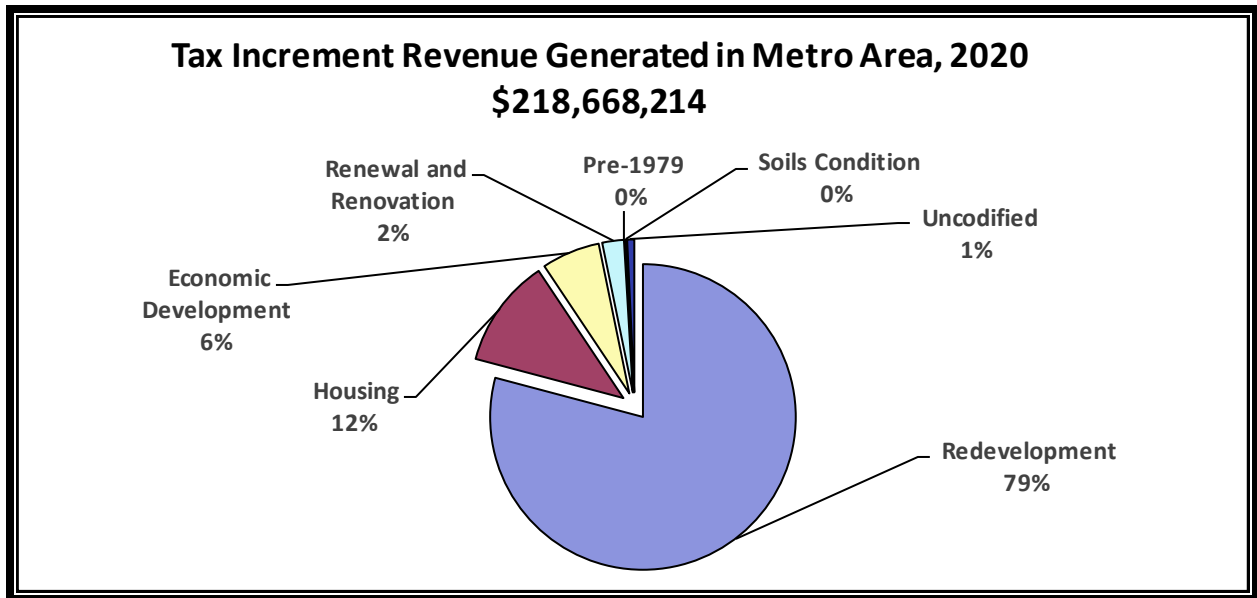
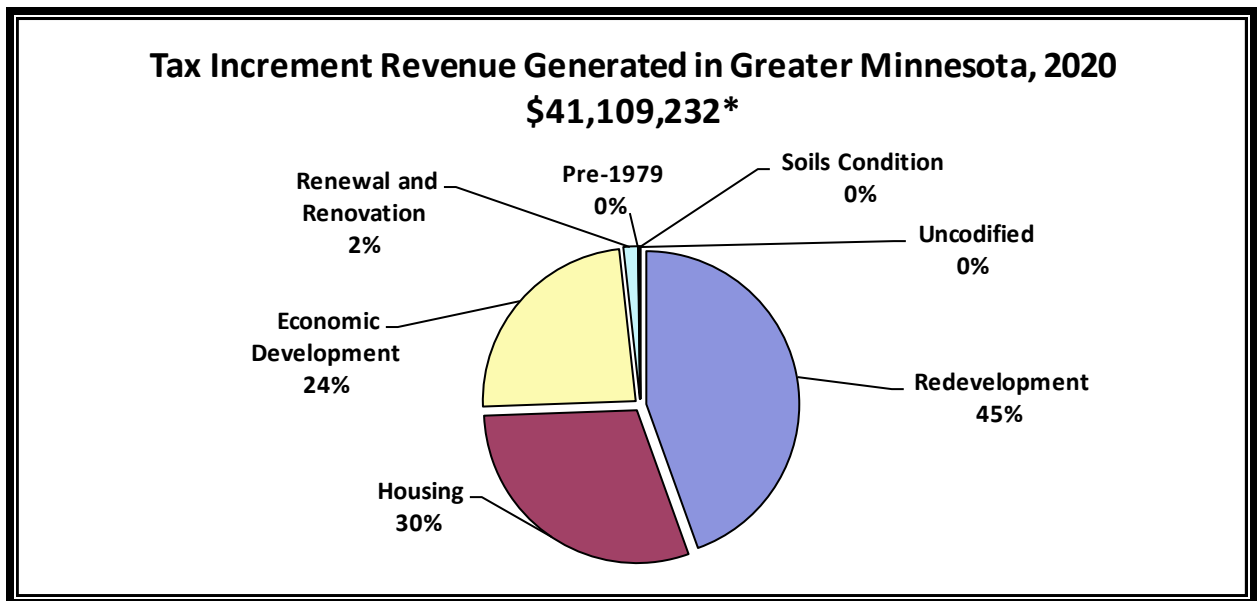


Figure 15.



\*Due to rounding, the sum of the percentages does not equal 100 percent.

In 2020, tax increment revenue increased nearly seven percent over the approximately \$243 million generated in 2019. As seen in Figure 16, the 2020 total surpassed \$250 million for the first time since 2011, and marked the largest tax increment revenue total over the past ten years.

Figure 16.

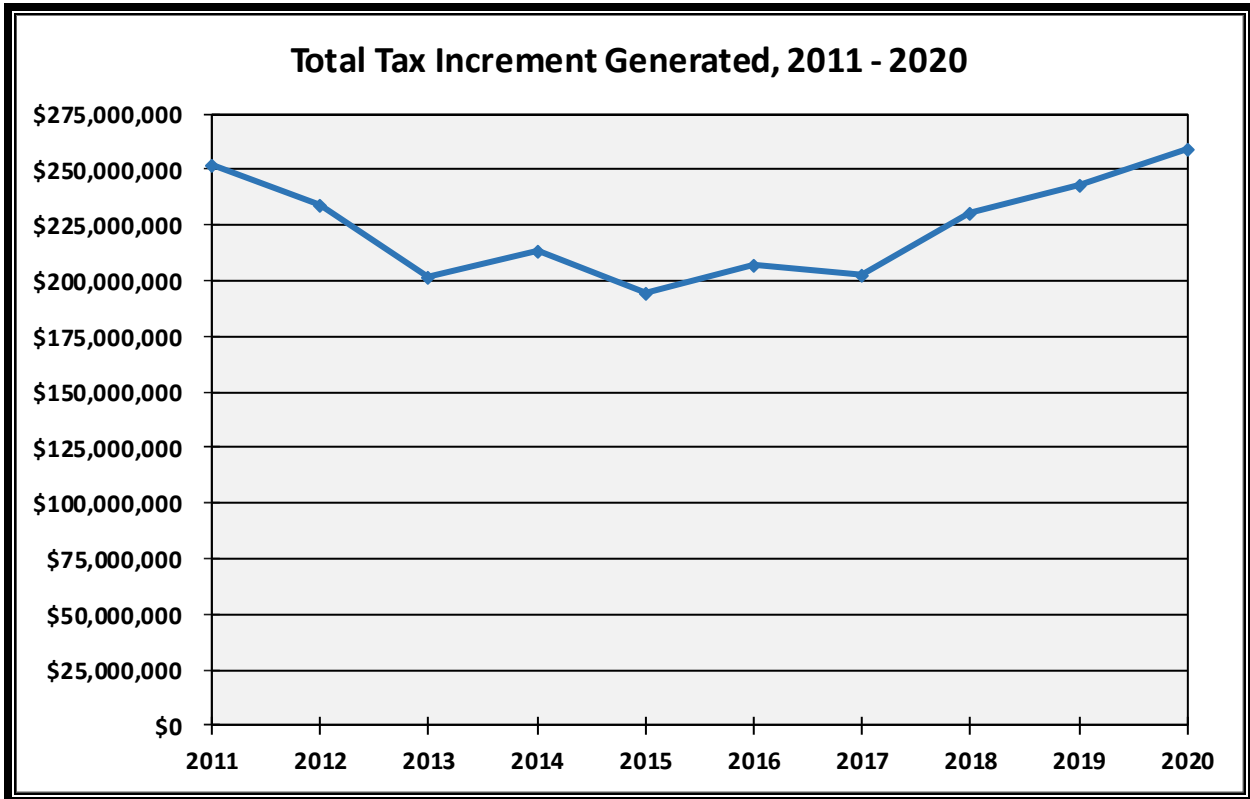
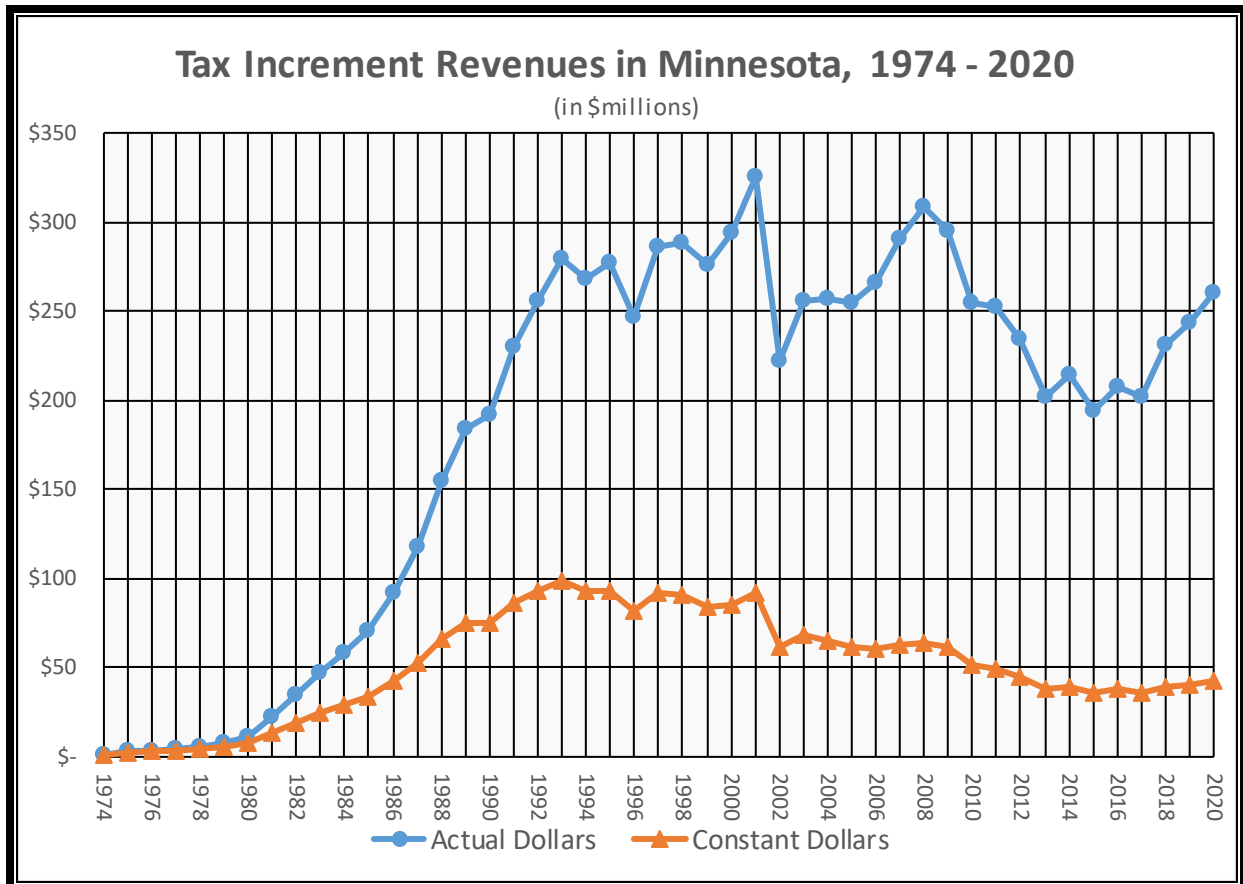


