



Report of the Vermont State Auditor

June 4, 2012

TAX INCREMENT FINANCING DISTRICT

City of Burlington Did Not
Always Administer Its District
According to Statutory
Requirements and Did Not Remit
All Monies Owed to the State
Education Fund

Thomas M. Salmon, CPA, CFE
Vermont State Auditor
Rpt. No. 12-03

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THOMAS M. SALMON, CPA, CFE
STATE AUDITOR



STATE OF VERMONT
OFFICE OF THE STATE AUDITOR

June 4, 2012

The Honorable Shap Smith
Speaker of the House of Representatives

The Honorable John Campbell
President Pro Tempore of the Senate

The Honorable Peter D. Shumlin
Governor

The Honorable Miro Weinberger
Mayor, City of Burlington

Mr. Paul Sisson
Interim Chief Administrative Officer,
City of Burlington

Dear Colleagues,

Act 45 of 2011 requires that the State Auditor's Office audit all active tax increment financing (TIF) districts every four years. Currently, the City of Burlington, Milton, Newport, and Winooski have established TIF districts and financed improvements in their districts.

This report assesses whether Burlington established and administered the waterfront TIF district according to statutory requirements and the extent to which the city has established performance measures and monitors actual results that demonstrate the TIF district is meeting intended goals.

Burlington complied with state statutes in the formation of its districts, but the city did not always administer its TIF district according to statutory requirements. Namely, Burlington utilized incremental property tax revenue for ineligible purposes and the city's determination of the amount of incremental property tax revenue to retain was not consistent with statutory requirements. As a result, the city retained \$1 million of statewide education increment that should have been remitted to the state. In addition to recommending that the city work with the state to resolve the shortfall in payments to the state, we also make recommendations designed to improve the city's administration of the TIF district. For example, we recommend that Burlington designate a city official to be responsible for reviewing statutory reporting requirements and documenting policies and procedures to ensure timely and accurate reporting.

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I would like to thank the management and staff of the City of Burlington for their cooperation and professionalism during the course of the audit. If you would like to discuss any issues raised by this audit, I can be reached at (802) 828-2281 or at auditor@state.vt.us.

Sincerely,

A handwritten signature in black ink that reads "Thomas M. Salmon CPA, CFE". The signature is written in a cursive style.

Thomas M. Salmon, CPA, CFE
Vermont State Auditor

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Abbreviations

ACA	Assistant City Attorney
ACCD	Agency of Commerce and Community Development
AG	Office of the Attorney General
BTC	The Burlington Town Center LLC
COPS	Certificates of Participation
DKB	DK Burlington Town Center Limited Partnership
DOT	Vermont Department of Taxes
FY	Fiscal Year
HUD	United States Department of Housing and Urban Development
JFC	Joint Fiscal Committee
JFO	Joint Fiscal Office
OTV	Original Taxable Value
SAO	State Auditor's Office
TIF	Tax Increment Financing
TPL	Trust for Public Lands
VEPC	Vermont Economic Progress Council
VSA	Vermont Statutes Annotated

Introduction

Since 1985, tax increment financing (TIF) districts have been available as a tool for Vermont municipalities to finance public infrastructure improvements in support of economic development. The TIF district approval process and administrative requirements largely are delineated in Vermont state statute. Typically, when a TIF district is established, certain real estate parcels within a municipality are designated as comprising the TIF district. Debt and other resources are utilized to finance public infrastructure improvements which support development in the district. Future incremental property tax revenue,¹ which is comprised of 1) incremental municipal property tax revenue (hereafter known as municipal increment) and 2) incremental statewide education property tax revenue (hereafter known as statewide education increment), within this designated district, is utilized over a set time period to pay for the debt incurred to finance the improvements.

TIF districts have been used in Vermont to finance public infrastructure improvements such as extending access to, or increasing capacity of waste water treatment plants and modifying or adding roadways. The city of Burlington established its TIF district on January 22, 1996 to redevelop the Lake Street district and nearby waterfront area. On June 23, 1997, the city expanded its TIF district with a sliver of property extending from the lakefront to Church Street to facilitate increasing the housing supply and parking garage additions to help stimulate a market for commercial retail stores and business offices.

TIFs not only affect the applicable municipality, they also have statewide tax implications. At the time municipalities were first granted authority to establish TIF districts, each municipality determined the amount of property taxes necessary to fund the local public school system and municipal operations. The establishment of a TIF district in a municipality potentially impacted the amount of funding available for general municipal operations and that municipality's school system. The method of funding public education costs for schools in Vermont changed dramatically with the passage of Act 60 in 1997 and the establishment of a statewide education

¹ Incremental property tax revenue is calculated based on the current property values of the TIF district less the TIF district property values at the time the TIF district was established, multiplied by the municipal and education property tax rates.

property tax set by the state to fund public education. Because of the change to a statewide education property tax funding mechanism, municipalities with TIF districts retain monies that otherwise would have been remitted² to the state for funding public education throughout the state.

Act 45 of 2011³ required the state auditor of accounts to audit all active TIF districts every four years. Because requirements for establishment and administration of TIF districts are largely set out in state statute, we elected to focus our audit towards determining compliance with the statutes applicable to Burlington's TIF district. Our audit objectives were to:

- assess whether Burlington adhered to requirements in state statute governing establishment of the TIF district;
- ascertain whether since inception to FY2010, Burlington has administered the TIF district according to statutory requirements, including a) utilizing the incremental property tax revenues to pay for eligible TIF district debt b) retaining the appropriate statewide education increment, and c) timely and accurately reporting TIF district property values and incremental tax revenue to city officials, the legislature and other state officials, as appropriate; and
- assess the extent to which Burlington has established performance measures and monitors actual results that demonstrate achievement of the state and municipality's economic and fiscal goals.

The audit work for our first objective largely consisted of comparing Burlington's documentary evidence of activities and actions associated with establishing its TIF district to the statutory requirements governing establishment of a TIF district. Our methodology for the second objective included a) obtaining TIF district debt payment schedules and analyzing other financial records to verify that incremental property tax revenue was used solely for debt payment or prefunding, b) obtaining legal opinions from the Office of the Attorney General (AG) regarding the calculation and

² Annually, the state establishes statewide education property tax rates. Municipalities collect statewide education property taxes on behalf of the state and remit the taxes collected to their local school systems, on behalf of the state, or to the state directly, depending on the amount collected relative to the amount required to fund the local school system. Since these are all state revenues, for simplification purposes, in our report, we refer solely to remitting payments to the state.

³ Previously, Act 190 of 2008 required the state auditor of accounts to audit all active TIF districts every three years.

retention of incremental property tax revenue, recalculating the incremental property tax revenue from inception of the TIF district through FY2010 and verifying that Burlington retained only those amounts allowed per statute, and c) comparing reports of TIF district property values and incremental property tax revenue to source documentation. To accomplish our third objective, we interviewed Burlington officials and reviewed Burlington's processes and procedures related to monitoring results of the TIF district. Additional detail on our scope and methodology can be found in appendix I.

Highlights: Report of the Vermont State Auditor

Tax Increment Financing District: City of Burlington Did Not Always Administer Its TIF District According to Statutory Requirements and Did Not Remit All Monies Owed to the State Education Fund

(June 4, 2012, Rpt. No. 12-03)

Why We Did This Audit

Pursuant to statutory requirements that we audit the TIF districts, our objectives were to 1) assess whether Burlington adhered to requirements in state statute governing establishment of the TIF district, 2) ascertain whether, since inception through FY2010, Burlington has administered the TIF district according to statutory requirements, including a) utilizing the incremental property tax revenues to pay for eligible TIF district debt, b) retaining the appropriate statewide education increment and c) timely and accurately reporting TIF district property values and incremental tax revenues to city officials, the legislature and other state officials, as appropriate, and 3) assess the extent to which Burlington has established performance measures and monitors actual results that demonstrate achievement of the state and municipality's economic and fiscal goals.

What We Recommend

We made multiple recommendations, including that Burlington should work cooperatively with the state to resolve the city's \$1 million shortfall in payments to the state education fund.

Findings

Burlington adhered to requirements in state statute associated with establishing and expanding its TIF district in 1996 and 1997, respectively. For instance, the city held publicly warned meetings to discuss formation and financing of the TIF district and obtained voter approval for anticipated financing. The city council and city officials worked together to identify and adhere to requirements associated with establishing the TIF district.

Certain aspects of Burlington's TIF district administration were not in accordance with statutory requirements. For example, of the \$8.3 million in incremental property tax revenue used by Burlington, approximately \$1.2 million was used for ineligible purposes – to pay refinanced debt associated with land (the Urban Reserve) that was acquired four years prior to the creation of the TIF district. Largely because of this error, the city's determination of the amount of the statewide education increment to retain was not consistent with statutory requirements. As a result, the city retained \$1 million that should have been remitted to the state. Additionally, Burlington has been required to issue reports related to the TIF district to both city and state organizations (executive and legislative branches). The city has not met all reporting requirements, but the information that was reported was consistent with its financial records. City officials provided various rationales for their approach to administering the TIF district, including a legal opinion justifying aspects of their approach. We considered the city's legal justifications but disagree with its conclusions based on discussions with the AG's office and reviews of records and other evidence. For example, the city argues that refinancing the Urban Reserve debt is a legitimate TIF district transaction. However, the AG's office advised that TIF districts are authorized for the purpose of funding expenditures such as acquisition of property that will stimulate development or redevelopment within the TIF district. If an investment has already occurred as it has in this instance (with the purchase of the land) the creation of a TIF district at a subsequent date does not serve the purpose of motivating the investment.

