

Framework for the Future

Options for the Focus, Funding and Governance of
NRP Program and Action Plan Activities after 2009

Supplemental Report
Potential Funding Options
City Council Committee of the Whole
March 20, 2008

Report of the **NRP Work Group:**

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On November 2, 2007, the City Council created an NRP Work Group to “facilitate decision-making relative to Tracks 2 and 3 of the work plan for Community Engagement System Improvements and Related Neighborhood Revitalization Program (NRP) Decisions.” On December 20, 2007, the NRP Work Group presented to the City Council Committee of the Whole a draft “Framework for the Future” which outlined a structure for the continuation of the NRP beyond 2009 and its connection to the broader community participation work of the City.

Upon receipt of the draft report, the Committee of the Whole directed the NRP Work Group to return by the end of the first quarter of 2008 with a deeper exploration of potential funding sources for administrative support of neighborhood groups and the continuation of the NRP.

The draft “Framework for the Future” identified the need for regular, committed funding for the administrative support of neighborhood groups, as well as a dedicated source of programmatic and capital funding which would be provided through a Neighborhood Investment Fund.

The NRP Work Group met six times to discuss the potential funding options outlined in the draft “Framework for the Future” report. Those options included:

1. Allocate a larger portion of the City’s annual CDBG revenues to neighborhood funding;
2. Reallocate the City’s current community engagement costs;
3. Use interest earnings from the Legacy Fund;
4. Extend the pre-1979 tax increment financing (TIF) Districts;
5. Request that the State remove the LGA reduction resulting from the decertification of pre-1979 TIF districts;
6. Provide Target Center debt relief;
7. Extend the current Real Estate Transaction Fees and dedicate a portion of those fees to neighborhood funding;
8. Increase the current Mortgage and Deed Registration Fees and dedicate a portion of those fees to neighborhood funding;
9. Establish a countywide tax for neighborhood and community revitalization;
10. Secure grants and long-term funding commitments and relationships with major local or national companies and foundations; and
11. Seek participation from other units of government (local, county, state and federal).

The NRP Work Group also considered a proposal to establish a Neighborhood Trust Fund that would raise funds for the NRP. This proposal called for the creation of an opt-out (semi-voluntary) special assessment against residential and commercial property.

In its initial work to develop the draft framework, the NRP Work Group identified several shared principles related to funding. These principles are:

1. The method and sources of funding must be consistent with the City’s adopted budget principles.

2. Every effort should be made to identify and commit funding source(s) that are stable, predictable and available for a significant period of time.
3. Every effort will be made to develop a legislative agenda that addresses neighborhood needs, stabilizes future funding for neighborhood initiatives, and can be supported by the City, NRP and the neighborhoods.

The NRP Work Group reviewed each option with these interests in mind and with the assistance of Finance and Intergovernmental Relations staff.

In the course of its discussions, the NRP Work Group achieved unanimous agreement on the extension of the pre-1979 TIF districts as the preferred source of funding for capitalization of the Neighborhood Investment Fund.

The NRP Work Group reached this consensus with the understanding that these funds also would be used for Target Center debt relief, an activity in the Common Project also stressed by reduced tax increment revenue. The NRP Work Group also understood that if sufficient funds were generated, this source could also serve as, or supplement, the funding for administrative support for neighborhood groups, as currently occurs in the NRP.

Pre-1979 Tax Increment Districts

The pre-1979 TIF districts are 15 of the 42 TIF districts that comprise the City's Common Project. They currently generate 60 percent of the Common Project's tax increment revenue (51 percent of the City's total tax increment) and were expected from the creation of the NRP to be a major funding source for the program. This expectation was unmet primarily as a consequence of the 2001 changes in property tax law which reduced the revenue derived from TIF districts across the state. The NRP, which was designed to be dependent on Common Project revenues, is now expected to fall short of the originally anticipated level of funding by approximately \$107 million, of which a minimum of \$85 million is directly attributable to 2001 legislative action. The Target Center finance plan was similarly impacted. With no change in market value, the tax increment collections for the Target Center tax increment district dropped from \$2.2 million in 2001 to \$1.4 million in 2002, requiring the redirection of other City revenues to meet the Target Center debt service obligations for which this increment was expected to be used in 2008 and thereafter.

These shortfalls can be remedied by legislative action that would extend the life of the pre-1979 TIF districts and permit the tax increment revenue collected during the period of extension to be used for neighborhood revitalization activities and Target Center debt service.