Figure 17 provides a longer view of tax increment revenue, illustrating the fully-recorded span of TIF usage in Minnesota, both in actual dollars and inflation-adjusted, or constant, dollars.<sup>40</sup> The substantial decline in revenue in 2002 reflects the impact of class rate reductions from the 2001 property tax reforms. Otherwise, actual tax increment revenues were generally rising until they reached a peak in 2008, just a few years after the number of districts peaked in 2004. The 2020 increase is the third consecutive increase after a five-year stretch of modest ups and downs.

<sup>40</sup> "Inflation-adjusted" and "constant dollars" refer to data adjusted for inflation using the Implicit Price Deflator for State and Local Governments setting 1974 as the base year (N.I.P.A. Table 1.1.9, October 2021).

Figure 17.



Sources: Minnesota Department of Revenue, *Property Taxes Levied in Minnesota*; 2003 Assessments, Taxes Payable 2004; Property Tax Bulletin No. 33; Table 22 (for 1995 and prior year actual dollars); and TIF annual reporting by development authorities to the OSA (for 1996 - 2019 actual dollars).<sup>41</sup> Constant dollars have been calculated by the OSA.

### Returned Tax Increment

In 2020, development authorities returned \$8,388,322 in tax increment revenue to county auditors for redistribution as property taxes to the cities, counties, and school districts. Tax increment revenue must be returned when a district receives excess tax increment revenue (increment in excess of the amount authorized in the TIF plan for expenditures) or when tax increment revenue is improperly received (such as increment received after the district should have been decertified) or improperly spent (such as for purposes not permitted by law).

<sup>41</sup> The actual dollars for 1995 and prior are the reported tax increment taxes payable, as compiled by the Department of Revenue from county reporting. This differs slightly from 1996 and later data, which reflects the tax increment revenues received by development authorities, as reported to the OSA. The drop in 1996 may reflect some of this discrepancy in the data, but the data is otherwise similar enough to illustrate the overall trends.

## Reported Debt

Tax increment is used primarily to pay for the up-front qualifying costs (such as land acquisition, site improvements, and public utility costs) that make new development a reality. Tax increment revenue, however, is not generally realized until after the new development is completed, assessed, and property taxes are paid. Therefore, up-front qualifying costs are paid with debt obligations or bonds. The types of bonds used, and the associated risk of tax increment revenues potentially being insufficient to pay the bonds, are important topics in tax increment financing.

The TIF Act defines bonds broadly to include:<sup>42</sup>

- General Obligation (GO) Bonds
- Revenue Bonds
- Interfund Loans
- Pay-As-You-Go (PAYG) Obligations
- Other Bonds

**General Obligation Bonds** – A GO bond pledges the full faith and credit of the municipality as security for the bond. If tax increment is not sufficient to make the required debt service payments, the municipality must use other available funds or levy a property tax to generate the funds to pay the required debt service payments.

**Revenue Bonds** – A revenue bond generally includes a pledge of only the tax increment revenue generated from the TIF district (and possibly other revenues like special assessments) for the required debt service payments and does not pledge the full faith and credit of the municipality as security for the bond.

**Interfund Loans** – An interfund loan is created when an 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 not later than 60 days after money is transferred, advanced, or spent. The terms and conditions for repayment of the loan must be in writing and include, at a minimum, the principal amount, the interest rate, and maximum term.<sup>43</sup> The authority or municipality bears the risks if the tax increment generated is not sufficient to repay the interfund loan.

**Pay-As-You-Go Obligations** – With a PAYG obligation, 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 reimbursed from tax increments pursuant to the terms of the PAYG note. Generally, in PAYG financing, the developer or note holder accepts the risks, and will not be reimbursed in full if sufficient tax increments are not generated as anticipated.

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<sup>42</sup> See Minn. Stat. § 469.174, subd. 3.

<sup>43</sup> Minn. Stat. § 469.178, subd. 7. Terms may be modified or amended.

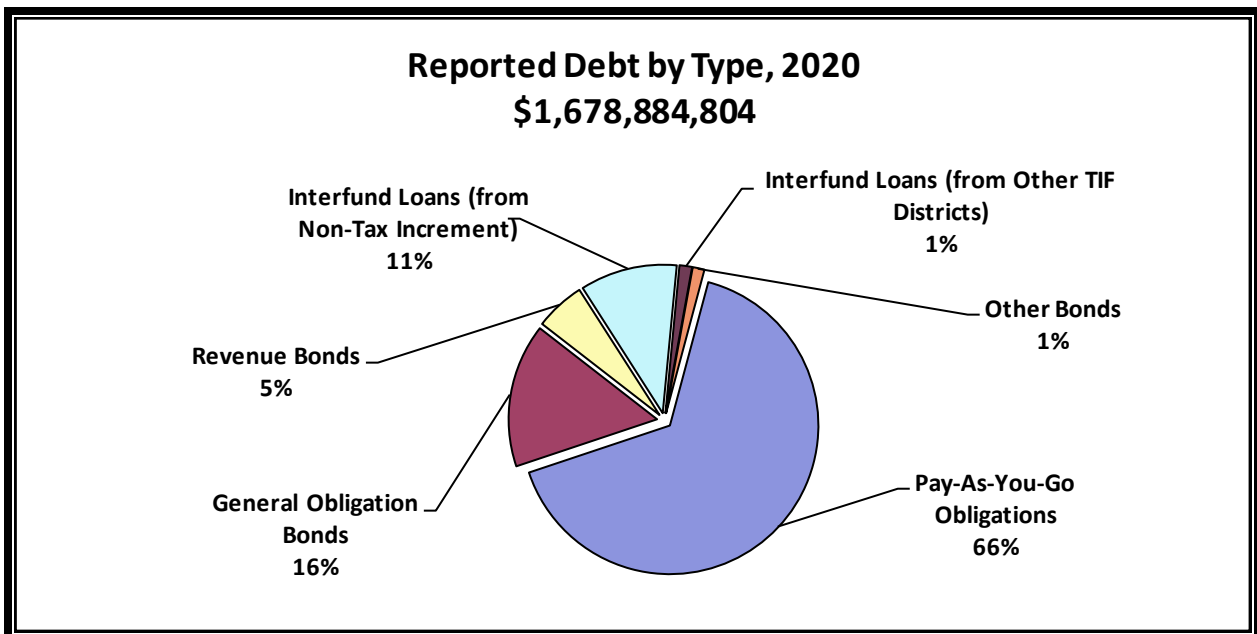
**Other Bonds** – Other bonds include various loans and other miscellaneous reported debts.