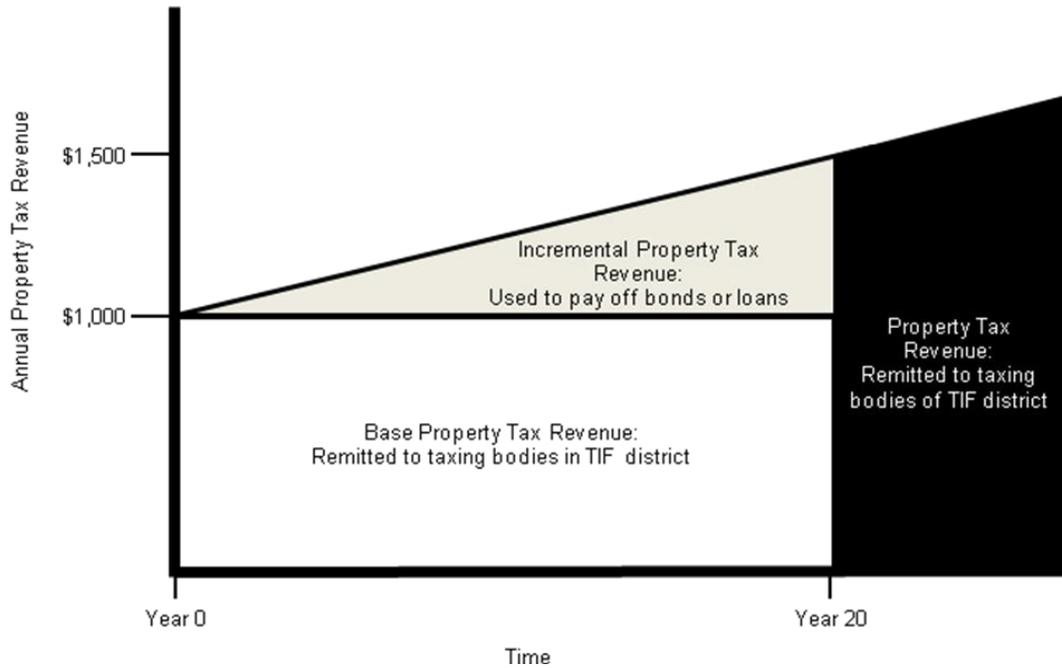
The city's establishment and monitoring of performance measures to indicate the extent to which its TIF district was meeting state and municipal economic and fiscal goals was limited. Specifically, Burlington did not 1) establish measures for all objectives (broaden the tax base, encourage development and improve employment opportunities), 2) consistently set targets and 3) consistently track actual results. According to city officials, they consider growth in property values to be the primary TIF district performance measure and believe this measure is sufficient to track the performance of the TIF district. However, without targets and actual results for measures relevant to all objectives, the city's ability to determine whether the TIF district is operating as intended is limited.

Background

Establishment of a TIF district allows a municipality to designate an area for improvement and earmark expected future growth in property tax revenues (i.e. incremental property tax revenue) in the designated area to pay for debt incurred to finance the costs of improvements. In theory, the improvements lead to increased property values and the resulting increased property tax revenues fund the cost of development. For example, assume that existing property in a TIF district generates \$1,000 a year in tax revenues. The municipality obtains approval for the use of incremental property tax revenue for a new project in the district and issues 20-year bonds to finance the project's costs. Over time, the district's property values grow and annual property tax revenues increase to \$1,500. The taxing authorities, including the municipality and the state, continue to receive their respective portions of \$1,000 (i.e. the base property tax revenue), and the \$500 difference (i.e. the incremental property tax revenue) is used to pay off the bonds over 20 years.⁴ Once the bonds are paid off, the taxing authorities (municipality and state) receive all of the property tax revenues (\$1,500 per year). Figure 1 illustrates how this example works.

⁴ In the event that a TIF district's incremental property tax revenue exceeds the amount needed to make bond payments in a given year, this "excess" incremental revenue is distributed to the municipal and state taxing authorities using a statutory formula as established in 24 VSA §1900. Alternatively, municipalities may retain the excess for the purpose of prefunding future TIF district debt. (32 VSA §5401(10)(E))

Figure 1: Simplified Illustration of How a TIF District Can Generate Incremental Revenue



Note: *This simplified graphic assumes a stable tax rate.*

Statutory Requirements Governing Burlington’s TIF Districts

Municipalities are responsible for establishing and administering TIF districts according to statutory parameters, including overseeing the financing for construction of public infrastructure improvements, calculating incremental property tax revenue, determining the amount of incremental property tax revenue the TIF district may retain, and deciding how it may be utilized.

Acts 87 (1985) and 204 (1988) established the initial framework in Title 24 Chapter 53 Subchapter 5 for the formation and operation of TIF districts in Vermont. The following is a summary of the original criteria in Acts 87 and 204 for establishing and administering TIF districts.

Establish, approve and record

- The purpose of TIF districts is to provide revenues for improvements⁵ located wholly or partly within the district that will encourage

⁵ The statute defines improvements as including installations, construction, or reconstruction of streets, utilities, parks, playgrounds, land acquisition, parking facilities and other public improvements necessary for carrying out the objectives of the TIF district.

development, provide for employment opportunities, improve and broaden the tax base or enhance the general economic viability of the municipality, region or state. [24 VSA §1893]

- The municipality's legislative body⁶ determines that the TIF district will serve the public purpose and creates the TIF district. [24 VSA §1892(a)]
- At least one public meeting, duly warned, must be held on the proposed TIF district plan with a description of TIF district boundaries and properties. [24 VSA§1892(a)]
- Upon adoption by the municipality's legislative body, the TIF district plan must be recorded with the municipal clerk and lister or assessor. [24 VSA§1892(b)]

Financial plan

- At least one public meeting, duly warned, must be held on a financial plan for proposed improvements. The elements of the financial plan shall include a statement of costs and sources of revenue, estimates of assessed values within the district, identification of the portion of assessed value to be applied to proposed improvements, tax increments for each year of the financial plan, amount of bonded indebtedness to be incurred, other sources of anticipated revenues and the duration of the financial plan. [24 VSA§1898(e)]

Allowable debt and period that debt may be incurred

- Incremental property tax revenue may be pledged and appropriated for payment of principal and interest on bonds issued for improvements contained wholly or partially within the district. [24 VSA §1897]
- Bonds may take the form of general obligation bonds or revenue bonds and must be approved by a majority of registered voters at a duly warned special or annual meeting. [24 VSA §1898(b) and 24 VSA §1897]

⁶ Legislative body means the mayor and alderboard, the city council, the selectboard and the president and trustees of an incorporated village.

-
- If revenue bonds are issued, they are payable solely from income proceeds, revenues, and tax increments resulting from the improvements in the TIF district. [24 VSA §1898(b)]
 - The municipality may incur debt relative to the TIF district for a period of 10 years following creation of the TIF district. The 10-year borrowing period commences April 1 of the year the TIF district is created by the municipality's legislative body. [24 VSA §1894]

Establish original taxable value (OTV)

- OTV is the sum of the aggregate taxable valuations of land and improvements in the TIF district on the date the district was approved as then most recently determined. [24 VSA §1895 and 24 VSA §1898(b)]
- On April 1 of the first year, the lister or assessor certifies the OTV of the TIF district parcels as then most recently determined. [24 VSA§1895]

Calculation and utilization of incremental property tax revenue

- Incremental property tax revenue equals current assessed value of properties located wholly or partially within the TIF district less OTV multiplied by the current tax rates of the municipality, the school district⁷ and any other taxing authority.⁸ [24 VSA §1896, 24 VSA §1897 and 24 VSA §1898(b)]
- The municipality's legislative body may pledge and appropriate incremental property tax revenue received from the TIF district for the payment of bond principal and interest. [24 VSA§1897]

⁷ The school district rate is determined by the state and is a statewide property tax.

⁸ TIF district taxable property shall be subject to the same total tax rate as other taxable property in the municipality, except as otherwise provided by law.

