Inter-Departmental Communication

Date: October 14, 2005

To: Jim Rowland, Chair, Budget and Audit Committee

From: Mark Funkhouser, City Auditor

Subject: Effects of incentives on city's financial condition and developing financial policies

I want to let you know that the City Manager apparently has not analyzed the effects of incentives on the financial condition of the city, as the City Council directed nearly two years ago. I am providing you with a copy of the TIF policy that former City Councilmember Evert Asjes introduced several years ago.

As you move forward with efforts to develop financial policies, I think you and the members of the City Council need information about the effects of the use of incentives on the city's financial condition.

The City Council directed the City Manager to provide an annual report of financial information about TIF and other economic development incentives. (Committee substitute for resolution 011726, approved by the City Council on February 5, 2004). The City Council specifically directed:

> That the City Manager is directed to issue an annual report of financial information about TIF and other economic development incentives to the City Plan Commission and the City Council.
>
> That the report will examine the use of incentives in the broader context of their impact on the City's overall fiscal condition and capacity. The report will present aggregate data on revenues, expenditures, debt levels, property tax base, fiscal and non-fiscal benefits and/or any other fiscal data that may assist the City Council in priority setting deliberations.
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> That prior to development of the annual report the City Manager will inform the City Council Budget and Audit Committee of the basic assumptions, or range of assumptions, to be used in the report.

I also recommended that the City Manager prepare the report as directed by the City Council. I made my recommendation in March 2005.

As far as I can tell, the City Manager has not analyzed the effects of development incentives of the city's financial capacity.

I have also recommended developing a public policy on the use of TIF (Resolution 010924). Former City Councilmember Evert Asjes introduced a policy in June 2001. The proposal was held off the agenda until it was released in July 2003. I have attached a copy of the proposed policy

cc: Members of the Budget and Audit Committee
Wayne A. Cauthen, City Manager

RESOLUTION NO. 010924

Establishing a policy for the use of tax increment financing.

WHEREAS, pursuant to Sections 99.800 to 99.865, RSMo, the Real Property Tax Increment Allocation Redevelopment Act, the Council has approved approximately 40 tax increment financing plans; and

WHEREAS, the City uses tax increment financing to finance, among other things, public infrastructure related to real estate development and redevelopment; and

WHEREAS, when the City approves the use of tax increment financing it is making a long-term commitment to reimburse developers for certain costs related to the approved projects; and

WHEREAS, this policy is intended to ensure that tax increment financing is used to achieve clear and substantial public benefits while protecting the financial condition of the City; and

WHEREAS, because the City uses tax increment financing to finance the construction of needed public infrastructure, such as streets, bridges, storm sewer facilities and sewers, public infrastructure financed through tax increment financing must be consistent with needs identified through the Citys capital planning process; and

WHEREAS, developers benefit through the use of tax increment financing by reduced costs of construction of public infrastructure and increased property values because of the construction of public infrastructure; NOW, THEREFORE,

BE IT RESOLVED BY THE COUNCIL OF KANSAS CITY:

Section 1. That the following factors will constitute the Citys policy for the use of tax increment financing:

> Maximum assessed valuation for use of TIF. The total assessed valuation of parcels for which tax increment financing has been approved will not exceed a percentage of the total assessed valuation of the City, which percentage will be determined by the Council.
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> Use of TIF limited to public infrastructure. Tax increment financing may be used to reimburse costs directly related to the construction of public infrastructure, such as streets, sidewalks, bridges, sewers, and storm water drainage facilities.
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> TIF Commission funded through the general fund. Tax increment financing revenues generated by new tax increment financing plans will not be used to pay the costs of operating the Tax Increment Financing Commission or administering the tax increment financing program. Tax Increment Financing Commission costs, except those attributable to existing plans, will be annually appropriated through the Citys budget process.

Use of PILOTS. The City will devote 100 percent of the increment in property taxes to payments in lieu of taxes.

Prohibition on use of EATS. The City will not approve tax increment financing plans which call for allocation of incremental economic activity taxes for payment of redevelopment costs for tax increment financing plans.

Appropriation for shortfall in PILOTS. If tax increment financing is used to support debt and there is a shortfall in payments in lieu of taxes below that estimated by the Tax Increment Financing Commission and developer, the City will appropriate general fund revenues to make up for the shortfall.

Annual budgets/reports required. For each tax increment financing plan the developer will be required to provide annual budgets, conforming to the Citys fiscal year, showing anticipated expenditures and sources of revenue, and will include comparisons of actual and budgeted expenditures for all prior years.

Required commencement of construction. All development agreements will require construction of public infrastructure in an approved tax increment financing project to begin within three years of City Council approval of the plan or project, unless otherwise extended for up to an additional three years.

Extension of project completion dates. A project completion date may be extended for up to an additional three years when the developer establishes the existence of unforeseen and unanticipated conditions that reasonably prevented the commencement or completion of actual construction during the initial approved period.

Limitation on reimbursement. All development agreements will require that if actual construction of public infrastructure has not commenced by the completion date, including the completion date as extended, the development agreements will expire and payments in lieu of taxes will not be available to reimburse costs related to public infrastructure. No completion date will extend beyond six years from the initial approval of the project.

Individual projects. The City may impose additional requirements on a project-by-project basis to insure responsible use of the tax increment financing.