Figures 18 and 19 identify and illustrate the amount of debt by type of obligation for 2020. In 2020, there was a total of nearly \$1.7 billion of outstanding debt associated with TIF districts. PAYG obligations were the predominant type of debt, making up 66 percent of the debt reported (up from 64 percent in 2019). GO bonds comprised about 16 percent of the total debt. Interfund loans (mostly from non-tax increment accounts) made up 12 percent of total debt. Revenue bonds made up five percent of total debt, and other bonds made up the rest.

**Figure 18.**

<b>Reported Amount of Debt by Type, 2020</b>	
<b>Type of Debt</b>	<b>Amount Outstanding</b>
Pay-As-You-Go Obligations	\$1,103,145,289
General Obligation Bonds	\$262,382,409
Revenue Bonds	\$91,394,989
Interfund Loans (from Non-Tax Increment)	\$177,364,916
Interfund Loans (from Other TIF Districts)	\$22,845,853
Other Bonds	\$21,751,348
<b>Total</b>	<b>\$1,678,884,804</b>

**Figure 19.**



## FINDINGS AND RESPONSES

The OSA oversees TIF and conducts reviews on the use of TIF by development authorities. Communication between the OSA and the development authorities often resolves issues identified in these reviews. Proactive steps by an authority to remedy potential problems often eliminate the need for the OSA to make formal findings and pursue compliance remedies. However, if an authority is not in legal compliance with the TIF Act, the OSA generally sends an initial notice of noncompliance (Initial Notice) to the governing body of the municipality that approved the TIF district in which the violation arose. The Initial Notice provides the findings and their bases, 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 must indicate the basis for any disagreement with the findings. After consideration of the Response, the OSA sends its final notice of noncompliance (Final Notice) to the municipality indicating whether issues are considered resolved. In addition, the OSA forwards information regarding unresolved findings of noncompliance to the appropriate county attorney who may bring an action to enforce the TIF Act. If the county attorney does not commence an action against the authority or otherwise resolve the finding(s) within one year after receiving a referral of a Final Notice, the OSA notifies the Attorney General and provides materials supporting the violation determinations.

### Summary of Findings and Responses

State law requires the OSA to provide a summary of the responses to notices of noncompliance it received from the municipalities and copies of the responses themselves to the chairs of the legislative committees with jurisdiction over tax increment financing.<sup>44</sup> This section of the Report summarizes the TIF legal compliance reviews and investigations concluded as of December 31, 2021. An Initial Notice and Final Notice were sent to the following municipalities:

1. City of Canby – An Initial Notice was sent on February 5, 2021. A Response from the City of Canby was received on March 22, 2021. A Final Notice was sent on March 31, 2021. (Appendix A.)
2. City of Dassel – An Initial Notice was sent on February 19, 2021. A Response from the City of Dassel was received on March 2, 2021. A Final Notice was sent on March 5, 2021. (Appendix B.)
3. City of Ironton – An Initial Notice was sent on October 7, 2021. The City of Ironton did not provide a written response within the required 60 days. A Final Notice was sent on December 23, 2021. (Appendix C.)

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<sup>44</sup> Minn. Stat. § 469.1771, subd. 1(c).

## **Excess Increment**

### **City of Canby**

#### *TIF District 1-4*

In the Initial Notice, the OSA found that the City of Canby, through 2019, had failed to return excess increment equaling \$237,057 for TIF District 1-4 in violation of the TIF Act.

In the City Response, the City accepted the findings of noncompliance and provided documentation that \$237,057 was returned to the Yellow Medicine County Auditor. The OSA considered this Finding resolved.

### **City of Canby**

#### *TIF District 1-12*

In the Initial Notice, the OSA found that the City of Canby had failed to return excess increment equaling \$5,486 for TIF District 1-12 in violation of the TIF Act.

In the City Response, the City accepted the findings of noncompliance and provided documentation that \$5,486 was returned to the Yellow Medicine County Auditor. The OSA considered this Finding resolved.

## **Administrative Expense Limit Exceeded**

### **City of Dassel**

#### *TIF District 7-1*

In the Initial Notice, the OSA found that the City of Dassel expended \$2,702 of tax increment from TIF District 7-1 in violation of the limit on administrative expenses.

In the City Response, the City agreed with the findings of noncompliance and returned the tax increment to the Meeker County Auditor. The OSA considered this Finding resolved.

## **Improper Use of Tax Increment**

### **City of Dassel**

#### *TIF District 7-1*

In the Initial Notice, the OSA found that the City of Dassel used \$3,266 of tax increment from TIF District 7-1 in violation of the TIF Act.

In the City Response, the City agreed with the findings of noncompliance and returned the tax increment to the Meeker County Auditor. The OSA considered this Finding resolved.

## **Improper Use of Tax Increment**

### **City of Ironton**

#### *TIF District 5*

In the Initial Notice, the OSA found that the City of Ironton used \$16,077 of tax increment from TIF District 5 in violation of the TIF Act.

Although the City did not provide a written response, the City returned the tax increment to the Crow Wing County Auditor. The OSA considered this Finding resolved.

## **Failure to Decertify the District in a Timely Manner**

### **City of Ironton**

#### *TIF District 5*

In the Initial Notice, the OSA found that the City of Ironton received \$20,263 of tax increment from TIF District 5 in violation of the TIF Act.

Although the City did not provide a written response, the City returned the tax increment to the Crow Wing County Auditor. The OSA considered this Finding resolved.



# **APPENDIX A**



February 5, 2021

The Honorable Nancy Bormann, Mayor  
The Honorable Diana Fliss, Council Member  
The Honorable Denise Hanson, Council Member  
The Honorable Dillan Meyer, Council Member  
The Honorable Alex J. Renaas, Council Member

**City of Canby**

110 Oscar Avenue North  
Canby, MN 56220

Re: City of Canby TIF Districts – Initial Notice of Noncompliance

Dear Mayor Bormann and Council Members:

The Office of the State Auditor (OSA) has examined the tax increment financing (TIF) plans, bond documents, audited financial reports, annual reporting forms, and other information regarding various TIF districts created by the City of Canby (City) and the City of Canby's Housing and Redevelopment Authority (HRA). After reviewing this information, the OSA finds that the City and HRA appear to be out of compliance with the TIF Act.<sup>1</sup> This Initial Notice of Noncompliance (Initial Notice) contains two OSA findings (Findings) and four comments (Comments).

State law requires the City to send its response to the Initial Notice (Response) in writing within 60 days after receipt of the Initial Notice. The Response must state whether the City accepts the OSA's Findings, in whole or in part, and the basis for any disagreement.<sup>2</sup> After reviewing the Response, the OSA is required to forward information on any unresolved issues to the Yellow Medicine County Attorney for review.<sup>3</sup>

If the City pays to Yellow Medicine County (County) an amount equal to the amount found to be in noncompliance, the OSA will consider the Finding to be resolved. Minnesota law provides that the City will receive 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 Initial Notice.<sup>4</sup>

All data relating to this examination, including this Initial Notice and the City's Response, are not public until the OSA has issued its Final Notice.<sup>5</sup>

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<sup>1</sup>See Minn. Stat. §§ 469.174 to 469.1799 inclusive, as amended.

<sup>2</sup>Minn. Stat. § 469.1771, subd. 1 (c).

<sup>3</sup>Minn. Stat. § 469.1771, subd. 1 (b).

<sup>4</sup>Minn. Stat. § 469.1771, subd. 5.