Period that incremental property tax revenue may be retained for payment of debt

- Incremental property tax revenue may be retained in each year subsequent to creation of the district for which the current assessed valuation exceeds the OTV until all capital indebtedness of the district has been fully paid. [24 VSA §1896 and 24 VSA §1898(b)]
- The TIF district continues until all indebtedness incurred by the municipality to fund the improvements in the TIF district has been paid. [24 VSA §1898(b) and 24 VSA §1894]
- To the extent incremental property tax revenue is pledged and appropriated for payment of debt incurred to finance development in the district, it must be segregated in a special account of the municipality. [24 VSA §1896]

Distribution of incremental tax revenue

- Incremental property tax revenue which in any tax year exceeds the principal and interest payments for the bonds issued for improvements in the district is required to be distributed to the municipality and school district in proportion that each budget bears to the combined total of both budgets unless otherwise negotiated. [24 VSA §1900]

Reporting

- Each year of the life of the TIF district, the lister or assessor for the municipality shall certify and report to the legislative body the amount that the OTV has increased or decreased and the proportion that any increase or decrease bears to the total assessed valuation of real property for that year. [24 VSA §1895]

Since the passage of Act 60 (Equal Education Opportunity) in 1997, the statutes related to TIF districts have undergone numerous amendments. Per 1 VSA §212, amendments generally take effect prospectively on July 1 following the date of their passage unless otherwise specifically provided. Accordingly, many of the changes to TIF statutes are applicable to Burlington's TIF district. See figure 2 for a timeline of select amendments to TIF legislation, the effective dates, and those changes impacting the Burlington TIF district from 1997 through 2010. Items in grey do not apply to Burlington's TIF district.

Figure 2: Timeline of Select Changes to TIF District Statutes and Applicability of Certain Amendments to Burlington (appendix II contains greater detail)

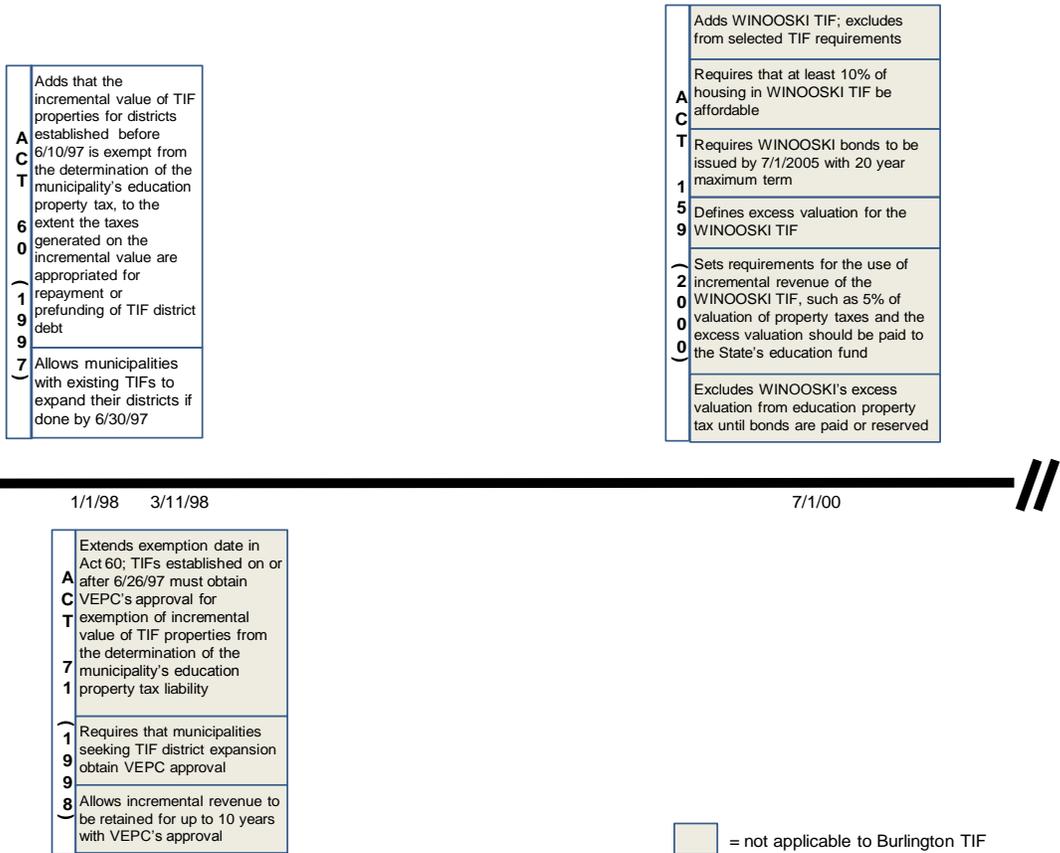


Figure 2: Timeline of Select Changes to TIF District Statutes and Applicability of Certain Amendments to Burlington (appendix II contains greater detail)—continued

<p>A C T 1 8 4 (2 0 0 6)</p> <p>Allows incremental revenue to be used to pay for related costs (as defined in act)</p> <p>Expands TIF goals and amends definition of TIF improvements</p> <p>Sets criteria for VEPC approval of TIF districts</p> <p>Allows 20-year debt borrowing period; must obtain VEPC approval if debt not incurred in first 5 years.</p> <p>Adds that OTV must be adjusted if >= 20% of properties in the municipality are reappraised</p> <p>Limits the retention of tax increment to 20 years commencing 4/1 of the year following VEPC approval</p>	<p>A C T 1 9 0 (2 0 0 8)</p> <p>Allows more financing instruments</p> <p>Amends definition of improvements to include those that serve TIF district</p> <p>Adds that TIF districts are now created as of 4/1 of the year so voted</p> <p>Changes period of retention of tax increment to 20 years from the date the debt was first incurred</p> <p>Allows that an equal proportion of excess municipal and state education tax increments may be used for prepayment or escrowed for financing; any remaining excess state education tax increment must be distributed to the education fund</p> <p>Requires municipalities to report to VEPC and DOT</p> <p>Requires SAO audit every 3 years</p>	<p>A C T 1 9 0 (2 0 0 8)</p> <p>Requires MILTON to proportionally apply state education property tax and municipal tax increments for repayment of debt incurred prior to 4/1/09 for Husky and Catamount TIFs; excludes these TIFs from proportionality rule</p>	<p>A C T 5 4 (2 0 0 9)</p> <p>Allows MILTON more debt financing options (retroactive to 7/1/08)</p> <p>Authorizes MILTON to select date to start retaining tax increment; OTV must be recertified if retention of education tax increment starts more than 5 years after TIF creation (retroactive to 7/1/08)</p>
<p>7/1/06</p>	<p>6/6/08</p>	<p>7/1/08</p>	<p>7/1/09</p>
<p>A C T 1 8 4 (2 0 0 6)</p> <p>Amends tax increment utilization so that no more than 75% of state education property tax increment and no less than 75% of municipal tax increment may be used to service debts and related costs</p> <p>Requires that distribution of excess municipal tax increment be distributed in proportion to the budget; limited usage of excess state education tax increment to prepayment and escrow for debt</p> <p>Requires VEPC and DOT report to legislature</p> <p>Allows extensions to the life of the MILTON TIFs</p>	<p>A C T 1 9 0 (2 0 0 8)</p> <p>Limits use of the tax increment to repaying the financing of improvements and related costs expenditures to the same proportion as the TIF benefits from these expenditures (proportionality rule)</p> <p>Sets WINOOSKI's FY 2008 common level of appraisal and directs that any overpayment of the education property tax be credited to fiscal year 2009 liability</p> <p>Requires that 2% of WINOOSKI's education property tax on the excess valuation of TIF properties be paid to the education fund</p> <p>Retroactively approves financing for BURLINGTON's TIF to 6/30/97</p>	<p>A C T 5 4 (2 0 0 9)</p> <p>Extends the BURLINGTON TIF's borrowing period by 5 years</p> <p>Requires BURLINGTON to submit proposal to legislature for calculating amount due to the education fund on new revenue growth in the TIF</p>	

Effect of Act 60 on Burlington's TIF District

Burlington established its TIF district on January 22, 1996. This was prior to the passage of Act 60 in 1997 which changed the state's education funding mechanism. With the passage of Act 60 and the state's migration to statewide funding for public education, the administration of TIF districts was complicated by the retention of incremental property tax revenue which includes statewide education increment and impacts statewide funding for public schools.

There are two components of incremental property tax revenue: statewide education increment and municipal increment. The distinction of state and municipal components in the incremental property tax revenue is significant because funding for public education in Vermont is mostly based on statewide education property taxes. The TIF program allows municipalities to retain the statewide education increment rather than remit the taxes to the state. The proportion of statewide education increment that municipalities may retain is contingent upon the extent to which the total incremental property tax revenue (statewide education increment and municipal increment) is pledged and appropriated for debt repayment or prefunding.