Current projections indicate that starting in 2010 the pre-1979 TIF districts could, if extended, generate annual revenue of \$40 million to \$50 million. This would be sufficient over a five to ten year period to restore the originally intended level of support for neighborhood-based activities, relieve the Target Center obligations and possibly provide some level of general development funding.

With this funding source - as with most other options - there is a trade-off of priorities. Extension of the pre-1979 TIF districts will delay the return of the captured tax capacity to the various taxing jurisdictions. For the City, this delays approximately 50 percent of the tax capacity generating the \$40 to \$50 million tax increment. This negative effect is mitigated by the deferral of an approximate \$10 million additional annual reduction in Local Government Aid (LGA), which under the current LGA formula would occur if the districts are decertified. (See option 4 below for further discussion of LGA.)

Other Options

The following options also were considered by the NRP Work Group. The first three options were included in the draft Framework as possible funding sources for administrative support for neighborhood groups. These three options also were considered as possible funding sources for the Neighborhood Investment Fund.

None of these options were considered to have the capacity, the sustainability or the feasibility to be considered for capitalization of the Neighborhood Investment Fund. The final two options, however, have potential for supplementing the Fund or its administrative support, and should be pursued.

1. **Community Development Block Grant (CDBG) Allocation**—Allocate an increased portion of the City's annual CDBG entitlement to administrative support for neighborhood groups.

The City will receive approximately \$13.3 million of CDBG funds in the 2008-09 program year (CDBG Year 34). Of this amount, \$233,000 is allocated for CPED's citizen participation program. The CDBG funds received by the City have declined 25 percent from 1997 to present.

The CDBG program has been fully subscribed with 72 percent used for the housing, economic development and planning activities administered by CPED (in CDBG Year 34). Use of these funds for administrative purposes would be limited to Target-area neighborhoods; capital uses are limited to programming consistent with federal CDBG guidelines. Total administrative programming may not exceed 20 percent of the total CDBG allocation. In 2008, that limit would be \$2.68 million, which is fully allocated to a number of functions including Planning, Health and Family Support, Civil Rights, Citizen Participation and CDBG Program Administration.

2. **Reallocation of the City's Current Community Engagement Costs**—Reallocate the savings that would accrue to City departments by centralizing community engagement functions.

The City currently spends approximately \$2.5 million on community engagement related activities (not including NRP). These costs include direct community engagement assistance provided to City departments; direct community engagement assistance provided to neighborhood groups; direct financial

assistance to neighborhood groups, business associations and public housing; and other City community-building activities (such as CCP/SAFE).

The costs associated with this work are based on existing programs and work from a number of departments and funding sources that may be integrated and shared across staff and, therefore, may be difficult to identify and move.

3. **Interest Earnings from the Legacy Fund**—Preserve the post-2009 corpus of the Legacy Fund but dedicate its annual investment earnings to administrative support for neighborhood groups or to the Neighborhood Investment Fund.

The interest earnings on the Legacy Fund would vary from \$699,000 to \$1.8 million per year (based on a return of 2.3 percent to 6.0 percent and a corpus of \$30.4 million). The return depends on both the principal balance and interest rates.

Under current City policy this revenue is expected to be used for City general development and is the only unrestricted continuing revenue source for this purpose.

4. **Remove the Local Government Aid (LGA) Reduction Resulting from the Decertification of the Pre-1979 TIF Districts**—Starting in 2009 the decertification of the pre-1979 TIF districts reduces by as much as \$10 million the LGA received from the State (under the current LGA formula). If the State were to hold the City harmless, the City could direct to the Neighborhood Investment Fund the amount of LGA that would have been lost.

The City's Five-Year Plan for 2011 and thereafter already assumes a \$6.1 million LGA reduction attributable to decertification. Assuming no adverse revenue or expense issues, this amount would be available for the Neighborhood Incentive Fund. However, holding Minneapolis harmless would have consequences for the size of the total State level of LGA funding and therefore the amounts received by other jurisdictions. Decertification aside, LGA is expected to continue to decline at a rate of \$1 million annually, resulting in either reduced City services or an increased levy. The trend under current law and the continuing legislative consideration of equitable formulas make LGA a diminishing and uncertain funding source.