<sup>5</sup>See Minn. Stat. § 6.715 (Information relating to an examination is confidential and/or protected 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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February 5, 2021  
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### FINDINGS OF NONCOMPLIANCE

The OSA's findings of noncompliance are as follows:

#### **Finding 1. City of Canby TIF District No. 1-4 – Excess Increment**

Excess increment is the amount of increment that exceeds the amount necessary to pay the costs authorized in the TIF plan.<sup>6</sup> The amount of excess increment is calculated by subtracting the total authorized costs, (less any amounts paid from other sources or due at a later date), from the total tax increment collected through the end of a calendar year.<sup>7</sup> Excess increment must be returned to the county auditor or be used to prepay, discharge, or escrow funds for any outstanding bonds within nine months after the end of each year.<sup>8</sup>

According to TIF Annual Reporting forms for the City's TIF District No. 1-4, the district has had excess increment each year since 2014, but has not returned excess increment within nine months of each year as is required by statute. As of December 31, 2019, the reported excess increment was up to \$467,057. That amount, however, appears to be overstated due to the City's inaccurate reporting of the TIF Plan authorized costs (reported as \$382,080). The City had not updated its reported TIF Plan authorized costs to reflect Modification #2 of the TIF Plan on May 15, 2012.<sup>9</sup> Modification #2 changed the total authorized costs under the Plan to be \$612,080.<sup>10</sup> Based on this amount and the City's reported amount of principal and interest due after the end of 2019, excess increment as of December 31, 2019, appears to be \$237,057. The City's TIF reports and representations indicate that no excess increment has been returned to the county auditor since the district's inception.

We find that, for increments received since inception and through 2019, the City of Canby has failed to return excess increment equaling \$237,057 for the City's TIF District No. 1-4, in violation of the TIF Act. Therefore, the City must return this amount to the county auditor. The county auditor shall then redistribute these returned funds in the manner provided by the TIF Act based on the City's Response to this Notice.<sup>11</sup>

When the City provides documentation that it returned **\$237,057** to the Yellow Medicine County Auditor, the OSA will consider this Finding resolved.

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<sup>6</sup>Minn. Stat. § 469.176, subd. 2.

<sup>7</sup>Ibid.

<sup>8</sup>Ibid.

<sup>9</sup>In the original TIF plan and its first modification, "budget" amounts in subsection 2.7 (Estimated Project Cost) failed to provide clear and separate identification of costs of the project versus interest as a financing cost. Amounts for fund reserves (capitalized interest) had been included in the total "Project Cost," (first as \$40,000, then increased to \$55,000), but the subsection did not include the \$212,080 of interest expenses reflected in Exhibit 3 (Tax Increment Bond Cash Flow Schedule) of the plan. After Modification #2, subsection 2.7 now presents separate estimates of project costs (\$240,000) and interest expenses (\$160,000), although it is not clear whether the identified interest expense is meant to represent total authorized interest or just a separation of the capitalized interest amount from project costs. As a total it would represent a significant reduction (from \$55,000 + \$212,080), but as a reference to capitalized interest it would be a significant increase (from \$55,000).

<sup>10</sup>Modification #2 did not alter Exhibit 3 but did increase subsection 2.8's estimate of indebtedness to match the new total of subsection 2.7 (\$400,000). This implies that the interest amount in subsection 2.7 is capitalized interest and omits regular interest identified in Exhibit 3. Adding the interest from Exhibit 3 (\$212,080) yields the apparent total of authorized costs (\$612,080).

<sup>11</sup>See Minn. Stat. § 469.1771, subd. 5.

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Mayor and Council, City of Canby  
February 5, 2021  
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In addition to resolving the current Finding, the City should be aware of and take steps to avoid future, related non-compliance issues, as described in footnote 12.<sup>12</sup>

### **Finding 2. City of Canby TIF District No. 1-12 – Excess Increment**

Unreturned excess increment also appears to be an issue for the City's TIF District No. 1-12. According to TIF Annual Reporting forms for the City's TIF District No. 1-12, the district had excess increment starting in 2017, but has not returned excess increment within nine months of each year-end as required by statute. As of December 31, 2019, the reported excess increment was \$7,486. That amount, however, also appears to be overstated due to inaccurate reporting of authorized costs, and should have been \$5,486.<sup>13</sup> Excess increment had not been reported as returned in prior years and communications with City representatives suggested this is the case for 2019 excess increment as well.

We find that the City of Canby has failed to return excess increment equaling \$5,486 for the City's TIF District No. 1-12, in violation of the TIF Act. Therefore, the City must return \$5,486 to the county auditor. The county auditor shall then redistribute these returned funds in the manner provided by the TIF Act based on the City's Response to this Notice.<sup>14</sup>

When the City provides documentation that it returned **\$5,486** to the Yellow Medicine County Auditor, the OSA will consider this Finding resolved.

### **ADDITIONAL COMMENTS**

In addition to making the Findings set forth above, the OSA makes the following observations:

#### **Comment 1. Inaccurate Reporting and Record Keeping**

Reporting for numerous districts has shown inconsistencies with audited financial statements and has been marked by numerous adjustments to prior year amounts. For TIF 1-4, for example, differences between TIF reporting and audited financial statements were seen frequently for principal and interest payments, fund balances, bond proceeds, and other amounts. Prior year adjustments were made in each year from 1998 to 2002, 2005, 2009 and 2010. A letter relating to the 2003 audited financial statements indicated the auditors "were unable to obtain sufficient data to audit the activities of the TIF Districts for the City of Canby."<sup>15</sup>

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<sup>12</sup>Based on the district's reporting of authorized costs and obligations, continued collection of excess increment appears likely until decertification. Future excess increments should be used only as permitted or returned as prescribed by Minn. Stat. § 469.176, subd. 2. In addition, the City should be aware of pooling restrictions on current and future tax increment balances that restrict the proportion of increment that may be spent for what are considered "out-district" expenses or costs. Minn. Stat. § 469.1763, subd. 4(a), the "Six-Year Rule" provision, places additional limits on permissible uses of increment starting in the sixth year following certification of the district. In general, it also provides that when these permissible uses have been exhausted, the district must be decertified.

<sup>13</sup>The reported amount of authorized costs appears to omit \$2,000 of capitalized interest expense, which when incorporated, reduces the excess increment by that amount.

<sup>14</sup>See Minn. Stat. § 469.1771, subd. 5.

<sup>15</sup>Letter dated May 5, 2004, from Nicole Larson of Kinner & Company Ltd to the City of Canby, attn.: Barbara Hoyhtya.

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Mayor and Council, City of Canby

February 5, 2021

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There also appears to be a disconnect between reported activities and the budgets and expected bond payment schedules found in TIF plans. For TIF districts 1-8, 1-9, 1-11, 1-12, and 1-14, interfund loans are the sole reported obligations of the districts but annual payments are not occurring despite schedules included in the TIF plan that provide for annual payments. For many districts, it is unclear if bond or loan proceeds ever provided capitalized interest or administrative expense funds as identified in the TIF plans, or how accurate reported expenditures may be.

Several reports for 2019 remained outstanding as of October 1, 2020, requiring a hold on tax increment distributions.<sup>16</sup>

For all HRA and City TIF districts, there is no reporting of out-district costs in the Project Costs Tab despite activity suggesting there are pooled expenditures.

For the HRA TIF districts and TIF 1-26 and 1-27 of the City, the reporting of the required decertification date appears to be inaccurate given the expected or actual timing of first receipt of tax increment.<sup>17</sup> This may stem in part from TIF plan language that typically anticipates decertification is required one year earlier than what statute allows.<sup>18</sup> For many City and HRA districts, the required decertification dates reported by the City to the OSA are also inconsistent with what the county is reporting. We recommend the City review all decertification dates and work with the county auditor to correct records as appropriate.<sup>19</sup>

A number of additional reporting issues are also noted.<sup>20</sup>

Any city, especially one as active as Canby is with the use of tax increment financing, must commit to detailed record keeping and reporting accuracy.

The City is not required to respond to this Comment in its Response.

### **Comment 2. Noncompliance with Interfund Loan Requirements**

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<sup>16</sup>The final reports for 2019 were received on January 15, 2021, and notices were sent to release withheld increment.

<sup>17</sup>Required decertification dates appear to be inaccurate for HRA districts 1-3, 1-4, 1-5, 1-8, 1-9, 1-10, and 1-11.

<sup>18</sup>Statute expresses duration limits as prohibiting increment from being paid after a certain number of years (based on type of district) after receipt of the first increment. Because the stated number of years is after the first receipt year and does not count the first receipt year, one more than the stated number of years is allowed to be collected. The TIF plans have identified expected required decertification years as if only the stated number of years of collections is allowed. See Minn. Stat. § 469.176, subd. 1b. In other instances, discrepancies in reported years may reflect actual first receipt occurring in a different year than the expected year.

<sup>19</sup>Discrepancies were noted for HRA districts 1-1, 1-8, 1-9, and 1-10, and City districts 1-6, 1-8, 1-9, 1-11, 1-18, and 1-28. Also note that in some cases the reported dates are consistent between the county and City/HRA date, but both appear inconsistent with actual limits.