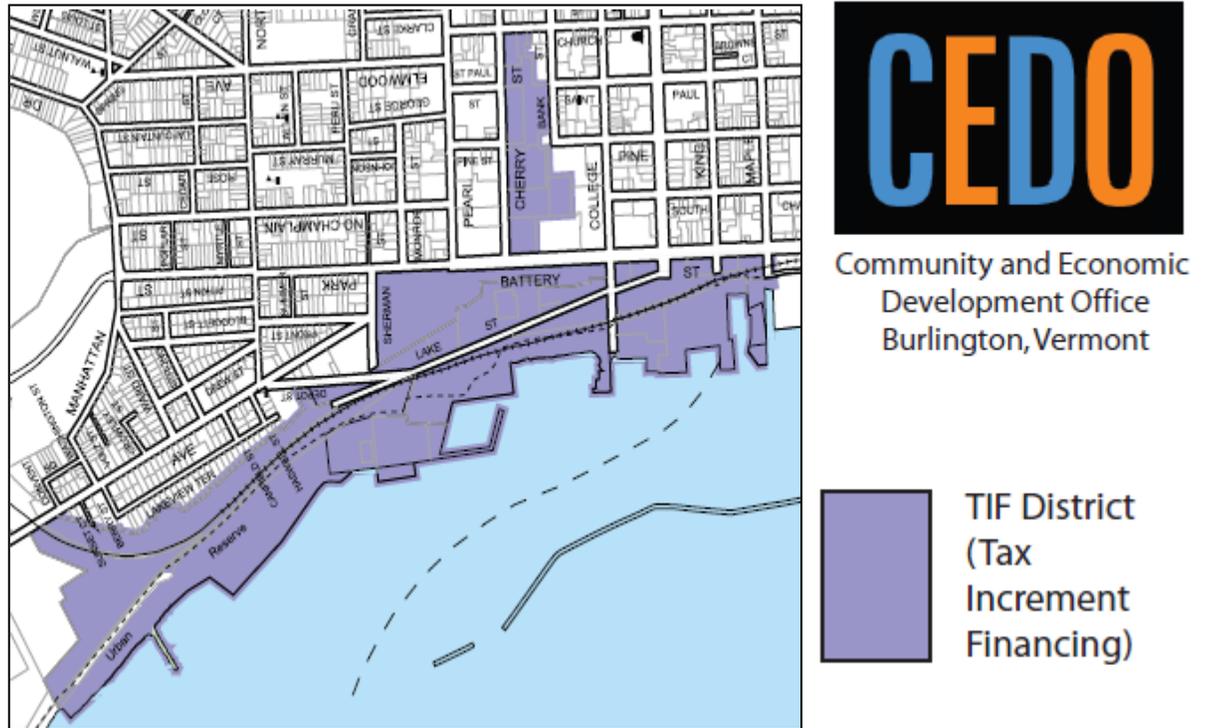
Burlington is one of two municipalities that may retain up to 100 percent of the statewide education increment.⁹

Burlington TIF District

On January 22, 1996, the City of Burlington created a TIF district known as the "Waterfront TIF District" along the central and northern end of the waterfront. On June 23, 1997, the city authorized an expansion of the district to include a sliver of property extending from the lakefront to Church Street. Figure 2 illustrates the TIF district.

⁹ Per Act 54 (2009 session), commencing January 1, 2010, Burlington's borrowing period for the waterfront TIF district was extended for five years. As a result, if new debt is incurred, the city will no longer be authorized to retain 100 percent of the statewide education increment. Beginning in the fiscal year in which there is incurrence of new TIF district debt, the city will need to calculate and make an annual payment on December 10 to the Education Fund each year until 2025. The payment will be 25 percent of the incremental value generated subsequent to April 1, 2010, excluding the incremental value of two TIF district properties.

Figure 3: Map of the Waterfront TIF District



Initially, the city intended the TIF district to be used to redevelop the Lake Street district and make the waterfront area more accessible and vibrant. But as the TIF progressed, the City invested in infrastructure upgrades and parking garage additions to stimulate the market for commercial retail stores and business offices.

According to city officials, infrastructure improvements to Lake Street, the Westlake Garage, and the Lakeside Parking Garage have encouraged business growth. Private “anchor projects” include Macy’s, the new Marriot Hotel, a new office and retail building on Lake Street, and 16 residential condos and 40 residential units of affordable housing also along Lake Street. The cost of the TIF district’s improvements was funded as follows:

- \$2.5 million in state grants from the Vermont Agency of Commerce and Community Development,

-
- \$1.6 million in United States Department of Housing and Urban Development (HUD) Section 108 loans, and
 - \$15.2 million in certificates of participation.¹⁰

¹⁰ A type of debt financing arrangement structured as a lease that pledges a specific revenue stream (such as incremental property tax revenue) for repayment.

Burlington Complied with State Statutes in Establishing Its TIF District

Burlington adhered to requirements in state statute associated with establishing and expanding its TIF district, including:

- holding publicly warned meetings to discuss formation and financing of the TIF districts,
- passing a city council resolution approving the TIF districts, and
- obtaining voter approval for anticipated financing.

Table 1 presents our assessment of Burlington’s compliance with the requirements for creating a TIF district and authorizing financing for improvements in the TIF district.

Table 1: Assessment of Burlington's Compliance with Required Steps for Creating a TIF District and Authorizing Financing

Statutory Requirements	Comments	Compliance
Hold publicly warned meetings on proposed TIF district plan, with a description of the TIF district boundaries and properties.	Meeting held on 1/22/96.	✓
Hold publicly warned meetings on a financial plan for proposed improvements.	Meeting held on 1/22/96.	✓
Adoption of TIF district plan by legislative body of municipality (e.g. city council).	City council approved district on 1/22/96.	✓
Record TIF district plan with municipal clerk and lister or assessor.	The plan was filed on 1/23/96.	✓
Obtain approval of majority of registered voters for general obligation or revenue bonds at a warned special or annual meeting.	Meeting held on 3/5/96 for financing of Waterfront Revitalization Project (i.e. TIF district). ^a Financing was approved by the voters.	✓

^a The voter resolution specified the authorization of HUD Section 108 financing or another equivalent financing source for Waterfront Revitalization Projects.

In addition, on June 23, 1997, in accordance with TIF district statutes, the city council voted to authorize an expansion of the TIF district as allowed by Act 60.

In establishing its TIF district, the city council worked closely with city officials to identify and adhere to the statutory requirements for establishing its TIF district. By carefully following the statutory criteria, Burlington appropriately established its TIF district as a financing tool for their impending projects.

Burlington Did Not Always Administer Its TIF District According to Statutory Requirements

Certain aspects of Burlington’s practices in administering its TIF district were not in accordance with statutory requirements. Specifically, the city used approximately \$1.2 million of the incremental property tax revenue generated by its TIF district to repay debt associated with a land acquisition that occurred prior to the creation of the TIF district and thus was ineligible to be paid with incremental property tax revenue. In addition, Burlington did not follow statutory criteria to determine how much statewide education increment to retain and underpaid the state \$1 million. The use of incremental property tax revenue for ineligible expenditures and underpaying the state its portion of the statewide education increment increases the likelihood that Burlington will need to retain statewide education increment for a longer period of time to repay its TIF district debt than it would have if it had complied with the uses specified in statute. Finally, the city met some, but not all reporting requirements, but the information reported was mostly consistent with the city’s financial records. Timely and accurate reporting is needed to monitor the status of the TIF district and to provide decision makers with information to make decisions about the TIF program.

Incremental property tax revenue occurs when municipal financed improvements in TIF districts facilitate development in the district, resulting in increased property values. The increase in property values (e.g. the net increase over the property value prior to improvements) multiplied by current property tax rates yields the incremental property tax revenue.

Burlington Inappropriately Utilized \$1.2 Million of Incremental Property Tax Revenue

State statutes put restrictions on how incremental property tax revenue can be used. Specifically, according to 24 VSA §1897 and 32 VSA §5401(10)(E), utilization of incremental property tax revenue is limited to repaying or

prefunding principal and interest on bonds issued within 10 years of the creation of the TIF district¹¹ to finance improvements¹² located wholly or partially within the TIF district.

Burlington is limited to using incremental property tax revenue to repay TIF district debt issued from April 1, 1996 to March 31, 2006 to finance improvements in the TIF district. As of June 30, 2010, Burlington has used about \$8.3 million in incremental property tax revenue to repay and prefund debt, \$8 million and \$277,000, respectively. However, the city has used \$1.2 million of incremental property tax revenue to repay certificates of participation (COPS)¹³ that were issued in 1999 to pay off (e.g. restructure or refinance) debt associated with the acquisition of 46 acres of waterfront property (the “Urban Reserve”) that occurred October 15, 1991¹⁴ – more than four years prior to the creation of the TIF district.

According to advice we obtained from the Office of the Attorney General, Burlington may not use incremental property tax revenue to pay the Urban Reserve debt. The AG concluded that the relevant debt to measure against the statutorily allowed borrowing period is the 1991 loan. It is the initial debt financing the land acquisition, not the subsequent debt, which must have originated during the statutorily allowed borrowing period. Likewise, the improvements financed with the initial debt must have occurred after creation of the TIF district. In this case, neither is true – the debt and improvement (i.e. land acquisition) originated in 1991, more than four years prior to the creation of the TIF district and the allowed borrowing period.

Further, the AG advised that TIF districts are authorized for the purpose of funding expenditures such as acquisition of property that will stimulate development or redevelopment with the TIF district. If an investment has already occurred as it has in this instance (with the purchase of the land), the creation of a TIF district at a subsequent date does not serve the purpose of motivating the investment.