5. **Target Center Debt Relief**—If the State were to provide debt relief for the Target Center, the City could dedicate some portion of the savings (the funds no longer needed to pay down the debt on the Target Center) to capitalize the Neighborhood Investment Fund.

Debt service and capital needs of the Target Center are paid from the following sources in the approximate amounts indicated:

- Entertainment Tax (\$1 million per year);
- Parking revenues (ranging from \$3.125 million in 2008 to \$5.6 million in 2024);
- Arena TIF District tax increment funds (\$975,000 in 2008);

- Common Project tax increment revenues (\$1.9 million in 2008, decreasing to \$1.5 million in 2013 to 2024).

The debt service requirement in 2008 is \$6.4 million on an outstanding balance of \$64.5 million and the City's contractually-obligated, capital requirement is \$600,000. If debt service was eliminated, Entertainment and Parking revenues could be redirected to neighborhood or City development. Tax increment from the Arena TIF District would still be needed to pay committed capital and other related costs. The finance plan for the Target Center is structured so that any shortfalls in revenue from the entertainment tax or tax increment are covered by contributions from the Parking Fund.

Debt service relief would require legislative action. Legislative action also would be required to use the tax increment to fund NRP post-2009. If all available funds were reallocated to NRP, relief from Target Center debt service would not be realized to improve the Parking Fund's financial condition or in the General Fund (where the entertainment tax would otherwise revert).

6. **Real Estate Transaction Fees**—This tax is a percentage added to the Mortgage Registry and Deed Taxes (see below) in some counties. It is used to fund the Environmental Response Fund, which provides grantees the funds to clean-up and improve properties within the county. This option would increase the percentage collected and earmark that increase for neighborhood revitalization.

The Environmental Response Fund was established in 1997, but expired last year. The 2007 omnibus tax bill included an extension of this authority, but the bill was vetoed by the Governor. Prior to that, the annual collection ranged from \$2 million to \$4 million.

This option would increase the overall Mortgage Registry and Deed Taxes (the method through which the Environmental Response Tax is collected), which has, in past years, been opposed by real estate groups as a deterrent to growth in the real estate market. The revenue capacity of this mechanism is dependent on economic conditions.

7. **Mortgage Registry and Deed Taxes**—The Mortgage Registry and Deed Taxes are collected by the County at the time of registration of a mortgage and the transfer of a deed. This option would increase both of these taxes and dedicate those increases to neighborhood revitalization.

Over an eleven-year period (1997-2007) the annual average collection of these taxes has ranged from \$23.8 million to \$114.3 million (combined). Ninety-seven percent of the revenue goes into the State's general fund; the remaining 3 percent is retained by the County for administration.

This is a volatile source of funding. Further, given the higher rates recently implemented for these taxes and the current condition of the housing market, the

State may not want to increase the tax further. There are also competing interests for this revenue from various housing organizations within the state.

8. **Neighborhood Trust Fund**—This option would create a new opt-out (semi-voluntary) special assessment against residential and commercial property through the utility billing or property tax system.

Depending on the assumptions made (amount of the fee, participation rate, etc.), it has been estimated that such an assessment could generate between \$1 million and \$8 million annually. However, the ability for taxpayers to “opt-out” is unique and untried which makes any preliminary estimate difficult. It is unclear if the City has the authority to implement such an assessment or if State authorization would be required.

9. **Countywide Tax for Neighborhood and Community Revitalization**—A new tax would be levied countywide to provide funds to both the City and the County for neighborhood and community revitalization. The City's portion of that tax could be used to provide funding for the Neighborhood Investment Fund.

The creation of a new countywide tax would require the approval of the Hennepin County Board of Commissioners. The NRP Work Group did not believe that the Commissioners would support this option.

10. **Grants/Long-term Funding Commitments from Local or National Companies and Foundations**—The City would pursue grants and other long-term funding commitments from corporations and foundations to support the Neighborhood Investment Fund.

This is an option that the City should aggressively pursue to supplement both the support for neighborhood groups' administrative needs and the Neighborhood Investment Fund. Annual funding capacity, however, would be unpredictable.

11. **Participation from Other Units of Government (local, County, State and Federal)**—Other units of government could choose to participate in neighborhood revitalization efforts by dedicating funds to support the Neighborhood Investment Fund.

This, too, is an option that the City should pursue to supplement both the support for neighborhood groups' administrative needs and the Neighborhood Investment Fund. However, there is no reason to assume that this would provide a consistent and adequate funding stream.