<sup>20</sup>For TIF 1-26, the addition in the Debt Tab for the 2014C bond should be removed. For TIF 1-29, first increment was reported for 2019 but put on the interest income line. Recently-received, belated reports for several district reflect adjustments to interest and revised amortization schedules as noted under Comment 2, but these adjustments include reporting an "Other" amount on line 25 of the Revenues & Expenditures Tab, presumably to balance reporting, when adjustments to prior year amounts would be more accurate.

## OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Canby

February 5, 2021

Page 5

Interfund loan provisions were added to the TIF Act in 2001 and require: approval by resolution before or within 60 days of money being transferred, advanced, or spent; written documentation of the terms and conditions for repayment; and maximum rates of interest.<sup>21</sup> In each of the audited financial statements since 2014, noncompliance with these requirements has been identified.

For TIF districts 1-8, 1-9, 1-11, 1-12, and 1-14, interfund loans are the sole obligations of the districts. The City has not complied with their TIF plan schedules for annual payments of principal, and has made potentially unauthorized prior year additions to principal for large, unplanned accruals of interest at high interest rates.<sup>22</sup> To the City's credit, it took action in December to decertify these districts, and in belated 2019 reporting, identified revised amortization schedules that reduced interest due for 2020. These actions serve to avert further noncompliance concerns.<sup>23</sup> The City should apply similar evaluations to all of its interfund loans.

The City is not required to respond to this Comment in its Response.

### **Comment 3. TIF 1-25 Activity Exceeds TIF Plan Estimates**

In the TIF plan for TIF 1-25, the estimated amount of bonded indebtedness is \$560,000, which corresponds with estimated costs of \$75,000 for site acquisition, \$320,000 of improvements, \$115,000 of capitalized interest, and \$50,000 of administrative expenses.

According to the 2019 TIF Annual Reporting Form, a pooled general obligation TIF bond was issued with \$1.1 million of proceeds going to TIF 1-25 for project costs that include \$72,817 for acquisition, \$519,759 for improvements, and \$62,376 for administrative costs. It is unclear whether the district, which must decertify by the end of 2023, will receive increment in excess of the plan's authorized costs. However, the activity of this district raises general concerns. Most specifically, an administrative expense limit violation (which is not evaluated until the end of the district) appears likely.

The City is not required to respond to this Comment in its Response.

### **Comment 4. TIF 1-26 Pooling Concerns**

In 2019, a new pooled TIF bond was issued, from which TIF 1-26 received a substantial share of the proceeds. These proceeds far exceed the district's other obligations and sets up likely pooling violations for future years. Pursuant to the Five-Year Rule, a bond must be issued (and its proceeds generally must be used) within five years after certification of the district for tax increment revenues spent to repay the

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<sup>21</sup>See Minn. Stat. § 469.178, subd. 7. Amendments in 2017 allow resolutions to be passed within 60 days of transfers, advances or expenditures where the original language required approval before such action. Interfund loans and advances made before August 1, 2001, were ratified subject to the interest rate limits and a maximum principal amount if no document specified the principal amount of the loan or advance.

<sup>22</sup>The lack of documented terms calls into question the appropriateness of compounding interest and additions to principal may be in excess of the maximum amount of principal that should be included in documented terms.

<sup>23</sup>Noncompliance concerns, beyond failing to maintain proper documentation of loan terms, may include potential for excess amounts of principal payments, excess amounts of interest payments, and improper adherence to the Six-Year Rule (under Minn. Stat. § 469.1763, subd. 4).

## OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Canby  
February 5, 2021  
Page 6

bonds to be considered as having been expended on an activity within the district.<sup>24</sup> Subsequent expenditures are considered out-district, pooling expenditures subject to percentage limitations. The district was certified September 25, 2014, but the bond was issued more than five years later on December 16, 2019. Therefore, scheduled payments will exceed the limits on pooling and represent expenditures in violation of the TIF Act.<sup>25</sup>

To the extent any such violations occurred for 2020, improper payments should be remedied by paying equal amounts to the county auditor.

The City is not required to respond to this Comment in its Response, but future findings are likely if not addressed.

### CONCLUSION

The City's Response to this Finding must be submitted in writing to the OSA within 60 days after receipt of this Initial Notice. The OSA is available to review and discuss the Finding within this letter at any time during the preparation of the Response. After considering the Response, the OSA will issue the Final Notice.

If you have any questions, please contact me at (651) 296-7979 or Jason.Nord@osa.state.mn.us. We look forward to receiving your Response.

Sincerely,

*/s/ Jason Nord*

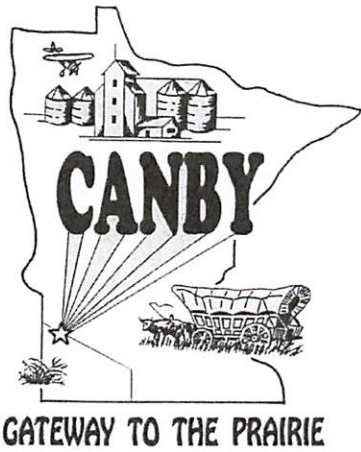
Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Bonnie Merritt, Account Clerk  
Rebecca Schrupp, City Administrator and HRA Executive Director

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<sup>24</sup>See Minn. Stat. § 469.1763, subd. 3.

<sup>25</sup>Such expenditures would appear, based on principal and interest reported as due in 2020, to violate the "Six-Year Rule" under Minn. Stat. § 469.1763, subd. 4(a), and such expenditures would, in time, violate the overall pooling limits of Minn. Stat. § 469.1763, subd. 2.



# City of Canby

March 17, 2021

Mr. Jason Nord  
Assistant State Auditor  
TIF Division Director  
Office of the State Auditor  
Suite 500  
525 Park Street  
St. Paul, Minnesota 55103

RECEIVED  
MAR 22 2021  
OFFICE OF THE STATE AUDITOR

Re: City of Canby TIF Districts – Initial Response to February 5, 2021 Notice of Noncompliance

Dear Jason,

The City of Canby hereby accepts the Office of the State Auditor's findings detailed in the February 5, 2021 Initial Notice of Noncompliance Letter regarding excess tax increment. The city will be addressing the other comments during the annual reporting process.

The City of Canby is returning \$237,057 in excess tax increment for TIF District 1-4, and \$5,486 in excess tax increment for TIF District 1-12 to Yellow Medicine County for redistribution to the taxing authorities.

Attached are photocopies of checks mailed to the Yellow Medicine County Auditor.

Sincerely,

Nancy Bormann  
Mayor





March 31, 2021

The Honorable Nancy Bormann, Mayor  
The Honorable Diana Fliss, Council Member  
The Honorable Denise Hanson, Council Member  
The Honorable Dillan Meyer, Council Member  
The Honorable Alex J. Renaas, Council Member

**City of Canby**

110 Oscar Avenue North  
Canby, MN 56220

Re: City of Canby TIF Districts – Final Notice of Noncompliance

Dear Mayor Bormann and Council Members:

On February 5, 2021, the Office of the State Auditor (OSA) sent the City of Canby (City) an Initial Notice of Noncompliance (Initial Notice) containing two OSA findings (Findings), one each for Tax Increment Financing (TIF) Districts No. 1-4 and 1-12. The OSA received the City's Response (City Response) on March 22, 2021.

This letter is the Final Notice of Noncompliance (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 issues raised by the review.

**FINDINGS OF NONCOMPLIANCE**

Two findings of noncompliance were made:

**Finding 1. City of Canby TIF District No. 1-4 – Excess Increment – RESOLVED**

In the Initial Notice, the OSA found that the City of Canby, through 2019, had failed to return excess increment equaling \$237,057 for TIF District 1-4 in violation of the TIF Act.

In the City Response, the City accepted the finding of noncompliance and provided documentation that \$237,057 was returned to the Yellow Medicine County Auditor. The OSA considers this Finding resolved.

**Finding 2. City of Canby TIF District No. 1-12 – Excess Increment – RESOLVED**

In the Initial Notice, the OSA found that the City of Canby had failed to return excess increment equaling \$5,486 for TIF District 1-12 in violation of the TIF Act.

In the City Response, the City accepted the findings of noncompliance and provided documentation that \$5,486 was returned to the Yellow Medicine County Auditor. The OSA considers this Finding resolved.

**Office of the State Auditor**

Mayor and Council, City of Canby

March 31, 2021

Page 2

**CONCLUSION**

The OSA considers the Findings resolved and appreciates the City's cooperation.

If you have any questions, please contact me at (651) 296-7979 or [Jason.Nord@osa.state.mn.us](mailto:Jason.Nord@osa.state.mn.us).