¹¹ Per 24 VSA §1894, the 10-year borrowing period commences on April 1 of the year the district is approved by the municipality’s legislative body.

¹² Per 24 VSA 1891, improvements include land acquisition and construction of streets and utilities.

¹³ A type of debt financing arrangement structured as a lease that pledges a specific revenue stream (such as incremental property tax revenue) for repayment.

¹⁴ The city acquired the Urban Reserve in 1991. To finance the acquisition, the city obtained a loan from the Trust for Public Lands (TPL). In 1993, the city borrowed money from the Burlington City Employees’ Retirement System (“Retirement System”) to pay off the TPL loan. Subsequently, in 1999, the city issued \$1,390,000 certificates of participation (COPS) to pay off the Retirement System loan.

Burlington's assistant city attorney (ACA) provided our office with a response to the AG's opinion (see exhibit A in appendix V) in which he put forward multiple rationales to justify the refinancing of the Urban Reserve debt as a legitimate TIF district transaction. We consulted with the AG's office regarding Burlington's analysis and the AG's office determined that the analysis did not alter their conclusion that the Urban Reserve debt may not be paid with TIF district incremental property tax revenue.

Also, we disagreed with some of the facts presented by the ACA. For example:

- The ACA explained that the 1999 COPs were utilized to extinguish the Retirement System's legal interest in the Urban Reserve and that this extinguishment of interest constituted an improvement. The Retirement System's interest, as described by the ACA, was an option to purchase the Urban Reserve, but it was never exercised. In fact, the records provided by the city indicate that the city maintained ownership of the property since its acquisition in 1991. Further, we obtained a legal opinion from external counsel that concluded the Retirement System's purchase option had no effect on legal ownership of the property and the city has held title to the property since 1991. Therefore, its extinguishment does not constitute a change of circumstance related to the property, therefore an improvement did not occur.
- The ACA argues that Burlington has openly held out its refinancing of the Urban Reserve as a TIF debt for 13 years and that the state has known and not objected to its inclusion. However, based upon the debt schedules that Burlington provided to our office and the information that Burlington provided to the Vermont Department of Taxes (DOT) and Joint Fiscal Office (JFO) for its limited review of the TIF district in 2009, we concluded that prior to our audit, DOT had no basis to know that incremental property tax revenue was being used to repay debt associated with a property purchased before the establishment of the TIF district. For example, in the schedule of TIF district improvements provided to DOT for purposes of its limited review, Burlington described one project as the "Urban Reserve Acquisition," and the date and type of financing as "1999; certificates of participation." Based on this characterization, a reader would not be able to discern that the acquisition of the property occurred in 1991.

Inappropriate use of incremental property tax revenue affects how much of the statewide education increment may be retained (e.g. kept by the city rather than remitted to the state) which will be addressed in the next section.

Burlington Inappropriately Retained \$1 Million of Statewide Education Increment

State statutes restrict the amount and length of time statewide education increment may be retained by municipalities. The amount of statewide education increment a municipality may retain is a function of how much incremental property tax revenue is generated by a TIF district and the extent to which the incremental property tax revenue is pledged¹⁵ and appropriated¹⁶ for repayment or prefunding of TIF district debt. State statute establishes the methodology municipalities are to use to calculate incremental

Incremental property tax revenue is comprised of two components: municipal increment and statewide education increment. Municipalities with approved TIF districts are exempt from paying the state some or all of the statewide education increment generated by incremental property values in TIF districts.

property tax revenue generated by TIF districts and to determine the proportion of statewide education increment that may be retained. Burlington may retain statewide education increment for up to 20 years from the date debt was issued.¹⁷

Mistakes in Burlington's Approach to Revenue and Retention Calculations

Burlington did not follow the methodology delineated in state statute for 1) calculating incremental property tax revenue and 2) determining the proportion of statewide education increment to retain.

¹⁵ For purposes of municipal debt financing, a pledge is a promise or commitment related to the use of a specified source (e.g. incremental property tax revenue) for repayment of the debt obligation. Burlington's debt arrangements pledge incremental property tax revenue as the source of repayment along with the municipality's general obligation (e.g. full faith, credit and taxing power).

¹⁶ Per Vermont statute, appropriations are planned expenditures.

¹⁷ Sec.72, Act 190 (2008 session).

(1) Calculation of Incremental Property Tax Revenue

Incremental property tax revenue is required by statute to be calculated as incremental property value growth (total current April 1 assessed value of TIF district properties less OTV¹⁸) multiplied by the municipal and statewide education property tax rates (i.e. tax rates of all taxing authorities).¹⁹ However, Burlington did not include all tax rates in its incremental property tax calculation. The city told us that they excluded certain tax rates because the rates had specific uses delineated in the city's charter and ordinances (see exhibit C in appendix V). We sought the advice of the AG's office with regard to whether the city's position was valid. According to guidance provided by the AG's office, there may be some merit in the city's position because the legislative intent with respect to TIF revenue calculations is ambiguous as a result of what appears to be legislative intent to treat certain Burlington municipal tax assessments specified in its city charter for a restricted use versus the requirement in the TIF statutes to include all tax rates in the calculation of incremental property tax revenue. Therefore, given this ambiguity, although the statute does not explicitly address whether certain tax rates may be excluded from the calculation of incremental property tax revenue, it is reasonable to conclude that certain tax rates may be excluded if the use has been designated (e.g. restricted) for a special use and the designation is included in state law, such as a city charter approved by the state legislature.²⁰ However, those tax rates delineated in the city charter, but without description of a specified use, must be included in the calculation of incremental property tax revenue.²¹

SAO calculated incremental property tax revenue through June 30, 2010, according to statutory requirements and guidance provided by the AG's

¹⁸ OTV is the sum of the aggregate value of land and improvements in the TIF district as of the date the district is approved (24 VSA §1898(b)).

¹⁹ 24 VSA §1896, 24 VSA §1897 and 24 VSA §1898(b) establish the requirements for calculating incremental property tax revenue.

²⁰ One example is the library tax rate which is designated for a specific use of the funds. 24 VSA App. §3-102c states "the city council shall annually assess upon the property grand list of the city to assist in meeting the appropriation made for the use of purchasing books and other media for the library department, a tax which will, in the judgment of the city council, be sufficient to assist in meeting such appropriation.."

²¹ For example, the retirement tax rate is authorized in city charter, but the use is not restricted for a singular purpose. 24 VSA App. §284 states "the city council is hereby given authority and power to provide in the annual budget an appropriation to the fund, as may be necessary to meet the required demands thereunder."

office and found that Burlington's TIF district generated \$8,362,000 of incremental property tax revenue - \$58,000 more revenue than the city accounted for in its records. This is primarily because of differences between which municipal tax rates Burlington excluded in its incremental property tax revenue calculation and the municipal tax rates that we excluded from our calculation.

We found that Burlington's inclusion of certain municipal tax rates in its calculation of incremental property tax revenue was not consistent with the rationale the city provided to support the exclusion of certain municipal tax rates. Specifically, Burlington included tax rates in its calculation that, according to its rationale, should have been excluded. For example, Burlington excluded the library tax rate because the city charter limited the use of the proceeds for a specific purpose, but the city included the park tax rate even though city charter designated a specific use for these funds as well. See table 2 for a comparison of the rates that Burlington included and excluded from the calculation to the rates that SAO included and excluded from the calculation according to advice from the AG's office. The table also demonstrates that there are tax rates, the first three listed, which Burlington should have excluded from its incremental property tax revenue calculation according to its own rationale.

Table 2: Comparison of Burlington’s tax rates included and excluded to the tax rates included and excluded by SAO in the calculation of incremental property tax revenue.

Municipal tax rates	City charter prescribes specific use, may be excluded^a	Excluded from Burlington Calculation	Excluded from SAO Calculation
Police/Fire	X	No	Yes
Parks	X	No	Yes
Streets	X	No	Yes
Library	X	Yes	Yes
Debt service	X	Yes	Yes
Retirement		Yes	No
CCTA		Yes	No
County		Yes	No
Emergency		Yes	No
Open space		Yes	No
Housing		Yes	No
General city		No	No
Highway		No	No

^a Per advice of AG’s office, these are the municipal rates that have a required specific use of the funds raised delineated in the city’s charter that may be excluded from the calculation of incremental property tax revenue.

The differences in tax rates used by Burlington in the calculation of incremental property tax revenue versus those used by SAO largely offset. However, the ambiguity that exists with regard to how the legislature intended provisions of the TIF statutes to work with the provisions of the city’s charter that specifies certain uses of municipal tax rates, means that municipalities have a mechanism to utilize municipal increment for purposes other than TIF district debt repayment. This could be significant since the result will be an increased reliance on the education increment versus the municipal increment to repay TIF district debt. Moreover, this means that the funds that otherwise would go to pay public education will be redirected to repayment of TIF district debt.

In addition, our calculation of incremental property tax revenue could be understated because one property located within the TIF district may have been incorrectly exempted from taxation by the city. We are referring this matter to the Department of Taxes for review because it is largely an issue related to tax compliance and is

not significant to our audit objective. Refer to appendix III for more details.

(2) Retention of Statewide Education Increment

Burlington is permitted to retain up to 100% of the statewide education increment to the extent all of the incremental property tax revenue is pledged and appropriated for the repayment or prefunding of TIF district debt.²² According to an Attorney General’s Office opinion, per 32 VSA §5401(10)(E), in order for Burlington to retain all of statewide education increment, all incremental property tax revenue must be pledged and appropriated for TIF-related debt.

Further, the AG advised that to the extent incremental property tax revenue is not pledged and appropriated for payment of TIF-related debt, the underlying growth in property value is subject to the statewide education property tax and a portion of the statewide education increment is owed to the state (i.e. may not be retained by Burlington).

If incremental property tax revenue is pledged for repayment or prefunding of TIF district debt, but not all of the incremental property tax revenue is appropriated for this purpose, the municipality must remit a portion of statewide education increment to the state equivalent to the percentage of incremental property tax revenue not appropriated.

To illustrate, if a TIF district generated \$1 million of incremental property tax revenue, comprised of \$750,000 statewide education increment and \$250,000 municipal increment, and pledges and appropriates the entire \$1 million, then 100 percent of the \$750,000 of statewide education increment may be retained. If all of the \$1 million of incremental property tax revenue is pledged for repayment, but only \$400,000 is appropriated, only 40 percent of the statewide education increment may

²² Per Act 54 (2009 session), commencing January 1, 2010, Burlington’s borrowing period was extended for five years. As a result, if new debt is incurred, the city will no longer be authorized to retain 100 percent of the statewide education increment. Beginning in the fiscal year in which there is incurrence of new TIF district debt, the city will need to calculate and make an annual payment on December 10 to the Education Fund each year until 2025. The payment will be 25 percent of the incremental value generated subsequent to April 1, 2010, excluding the incremental value of two TIF district properties.

be retained. In this example, \$450,000 ($\$750,000 \times 60$ percent) of statewide education increment would be remitted to the state.

By entering into various financing arrangements, Burlington has pledged to repay approximately \$23.2 million in debt service using incremental property tax revenue. However, we found that Burlington's appropriation (e.g. actual debt payments and prefunding) of incremental property tax revenue for eligible debt repayment or prefunding from 1997 to 2010 ranged from 0 percent to 100 percent and the median was 85.1 percent of incremental property tax revenue generated by the district. The actual eligible use was less than one hundred percent because the city spent approximately \$1.2 million²³ on ineligible debt repayment (the Urban Reserve).

Burlington should have limited its retention of statewide education increment to the extent it had eligible uses. However, Burlington generally retained all of the statewide education increment and this resulted in a shortfall of payments to the state education fund. We recalculated how much education increment Burlington should have retained from 1997 to 2010, correcting for 1) Burlington's incorrect inclusion and exclusion of municipal tax rates and 2) incorrect use of funds to repay Urban Reserve debt. We concluded that Burlington did not remit \$1 million in statewide education increment²⁴ owed to the state. See table 3 for an illustrative year, 2009, showing the calculation of the amount of statewide education increment that should have been remitted to the state that year.

²³ The \$1.2 million is comprised of municipal and statewide increment.

²⁴ An additional \$200,000 represents municipal increment.

Table 3: Calculation of Burlington's Percentage of Incremental Revenue Appropriated and Underpayment of Statewide Education Increment for FY 2009

Description	Percentage of Incremental Revenue Appropriated	Calculation of Underpayment
Statewide education increment	\$1,059,000	
Municipal increment ^a	352,000	
Total incremental property tax revenue	1,411,000	
Eligible debt service payments ^b	1,259,000	
Percent of incremental property tax revenue appropriated (\$1,259,000/\$1,411,000)^c	89.2%	
Amount of statewide education increment actually retained		\$1,058,000
SAO calculation of statewide education increment that should have been retained (\$1,059,000 x 89.2 percent)		945,000
Amount of Burlington's underpayment to State for FY2009		\$113,000

^a Includes revenue associated with all municipal tax rates, except the tax rates that met the statutory requirement for exclusion. See table 2 for rates that we excluded.

^b Excludes payments of \$106,447 made for the Urban Reserve debt.

^c The percentage of incremental property tax revenue appropriated by Burlington differed for most years.

Burlington's use of incremental property tax revenue for ineligible purposes and retention of more statewide education increment than allowed per statute increases the likelihood that the city will retain statewide education increment for a greater period of time than if Burlington administered its TIF district in accordance with statute.

Burlington Did Not Meet All Reporting Requirements, but the Information Reported Was Consistent with Its Financial Records

At various times Burlington has been required to issue reports related to the TIF district to both city and state organizations (executive and legislative branches).

City Council

In the first year of the TIF district, the city assessor was required to report the assessed value of the property within the TIF district to the city council. The city assessor did not report the assessed value of the TIF district property in the first year of the TIF district.

In each year thereafter (until the end of the TIF district life), the assessor is required to certify and report to the city council the amount the TIF district properties have either increased or decreased in relation to the value established in the first year of the district. The city assessor did not report the changes in assessed TIF district property value to the city council.

State Agencies

Per a statutory amendment effective in 2008 the city is required annually to provide information about the TIF district to DOT and the Vermont Economic Progress Council (VEPC) by December 1.²⁵ The required information includes scope of the planned improvements and development, debt service payments, the original taxable property, incremental property value growth, the annual tax increment, and the annual amount of tax increments utilized.

The city did not provide the required annual reports to VEPC or DOT by the December 1 deadline. Although Burlington did not provide the annual reports, one piece of the required data, incremental property growth was provided to DOT annually in connection with the state's data gathering processes related to statewide public education funding. We found this reported data to be consistent with city schedules. Nevertheless, the other required data was not provided to the DOT or VEPC.

²⁵ 24 VSA§1901.

Legislative Committee

The city was required to provide a one-time report to the Joint Fiscal Committee (JFC) in August 2009. Also commencing July 1, 2010, the city is required to report annually to the Joint Fiscal Committee.

The city submitted the one time report to the JFC by the August 2009 deadline and the report contained accurate information, based upon the city's records. Although the filing of the annual report to the JFC is outside the scope of our audit (i.e. subsequent to June 30, 2010), we obtained the reports filed July 1, 2010 and July 1, 2011 and it appears that these reports were filed timely and contained the information required by statute.

The city's failure to meet some of its reporting requirements was the result of 1) a lack of documented policies and procedures related to TIF district reporting requirements, 2) a lack of awareness of the requirement to provide data to the city council and 3) city officials' belief that statutory amendments subsequent to the establishment of Burlington's TIF district generally did not apply.

If the city had established and documented policies and procedures related to reporting requirements, they may have recognized that statute required that certain data be reported to the city council and to VEPC and DOT. Without documented procedures, the risk increases that reporting will not be timely or will not occur at all.

According to city officials, they were not aware of the requirement to report to the city council until we brought it to their attention. The city officials were aware of reporting requirement to DOT and VEPC; however, they thought the requirement did not apply to them since it was effective subsequent to the establishment of the TIF district. In addition, according to the Executive Director of VEPC, he believed that the annual reporting requirement did not apply to Burlington. However, commencing in 2011, VEPC developed a template for all municipalities with TIF districts to complete, including Burlington.

Timely and accurate reporting of the TIF district data to city and state officials facilitates monitoring of the status of the TIF district which is critical to ensuring that the TIF district operates as expected. Accomplishing this may be difficult without periodically reviewing applicable statutes and establishing policies and procedures to ensure timely and accurate reporting. Further, without accurate information, municipal and state officials may find it difficult to make informed decisions about the program.

Burlington's Establishment and Monitoring of Performance Measures Was Limited

The city's establishment and monitoring of performance measures to indicate the extent to which its TIF district was meeting municipal and state economic and fiscal goals was limited. Specifically, Burlington did not 1) establish measures for all objectives (i.e. goals), 2) consistently set targets and 3) consistently track actual results. Without pertinent data indicating the extent to which the municipality has met its goals, decisions made regarding the TIF district may be less effective than if complete performance information was available and utilized.

Although the statutes governing TIF district creation and administration do not contain an explicit requirement for municipalities to establish and monitor performance relative to achievement of the three TIF district goals, benefits can accrue from the effective use of performance measurement. In addition, the state emphasizes performance measurement via its requirement for state organizations to annually submit a variety of performance measurement information to the general assembly. According to the Government Finance Officers Association, for every specific economic development incentive (e.g. tax increment financing), the economic benefit to the government, as well as the cost of the incentive, should be measured and compared against the goals and criteria that have been previously established for the incentive.

Table 4 provides a comparison of the state's and city's objectives (i.e. goals) related to measures and targets established by Burlington and whether actual results were monitored.