Sincerely,

*/s/ Jason Nord*

Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Bonnie Merritt, Account Clerk  
Rebecca Schrupp, City Administrator and HRA Executive Director

# **APPENDIX B**



February 19, 2021

The Honorable Ron Hungerford, Mayor  
The Honorable Nicole Carlen, Council Member  
The Honorable James Hallquist, Council Member  
The Honorable Bob Lalone, Council Member  
The Honorable Tom Weseloh, Council Member  
**City of Dassel**  
P.O. Box 391  
Dassel, MN 55325

Re: TIF District No. 7-1 – Initial Notice of Noncompliance

Dear Mayor Hungerford and Council Members:

The Office of the State Auditor (OSA) has examined the tax increment financing (TIF) plan, annual TIF reporting forms, audited financial statements, and tax increment distribution data provided by Meeker County for TIF District 7-1 of the City of Dassel (City). Based on this review, and lacking additional information because of the City's failure to respond to inquiries, the OSA finds that the City is not in compliance with the TIF Act.<sup>1</sup> This Initial Notice of Noncompliance (Initial Notice) contains two findings (Findings) and one additional comment (Comment).

State law requires the City to send its Response in writing within 60 days after receipt of the Initial Notice. The Response must state whether the City accepts the OSA's Findings, in whole or in part, and the basis for any disagreement.<sup>2</sup> After reviewing the Response, the OSA is required to forward information on any unresolved issues to the Meeker County Attorney for review.<sup>3</sup>

If the City pays to Meeker County (County) an amount equal to the amount found to be in noncompliance, the OSA will consider the Findings to be resolved. Minnesota law provides that the City will receive 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 Initial Notice.<sup>4</sup>

All data relating to this examination, including this Initial Notice and the City's Response (Response), are not public until the OSA has issued its Final Notice.<sup>5</sup>

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<sup>1</sup>See Minn. Stat. §§ 469.174 to 469.1799 inclusive, as amended.

<sup>2</sup>Minn. Stat. § 469.1771, subd. 1 (c).

<sup>3</sup>Minn. Stat. § 469.1771, subd. 1 (b).

<sup>4</sup>Minn. Stat. § 469.1771, subd. 5.

<sup>5</sup>See Minn. Stat. § 6.715 (Information relating to an examination is confidential and/or protected 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.).

## Office of the State Auditor

Mayor and Council, City of Dassel  
February 19, 2021  
Page 2

### FINDINGS OF NONCOMPLIANCE

The OSA's Findings of noncompliance regarding TIF District 7-1 is as follows:

#### **Finding 1. TIF District 7-1 – Administrative Expense Limit Exceeded**

The TIF Act limits the amount of tax increment that may be used for administrative expenses to ten percent of the total estimated tax increment expenditures authorized by the TIF plan or the total tax increments distributed from the county, whichever is less.<sup>6</sup> For TIF District 7-1, the limit is ten percent of the \$14,593 of tax increments distributed from the county, or \$1,459.<sup>7</sup> The City has reported expending \$4,161 of tax increments for authority administrative expenses for TIF District 7-1.<sup>8</sup>

We find that the City of Dassel expended \$2,702 of tax increment from TIF 7-1 in violation of the limit on administrative expenses. An amount equal to \$2,702 must be returned to the county auditor.

When the City provides documentation that it returned **\$2,702** to the Meeker County Auditor, the OSA will consider this Finding resolved.

#### **Finding 2. TIF District 7-1 – Improper Use of Tax Increment**

The TIF Act's general limitation on the use of tax increment provides that tax increment revenues must be used in accordance with the TIF plan and, generally, may be solely used: (1) to pay the principal and interest on bonds (including pay-as-you-go notes) issued to finance a project, or (2) to finance or pay capital and administrative costs pursuant to the various development acts found in Minnesota Statutes Chapter 469.<sup>9</sup> If an authority expends tax increment revenues for a purpose not permitted under this and other limitations, the authority must pay to the county auditor an amount equal to the expenditures made in violation of the law.<sup>10</sup>

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<sup>6</sup>Minn. Stat. § 469.176, subd. 3(b).

<sup>7</sup>Ten percent of the total estimated tax increment expenditures authorized by the TIF plan equals \$4,846. This ignores the TIF plan's inclusion of a "Developer/Property Owner Deposit" of \$5,500, which is not tax increment revenue, and the associated administrative costs planned to be paid by that deposit.

<sup>8</sup>The City initially reported expending \$6,371 on administrative expenses in 2007. While the 2007 reporting form identified receipt of \$6,503 of tax increments in one section, it also reported a "Tax Increments Receivable" of \$6,610 and a "Cash Overdraft" of \$6,610 in another section (which suggests an implicit interfund loan was financing the administrative expenses). There was no subsequent reporting of additional administrative expenses. The 2010 and subsequent reporting forms indicated \$2,210 of the \$6,371 of administrative expenditures were paid with other (non-increment) funds, leaving \$4,161 as the amount of administrative expenses paid with tax increment. (The TIF plan had included plans for \$5,500 of administrative costs to be covered by a \$5,500 developer deposit and \$4,848 from tax increments.) The "Cash Overdraft" became a smaller accounts payable beginning with 2010 reporting, and the payable was eventually reduced to zero, suggesting the implicit interfund loan was paid off. Emails to the City seeking clarification of administrative expenses were unanswered.

<sup>9</sup>See Minn. Stat. § 469.176, subd. 4.

<sup>10</sup>Minn. Stat. § 469.1771, subd. 3.

## Office of the State Auditor

Mayor and Council, City of Dassel

February 19, 2021

Page 3

According to reporting by the county auditor, \$14,593 of tax increment was distributed from 2008 through 2016 to the City for TIF District 7-1.<sup>11</sup> The City reported expending \$7,166 to make payments on a pay-as-you-go (PAYG) obligation.<sup>12</sup> The City reported \$4,161 of administrative expenses as being made with tax increment, for a total of \$11,327 of identified expenditures.<sup>13</sup> The district decertified as of December 31, 2015, and subsequent reporting (ending for 2018) indicated no remaining balances of tax increment. Therefore, \$3,266 of tax increment ( $\$14,593 - \$11,327 = \$3,266$ ) appears to have been improperly used.

We find that the City of Dassel has used \$3,266 of tax increment from TIF District 7-1 in violation of the TIF Act. Therefore, the City must return \$3,266 to the county auditor.

When the City provides documentation that it returned **\$3,266** to the Meeker County Auditor, the OSA will consider this Finding resolved.<sup>14</sup>

### ADDITIONAL COMMENT

In addition to making the Findings set forth above, the OSA makes the following observation:

#### **Comment 1. TIF District 7-1 – Inaccurate Reporting**

The City reported receiving a total of \$13,305 of tax increment, but this reporting is inconsistent with data reported by Meeker County that indicated \$14,593 of tax increment was distributed.<sup>15</sup> Amounts matched for 2009-2011 and 2015-2016, but differed in 2007-2008 and 2012-2014. A prior-year adjustment in the 2010 annual reporting seemed to resolve the 2007-2008 discrepancies and essentially confirmed that no 2007 increment was received.<sup>16</sup> The 2012-2014 discrepancies remain unexplained.

The City reporting of tax increment mostly matches the audited financial statements. Most other TIF reporting on the annual reporting forms, for this and other districts, however, does not match the financial statements.<sup>17</sup> Discrepancies are seen in cash balances, receivables, payables, fund balances, and expenditures.

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<sup>11</sup>See the Comment for identification of discrepancies in reported tax increments between the City and the County. County reporting is trusted given other reporting inaccuracies by the City for this and previous districts. See the OSA's 2014 Tax Increment Financing Legislative Report for a prior Notice of Noncompliance.

<sup>12</sup>This includes \$6,639 for interest and \$527 for principal.

<sup>13</sup>See Finding 1 and footnote 8 for additional discussion of administrative expenses. Any other expenditures potentially included in the reported payable amounts that may exceed the reported PAYG and administrative expenditures are unsubstantiated and therefore improper.

<sup>14</sup>This Finding is in addition to the amount of Finding 1, and a total return of \$5,968 is required to resolve both findings.

<sup>15</sup>Meeker County reported tax increment distributions to the OSA on annual County TIF Information Forms.

<sup>16</sup>The City reported receiving \$6,503 of tax increment in 2007 and \$916 in 2008 versus the county reporting of a \$967 distribution in 2008. The 2010 reporting form identified prior year receipts of increment as \$6,452 less than the previously reported amounts.

<sup>17</sup>The financial statements show a combined "TIF Funds" that also included TIF District 5-1 through at least 2008 and TIF District 6-1 through at least 2014.

**Office of the State Auditor**

Mayor and Council, City of Dassel  
February 19, 2021  
Page 4

TIF reporting prior to 2010 included amounts for site improvements, bond interest, and loan/note interest, but this did not match the prior-year activity reported on the 2010 reporting form.<sup>18</sup> Reporting for 2010 and 2011 identified pay-as-you-go principal and interest payments. The only reported activity after 2011 was the declining payable that became an increasing receivable. This implicit interfund loan activity was not properly reported as an interfund loan and it is not clear if an interfund loan was properly authorized.<sup>19</sup> The receivable was eliminated in the 2018 report, which included an “Other” amount explained in a comment as “Transfer in from general fund” to make the report balance.