Table 4: Comparison of Objectives and Measures to Targets Established and Actuals Monitored

Objective	Measures	Targets Established	Actuals Monitored
Broaden the tax base	Growth in incremental property value and incremental property tax revenue	No ^a	Yes
Encourage development	Construction of additional parking facilities	No	No ^b
	Creation of affordable housing on waterfront	Yes	No ^b
	Square footage of remediated waterfront properties	Yes	No ^b
	Lake Street improvements, including installation of curbing and sidewalks	Yes	No ^c
Improve employment opportunities	None	No	No

^a Targets were established for property value growth for the TIF district in 1996, however the targets were not updated when the TIF district was significantly expanded in 1997.

^b According to the Director of Community Economic Development Organization, the project status associated with the performance measures has only been updated through 1998.

^c Some of the Lake Street improvements were completed and reported in 1998. However, other improvements were not completed and the city did not monitor results subsequent to 1998.

The city did not consistently monitor the performance measures it had established because the city considers its primary TIF district performance measure the growth in property values in the TIF district and city officials believe this measure is sufficient to track the performance of the TIF district. Further, the city believes it is not compelled to establish and track performance measures since statute does not require it.

Although the city has consistently measured and monitored the growth of property values in the TIF district, without comparison to a target for growth it is difficult to discern whether the level of actual activity was the expected outcome. Further, without measures for all objectives and consistent monitoring for the measures it established, the city lacks a systematic mechanism to accurately determine whether the TIF district is operating as intended.

Conclusion

Burlington adhered to requirements in state statute associated with establishing and expanding its TIF district. However, certain aspects of Burlington's practices in administering its TIF district were not in accordance with statutory requirements. Specifically, the city used approximately \$1.2 million of the incremental property tax revenue generated by its TIF district to repay debt associated with a land acquisition that occurred prior to the creation of the TIF district and thus was ineligible to be paid with incremental property tax revenue. This mistake is the primary cause of the reduced percentage of eligible uses of incremental property tax revenue which impacts the amount of statewide education increment that may be retained. The city should have limited its retention of statewide education increment to the extent it had eligible uses. However, Burlington generally retained all of the statewide education increment and did not remit \$1 million in statewide education increment owed to the state. City officials provided various rationales for their approach to administering the TIF district, including a legal opinion justifying aspects of their approach. We considered the city's legal justifications but disagree based on discussions with the AG's office and reviews of records and other evidence.

Due to the extension of the city's borrowing period for an additional 5 years commencing January 2010, it's possible that the waterfront TIF district will continue to retain statewide education increment through 2025. Because of the continuing effect that this will have on statewide education funding, it is critical that Burlington correct the mistakes in its approach to administering the TIF district. Without such a correction, Burlington could continue to retain statewide education property taxes that should be remitted to the state.

Recommendations

We recommend that the Burlington chief administrative officer:

1. Cease using incremental property tax revenue for payment of the certificates of participation related to the 1991 purchase of the Urban Reserve,
2. Modify the calculation of incremental property tax revenue to include all components of the municipal tax rates that do not have restricted uses approved by the legislature,

-
3. Work cooperatively with the state to resolve the city's \$1 million shortfall in payments to the state education fund,
 4. Designate a city official to be responsible for reviewing the statutory requirements for reporting and to document policies and procedures to ensure timely and accurate reporting, and
 5. Designate a city official to establish and monitor a set of performance measures, including numerical targets for all measures.

Management Comments and Our Evaluation

In a letter dated May 9, 2012, the city attorney and corporation counsel for the City of Burlington provided a written response to a draft of this report on behalf of the city, which can be read in its entirety in appendix IV.

The city generally disagreed with the findings of our report and proffered various legal arguments, but no new documentary evidence, to support their positions and disagreements. In addition, the city states that even if our conclusion (the city inappropriately used incremental property tax revenue to pay for Urban Reserve debt) is correct, the remedy would not be to refund the state education increment to the state, but rather the city could and would prefund other TIF eligible debts. We consulted with the attorney general's office regarding the city's legal arguments in its comments on the draft report and the AG's office stated that its conclusions remain the same. Given that the AG's conclusion remains unchanged and the city did not provide new documentary evidence, we did not revise our findings and conclusions, although we provided clarifying language where appropriate. In addition, based on our consultation with the AG's office, we revised the report title and our third recommendation to recognize that state statute does not explicitly address how to resolve the city's inappropriate use of incremental property tax revenue and the resulting \$1 million shortfall of payments to the state's education fund.

Appendix IV contains the city's response followed by our detailed analysis. Appendix V contains the city's exhibits that it included in its response. Many of Burlington's arguments relate to their contention that they don't owe any money to the state. Our evaluation addresses each of their arguments, but our overall conclusions remain the same. The following summarizes the city's major points and our evaluation.

Utilization of incremental property tax revenue to pay for Urban Reserve debt

The city stated that the use of incremental property tax revenue to pay for the 1999 certificates of participation issued to refinance the Urban Reserve property debt was appropriate and legal and that the city does not owe any money to the state. The city posits three main arguments for its position.

Definition of improvements

The city contends that the AG's office and our office have construed the definition of improvement too narrowly and, that at the time of the Urban Reserve refinancing, municipalities were given wide latitude to define what constituted an improvement. The city reasons that its retention of the ownership of the Urban Reserve was preferable to the Burlington City Retirement System ("Retirement System") gaining ownership per the terms of its financing arrangement with the city.²⁶ Refinancing the Retirement System debt in 1998 with certificates of participation (COPs) enabled the city to realize its preference and the city argues this constitutes an improvement. In the first place, the city did not appear to be at risk of losing ownership of the Urban Reserve property. Specifically, the second amendment to the Purchase and Sale contract with the Retirement System, dated September 30, 1998, converted the arrangement to a long term financing arrangement, extinguishing the October 15, 1998 purchase option. Second, even if the city had failed in its' efforts to amend the financing arrangement with the Retirement System, according to the advice previously provided to us by the AG's office, refinancing a 1991 debt is not an improvement associated with the city's TIF district. The relevant debt to measure against the statutory borrowing period is the initial debt in 1991 that funded the city's acquisition of the property almost four years prior to the creation of the TIF district. Third, the city took title to the property in 1991 and continued to be the owner, regardless of the financing mechanism.

Retroactive approval

According to the city, the legislature retroactively approved Burlington's use of COPs in its waterfront TIF district under broad language which encompassed all of the COPs previously issued, specifically the 1999 COPs used to refinance the Urban Reserve property. The legislature's retroactive

²⁶ Per the terms of the arrangement, the city was required to pay \$1,148,000 plus interest to the Retirement System prior to October 15, 1998 or the Retirement System had the option to purchase the Urban Reserve.

authorization mentions a period during which COPs may be issued that is inclusive of the issuance date of the 1999 COPs for the Urban Reserve debt refinancing. However, this authorization clarifies the period during which Burlington may issue COPs, rather than approves the issuance of specific COPs during the period.

Based upon our consultations with the AG's office and testimony presented by Burlington on April 9, 2008 to the Senate Finance Committee, it appears the intent of the legislature was to settle a dispute between DOT and Burlington regarding whether the city could use COPs as a type of financing instrument for improvements in its TIF district rather than to approve the issuance of specific COPs. During its legislative testimony, the city requested 1) that it be able to continue to utilize COPs to finance TIF district improvements even though DOT asserted that its options were limited to general obligation bonds and 2) that municipalities be given greater flexibility in financing options for their TIF districts. Further, during its testimony, the city did not mention the Urban Reserve 1999 certificates of participation.

State was aware of Burlington's use of TIF revenue for the Urban Reserve

Finally, the city argues that the state should be estopped from asserting any claim respecting its use of TIF increment for a variety of reasons, including that the city has openly presented the use of TIF increments to refinance the Urban Reserve debt and their belief that the state knew the purpose for which the COPs were issued, to support their contention that the state knew about and acquiesced to the city's use of incremental property tax revenue to pay for the Urban Reserve refinanced debt.

During the course of our audit, we concluded that DOT had no basis to know that incremental property tax revenue was being used to repay debt associated with a property acquired prior to the creation of the TIF district. Our conclusion was based upon documentary evidence provided by Burlington, including data Burlington provided to DOT in connection with DOT's and JFO's limited review of TIF districts in 2009. For example, Burlington provided DOT a schedule of TIF district improvements and described one project as "Urban Reserve acquisition" and the date and type of financing as "1999; certificates of participation." Burlington also provided debt schedules which describe the 1999 COPs as "Urban Reserve 1999." The city also provided DOT with a copy of the 1996 city ballot referendum that lists various uses of tax increment, including for retirement and/or refinancing of the urban reserve debt. Taken together, a reader would not be able to discern that the acquisition and original financing of the property occurred in 1991.

The city also claims that it provided the 1996 ballot referendum to VEPC and the legislature without any questioning of the propriety of using the TIF increments to refinance the urban reserve debt, but the city did not provide our office with any documentary evidence to substantiate the claim.