Beginning with 2010 reporting, the City’s annual reporting of the estimated costs authorized in the TIF plan has omitted estimated amounts for interest costs that were identified in the TIF plan.

Accurate reporting is essential for compliance and oversight of tax increment financing activity.

The City is not required to respond to this Comment.

**CONCLUSION**

The City’s Response to these Findings must be submitted in writing to the OSA within 60 days after receipt of this Initial Notice. The OSA is available to review and discuss the Findings within this letter at any time during the preparation of the Response. After reviewing the Response, the OSA will issue the Final Notice.

If you have any questions, please contact me at (651) 296-7979 or Jason.Nord@osa.state.mn.us. We look forward to receiving your Response.

Sincerely,

*/s/ Jason Nord*

Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Terri Boese, City Administrator

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<sup>18</sup>Pre-2010 reporting identified \$132, \$45, and \$250 of loan/note interest payments for 2007, 2008, and 2009, respectively; \$300 of bond interest payments in 2009; and \$871 and \$2,244 of site improvement expenditures in 2008 and 2009, respectively. By contrast the 2010 report form identified prior activity as a total of \$358 of principal payments and \$3,612 of interest payments on the PAYG obligation.

<sup>19</sup>See Minn. Stat. § 469.178, subd. 7.



## CITY OF DASSEL

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March 2, 2021

Office of the State Auditor  
525 Park Street, Suite 500  
St. Paul, MN 55103

Re: TIF District No. 7-1 – Notice of Noncompliance

Dear Mr. Nord,

This letter is in response to your initial notice of noncompliance dated February 19, 2021 for TIF District No. 7-1 in the City of Dassel.

Dassel City Council agrees with the findings of noncompliance and has reimbursed Meeker County on January 20, 2021 for administrative expenses, which exceeded the limit for TIF District No. 7-1.

Sincerely,

A handwritten signature in blue ink that reads "Terri Boese".

Terri Boese  
City Clerk/Treasurer

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*The city is an equal opportunity provider and employer.*

---

460 3<sup>rd</sup> Street • PO Box 391 • Dassel, MN 55325  
Phone 320.275.2454 • Fax 320.275.2713  
[www.ci.dassel.mn.us](http://www.ci.dassel.mn.us)





Julie Blaha  
State Auditor

Suite 500  
525 Park Street  
Saint Paul, MN 55103

March 5, 2021

The Honorable Ron Hungerford, Mayor  
The Honorable Nicole Carlen, Council Member  
The Honorable James Hallquist, Council Member  
The Honorable Bob Lalone, Council Member  
The Honorable Tom Weseloh, Council Member  
**City of Dassel**  
P.O. Box 391  
Dassel, MN 55325

Re: TIF District No. 7-1 – Final Notice of Noncompliance

Dear Mayor Hungerford and Council Members:

On February 19, 2020, the Office of the State Auditor (OSA) sent the City of Dassel (City) an Initial Notice of Noncompliance (Initial Notice) containing two OSA findings (Findings) for Tax Increment Financing (TIF) District No. 7-1. The OSA received the City's Response (City Response) on March 2, 2021.

This letter is the Final Notice of Noncompliance (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.

#### **FINDINGS OF NONCOMPLIANCE**

Two findings of noncompliance was made:

#### **Finding 1. TIF District 7-1 – Administrative Expense Limit Exceeded – RESOLVED**

In the Initial Notice, the OSA found that the City of Dassel expended \$2,702 of tax increment from TIF 7-1 in violation of the limit on administrative expenses.

In the City Response, the City agreed with the findings of noncompliance and identified that \$7,455 was returned to the Meeker County Auditor, which the OSA confirmed with the County.<sup>1</sup> This amount is sufficient to cover both findings. The OSA considers this Finding resolved.

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<sup>1</sup>The \$7,455 amount matches a higher remedy amount mentioned in a prior email from the OSA to the City as being appropriate if there was a lack of documentation for the maximum administrative expenses allowed. The City appears to have found that this amount is the more appropriate amount to return as documentation of administrative costs may have been lacking.

**Office of the State Auditor**

Mayor and Council, City of Dassel  
March 5, 2021  
Page 2

**Finding 2. TIF District 7-1 – Improper Use of Tax Increment – RESOLVED**

In the Initial Notice, the OSA found that the City of Dassel used \$3,266 of tax increment from TIF District 7-1 in violation of the TIF Act.

In the City Response, the City agreed with the findings of noncompliance and identified that \$7,455 was returned to the Meeker County Auditor, which the OSA confirmed with the County. This amount is sufficient to cover both findings. The OSA considers this Finding resolved.

**CONCLUSION**

The OSA considers the Findings resolved and appreciates the City's cooperation.

If you have any questions, please contact me at (651) 296-7979 or Jason.Nord@osa.state.mn.us.

Sincerely,

*/s/ Jason Nord*

Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Terri Boese, City Administrator

# APPENDIX C

# STATE OF MINNESOTA



**Julie Blaha**  
State Auditor

Suite 500  
525 Park Street  
Saint Paul, MN 55103

October 7, 2021

The Honorable Greg Stanich, Mayor  
The Honorable Shawn Hamdorf, Council Member  
The Honorable Jeff Midthun, Council Member  
The Honorable Eric Heglund, Council Member  
The Honorable Rose Stromberg, Council Member

**City of Ironton**

P.O. Box 97  
Ironton, MN 56455

Re: TIF District No. 5 – Initial Notice of Noncompliance

Dear Mayor Stanich and Council Members:

The Office of the State Auditor (OSA) has examined the tax increment financing (TIF) plan, annual TIF reporting forms, audited financial statements, pay-as-you-go (PAYG) TIF note, and tax increment distribution data provided by Crow Wing County for TIF District 5 of the City of Ironton (City). Based on this review, and lacking additional information because of the City's failure to continue reporting and failure to respond to inquiries, the OSA finds that the City is not in compliance with the TIF Act.<sup>1</sup> This Initial Notice of Noncompliance (Initial Notice) contains two findings (Findings).

State law requires the City to send its Response in writing within 60 days after receipt of the Initial Notice. The Response must state whether the City accepts the OSA's Findings, in whole or in part, and the basis for any disagreement.<sup>2</sup> After reviewing the Response, the OSA is required to forward information on any unresolved issues to the Crow Wing County Attorney for review.<sup>3</sup>

If the City pays to Crow Wing County (County) an amount equal to the amount found to be in noncompliance, the OSA will consider the Findings to be resolved. Minnesota law provides that the City will receive 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 Initial Notice.<sup>4</sup>

All data relating to this examination, including this Initial Notice and the City's Response (Response), are not public until the OSA has issued its Final Notice.<sup>5</sup>

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<sup>1</sup>See Minn. Stat. §§ 469.174 to 469.1799 inclusive, as amended.

<sup>2</sup>Minn. Stat. § 469.1771, subd. 1 (c).

<sup>3</sup>Minn. Stat. § 469.1771, subd. 1 (b).

<sup>4</sup>Minn. Stat. § 469.1771, subd. 5.

<sup>5</sup>See Minn. Stat. § 6.715 (Information relating to an examination is confidential and/or protected nonpublic until the

## OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Ironton  
October 7, 2021  
Page 2

### FINDINGS OF NONCOMPLIANCE

The OSA's Findings of noncompliance regarding TIF District 5 are as follows:

#### **Finding 1. TIF District 5 – Improper Use of Tax Increment**

The TIF Act's general limitation on the use of tax increment provides that tax increment revenues must be used in accordance with the TIF plan and, generally, may be solely used: (1) to pay the principal and interest on bonds (including pay-as-you-go notes) issued to finance a project, or (2) to finance or pay capital and administrative costs pursuant to the various development acts found in Minnesota Statutes Chapter 469.<sup>6</sup> If an authority expends tax increment revenues for a purpose not permitted under this and other limitations, the authority must pay to the county auditor an amount equal to the expenditures made in violation of the law.<sup>7</sup>

The City entered into a development agreement with Ironton Townhomes LP and issued a tax increment revenue note (Note), both dated August 18, 1999.<sup>8</sup> The Note stated that amounts due shall be payable on each February 1 and August 1, commencing August 1, 2002, and continuing through February 1, 2016 (the "Payment Dates").<sup>9</sup> It further indicated, "This Note shall terminate and be of no further force and effect on any date upon which the City shall have terminated the Development Agreement, on the last Payment Date following payment thereon of the Available Tax Increments then due, or on the date that all amounts payable hereunder shall have been paid in full, whichever occurs earliest."<sup>10</sup> This means that the Note should have terminated no later than February 1, 2016; and the City's clerk acknowledged via email that February 1, 2016, is the date the Note should have expired.<sup>11</sup> Additional payments to Ironton Townhomes LP after termination of the Note represent expenditures of tax increment for a purpose not permitted under the TIF Act.

On each payment date, the City was obligated to pay the lesser of "the Available Tax Increments received by the City within the 6-month period preceding said Payment Date" or the sum of unpaid principal, interest, and administrative expenses.<sup>12</sup> The February 1, 2016, payment, therefore should have included the second-half settlement of tax increments distributed by the county in December of 2015. This payment appears to have been reported on the 2015 TIF Annual Reporting Form.<sup>13</sup>

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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).

<sup>6</sup>See Minn. Stat. § 469.176, subd. 4.

<sup>7</sup>Minn. Stat. § 469.1771, subd. 3.

<sup>8</sup>The OSA received a copy of the Note. The development agreement is cited in the Note but was not received or reviewed by the OSA.

<sup>9</sup>See paragraph [3] of the Note.

<sup>10</sup>See paragraph [5] of the Note.

<sup>11</sup>Email from Melissa Knutson to Kurt Mueller dated April 10, 2019.

<sup>12</sup>See paragraph [4] of the Note.

<sup>13</sup>In 2015 and 2016, payments of interest on the Note for each year matched the reporting of increment received for each of those years, less the administrative expenditures, and did not change the cash balances. If February payments were reported for the following year, the reporting of payments would either align with half-year

## OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Ironton  
October 7, 2021  
Page 3

The City continued to report payments of interest pursuant to the Note on their 2016 and 2017 TIF Annual Reporting Forms, of \$8,061 and \$8,500 respectively. After adjusting for the inclusion of non-TIF revenues, the amount of tax increments expended in each year appears to be \$8,059 and \$8,018, respectively.<sup>14</sup> The City has not submitted subsequent TIF Annual Reporting Forms so it remains unclear if additional expenditures were made on the terminated Note.<sup>15</sup>

We find that the City of Ironton has used \$16,077 of tax increment from TIF District 5 in violation of the TIF Act. Therefore, the City must pay \$16,077 to the county auditor.

When the City provides documentation that it returned **\$16,077** to the Crow Wing County Auditor, the OSA will consider this Finding resolved.<sup>16</sup>

### **Finding 2. TIF District 5 – Failure to Decertify the District in a Timely Manner**

The TIF Act requires a TIF District to be decertified and the pledge of tax increment discharged when sufficient money has been set aside to pay, based on the increment to be collected through the end of the calendar year, qualifying obligations incurred within the first five years of the district.<sup>17</sup> If an authority includes or retains property in a TIF district that does not qualify for inclusion or retention within the district, the authority must pay to the county auditor an amount equal to the increment collected from the property for the year or years.<sup>18</sup>

TIF District 5 had no other obligations other than the single pay-as-you-go Note referenced in Finding 1, and reported no other expenditures except for administrative expenses. The district therefore should have been decertified no later than 2016 when the Note terminated. The district was not decertified until 2019, resulting in the improper receipt of increment in 2017, 2018, and 2019. According to the reporting of tax increment distributions by Crow Wing County, the City received increment totaling \$20,263 for these three years.<sup>19</sup> In addition, there is a portion of 2019 tax increment that was withheld, and continues

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increments for two years, or the cash balance would have been affected.

<sup>14</sup>Tax increment revenues reported on the TIF Annual Reporting Forms appear to have included receipts of excess TIF taxes. Excess TIF taxes are not tax increment revenue. Tax increment revenue is limited to the tax on captured value resulting from the lesser of the current or original tax rates, and when the current rate is higher than the original rate, the excess taxes on the captured value caused by the difference in the rates is distributed as excess taxes. See Minn. Stat. § 469.1763, subdivision 3 (Limiting tax increment to the lesser of the local taxing rates or the original local tax rate), and subd. 9 (Identifying distribution of the excess taxes).

<sup>15</sup>The audited financial statements indicate expenditures of \$101 in 2018, \$20,875 in 2019, and a remaining balance of \$1,357. However, property tax revenues in the fund appear to exceed amounts reported as having been distributed by the county. Finding 2 supplants the need to identify specific expenditures after 2016.

<sup>16</sup>The 2017 portion of this Finding is also included in Finding 2, and a total return of \$28,322 is required to resolve both findings.

<sup>17</sup>Minn. Stat. § 469.1763, subd. 4(b).

<sup>18</sup>Minn. Stat. § 469.1771, subd. 2.

<sup>19</sup>The county reports tax increment distributions annually to the OSA. The City reported receiving amounts that differed from the county-reported distributions, and apparently included receipts of excess TIF taxes and possibly other revenues.

## OFFICE OF THE STATE AUDITOR

Mayor and Council, City of Ironton  
October 7, 2021  
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to be held, by the county auditor pursuant to notifications required when the 2018 and subsequent TIF Annual Reporting Forms were not submitted.<sup>20</sup> Receipt of this additional \$3,969 of increment would also be improper and ultimately requires follow-up resolution.

We find that the City of Ironton failed to decertify TIF 5 when required and received \$20,263 of tax increment in violation of the TIF Act. Therefore, the City must return \$20,263 to the county auditor.

When the City provides documentation that it returned **\$20,263** to the Crow Wing County Auditor, the OSA will consider this Finding resolved.<sup>21</sup> The county auditor shall then redistribute these returned funds and the \$3,969 of increment it has withheld from the district in the manner provided by the TIF Act based on the City's Response to this Notice.<sup>22</sup>

### CONCLUSION

This Initial Notice of Noncompliance contains two Findings requiring a total payment to the Crow Wing County Auditor of **\$28,322** to remedy the violations. If the City provide documentation that it has paid \$28,322 to the Crow Wing County Auditor, the OSA will consider the Findings resolved.

The City's Response to these Findings must be submitted in writing to the OSA within 60 days after receipt of this Initial Notice. The OSA is available to review and discuss the Findings within this letter at any time during the preparation of the Response. After reviewing the Response, the OSA will issue the Final Notice.

If you have any questions, please contact me at (651) 296-7979 or Jason.Nord@osa.state.mn.us. We look forward to receiving your Response.

Sincerely,

*/s/ Jason Nord*

Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Amanda Meyer, City Clerk/Treasurer

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<sup>20</sup>Per an email from Melonie Flaws on 9/23/21, the county has withheld \$3,968.74 pursuant to notifications required under Minn. Stat. § 469.1771, subd. 2a.

<sup>21</sup>This Finding includes \$8,018 of the amount for Finding 1, and a total return of \$28,322 is required to resolve both findings.

<sup>22</sup>See Minn. Stat. § 469.1771, subd. 5.



December 23, 2021

The Honorable Greg Stanich, Mayor  
The Honorable Shawn Hamdorf, Council Member  
The Honorable Jeff Midthun, Council Member  
The Honorable Eric Heglund, Council Member  
The Honorable Rose Stromberg, Council Member

**City of Ironton**

P.O. Box 97  
Ironton, MN 56455

Re: TIF District No. 5 – Final Notice of Noncompliance

Dear Mayor Stanich and Council Members:

On October 7, 2021, the Office of the State Auditor (OSA) sent the City of Ironton (City) an Initial Notice of Noncompliance (Initial Notice) containing two OSA findings (Findings) for Tax Increment Financing (TIF) District 5. The OSA did not receive a written response from the City within the required 60 days, nor as of the date of this notice. However, the OSA learned from the City, and confirmed with the County, that a payment of \$28,322 was made to remedy the findings within the 60-day period.

This letter is the Final Notice of Noncompliance (Final Notice) of the Office of the State Auditor. It summarizes the initial findings and the City's responsive payment, and provides the OSA's final conclusion regarding the issues raised by the review.

**FINDINGS OF NONCOMPLIANCE**

Two findings of noncompliance were made:

**Finding 1. TIF District 5 – Improper Use of Tax Increment – RESOLVED**

In the Initial Notice, the OSA found that the City of Ironton used \$16,077 of tax increment from TIF District 5 in violation of the TIF Act.

Although the City did not provide any written response to date, the OSA has confirmed with the county that the City returned \$28,322 to the Crow Wing County Auditor. This amount is sufficient to cover both findings. The OSA considers this Finding resolved.

**Finding 2. TIF District 5 – Failure to Decertify the District in a Timely Manner – RESOLVED**

In the Initial Notice, the OSA found that the City of Ironton received \$20,263 of tax increment from TIF District 5 in violation of the TIF Act.



**Office of the State Auditor**

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Again, the OSA confirmed with the county that \$28,322 was returned to the Crow Wing County Auditor. This amount is sufficient to cover both findings. The OSA considers this Finding resolved.

**CONCLUSION**

The OSA considers the Findings resolved and appreciates the City's cooperation.

If you have any questions, please contact me at (651) 296-7979 or Jason.Nord@osa.state.mn.us.

Sincerely,

*/s/ Jason Nord*

Jason Nord  
Assistant State Auditor  
TIF Division Director

cc: Amanda Meyer, City Clerk/Treasurer