The remaining reasons cited by the city in its argument do not appear relevant. For example, the city states that the state was party to agreements related to the deeding of the Urban Reserve lands to the city in 1991, but the TIF district wasn't established until 1996 and the refinancing was in 1999 so it is difficult to see how these disparate dates can be connected. The city also cites the Agency of Commerce and Community Development (ACCD) award to the city of a \$2.5 million Downtown Board grant to be utilized for repayment of debt incurred to construct a parking facility, but the parking garage is a separate transaction and the grant agreement signed by ACCD does not mention the Urban Reserve, so the grant seems unconnected to the Urban Reserve as well.

Calculation of incremental property tax revenue

The city stated that it believes its calculation of municipal incremental property tax is correct and substantially complied with legal requirements, but that since it is a complex matter, it plans to work cooperatively with state entities such as VEPC, DOT and the AG's office to reach an understanding of how to treat municipal taxes which seem to be specifically dedicated and other taxes which the city believes the treatment of is ambiguous. Our audit report reflected the advice of the AG's office that stated that Burlington may exclude a portion of its municipal tax revenues from its TIF revenue calculation if the legislature has approved the designation of these revenues for a specific purpose. The AG found that there are several municipal taxes (see report Table 2) that are authorized by Burlington's city charter (approved by the legislature) for a specific purpose. Further, the AG advised that other taxes authorized by the city's charter, which the city excluded from its calculation, did not have language specific enough to override the general rule that the TIF calculation includes "all taxes levied by the municipality" and must be included in the TIF revenue calculation. The ambiguity cited the by AG's office is whether any municipal taxes can be excluded, but it has taken a broad view that the legislature may have intended that some be excluded, namely those tax rates that the legislature has approved for a specific purpose. This opinion has the benefit of bringing consistency to Burlington's own approach since the city was not consistent in applying its own methodology.

Although we believe our current recommendation is valid given the current statutes and the AG's opinion, we encourage Burlington to work cooperatively with the state given the significance of the municipal increment that has been excluded by Burlington and used for non-TIF district purposes. From the creation of the TIF district in 1996 through June 30, 2010, Burlington excluded approximately \$1 million of municipal increment from the TIF district, as a result of excluding components of its tax rate from the calculation of incremental property tax revenue.²⁷ As Burlington noted in their response, this issue is likely to have significance for other municipalities as well.

Reporting requirements

The city believes it has substantially complied and also believes that most reporting requirements do not apply to the city's waterfront TIF district, reasoning that those requirements were imposed after its creation and implementation and that VEPC operated with the understanding that the VEPC reporting and approval requirements did not apply to the city's TIF district. The city also believes that to the extent there were reporting requirements which the city failed to adhere to, the failure was a technical rather than a substantive omission.

Based on advice we obtained from the AG's office and legal counsel for the DOT regarding how to determine whether statutory amendments apply to existing TIF districts, we concluded that the reporting requirements we specify in our report are applicable to the city's TIF district. According to the legal counsel we received, amendments are generally effective prospectively unless there is evidence to suggest otherwise, such as a statement of legislative intent at the beginning of a law which might indicate otherwise or if the facts and circumstances in a specific situation indicate the amendment is not applicable. There was no statement of legislative intent relative to the addition of annual reporting requirements in Act 190 (2008) and the city has not provided us with documentary evidence that the city of Burlington was specifically exempted from the annual reporting requirement.

The city indicated that VEPC believed that the city was exempt from these reporting requirements as well. According to the VEPC executive director,

²⁷ SAO calculated incremental property tax revenue through June 30, 2010 according to statutory requirements and the AG's guidance that certain tax rates may be excluded from the calculation if the use has been restricted for a specific purpose. Based on this, we calculated that the TIF district generated \$58,000 more revenue than the city accounted for in its records.

he considered Burlington exempt from the requirement until recently. Commencing in 2011, VEPC developed a template for all municipalities with TIF districts to complete and according to the director, this would satisfy the municipalities' Act 190 reporting requirements. Accordingly, we will add this information to our report, but it does not change our conclusion that the city did not comply with reporting requirements, rather it describes an additional cause for the city's failure to comply.

The city stated that it does not object to our recommendation to designate a city official to be responsible for reviewing statutory requirements and documenting policies and procedures to ensure timely and accurate reporting. In addition, the city plans to work with relevant state entities to ensure it remains fully compliant with all legal requirements for its TIF districts going forward.

Performance measures

The city disagreed with our finding that the city's establishment and monitoring of performance measures was limited since there are no legal requirements for establishing and monitoring a set of performance measures for the waterfront TIF district. However, the city notes that it has no objection with respect to adopting our recommendation relative to the new projects and financing in the waterfront TIF district and the new downtown TIF district, since it believes that these districts are subject to statutory requirements relative to performance measures.

Although there are no explicit legal requirements for municipalities to establish and monitor performance measures for TIF districts, benefits can accrue from the effective use of performance measurement and not all good practices are mandated in statute. Further, without measures and targets for all municipal and state economic and fiscal goals, it is difficult to discern whether Burlington's waterfront TIF district is operating as intended. Given that the city is utilizing state education funds to repay the debt associated with TIF district improvements, even absent a statutory requirement to measure the results, the city should be able to provide the state with information regarding the quantitative results of its investment in the city's TIF district.

The city also disagreed with the data presented in Table 4 in the report that indicates that actual results were not monitored for construction of parking facilities and creation of affordable housing on the waterfront subsequent to 1998. However, the city did not provide additional documentary evidence to demonstrate that actual results were monitored. The city acknowledges that

it did not update a performance measurement document, but stated that city officials can identify the number of additional parking facilities constructed, etc. and notes that the city could work with state entities to produce or reproduce data for measuring the success of the waterfront TIF district.

Other Comments from the City of Burlington

Also, in an email dated May 9, 2012, the assistant city attorney points out that, although we addressed our recommendations to the assistant administrative officer, the city has an interim chief administrative officer and requests that we address our recommendations to the City of Burlington rather than to a specific city official. Generally accepted government auditing standards specify that recommendations are effective when they are addressed to parties that have the authority to act and our office's adopted practice is to address recommendations to specific officials. In keeping with these standards and our own practices, we will modify the report to address the recommendations to the chief administrative officer. We reviewed the duties of chief administrative officer delineated in the city's charter and it appears that this position, interim or otherwise, would have the authority to act upon the recommendations.

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In accordance with 32 V.S.A. §163, we are also providing copies of this report to the secretary of the Agency of Administration, commissioner of the Department of Finance and Management, and the Department of Libraries. In addition, the report will be made available at no charge on the state auditor's web site, <http://auditor.vermont.gov/>.

Appendix I

Scope and Methodology

To address our three audit objectives we performed an analysis of the legislative statutes related to the creation, financing, administration and reporting requirements for tax increment financing districts in Vermont (contained in Titles 24 and 32), including numerous amendments and legislative acts since the original enabling legislation in 1985 (Act 87). In addition, we met with officials from the municipality and DOT to understand their statutory interpretation of TIF legislation and sought authoritative opinions from the Office of the Attorney General in cases in which interpretations diverged.

We reviewed a wide variety of published guidance and research on the use of tax increment financing as an economic development tool. This included publications by the Government Finance Officers Association, audit reports of TIFs in other states, a 2009 study conducted jointly by DOT and the legislative joint fiscal office, which reported specifically on the existing TIF districts in Vermont,²⁸ among others.

In planning and executing our work with respect to our first objective, we interviewed municipal officials and obtained available documentation for the establishment and expansion of the TIF district, public hearing warnings, city council approval, and the TIF district plan. These documents and records were assessed against the requirements contained in Vermont statutes Titles 24 and 32 to determine whether the municipality adhered to requirements for the establishment of a TIF district. We reviewed documents for the debt financing including voter warnings and approvals, loan documents, and a grant agreement.

In performing work in support of our second objective, we interviewed city officials, personnel from DOT's Division of Property, Valuation and Review and the Vermont Department of Education regarding their processes, policies, and procedures related to administering the TIF district. We performed walkthroughs of the city's processes related to administering the TIF district in order to gain an understanding of internal controls sufficient to plan the scope of our detail testing related to utilization of incremental property tax revenue, the calculation and retention of incremental property tax, and reporting. As a result, we determined to perform a combination of detail testing for two years, FY 2005 and FY 2006, and recalculations of key calculations from inception.

²⁸As required by 32 VSA §5404a(i).

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We performed a variety of tests, as follows:

- verified the allowability of TIF expenditures by reviewing original source documentation,
- verified the debt service payments reported in the city's schedule of TIF revenue and debt service payments to the amortization schedules and bank statements,
- cross referenced TIF parcels from the property maps to the TIF property reports to determine proper inclusion/exclusion of TIF properties since inception of the TIF district,
- reviewed TIF property value trends for all years by comparing the property values from inception through 2010 for consistency, errors, and missing information,
- verified the information reported on the FY 2005 and FY 2006 TIF property reports to source documents such as the grand list, property tax bill, lister cards to validate the accuracy of the information reported,
- reconciled Form 411²⁹ to the grand list for FY 2005 and FY 2006 to ensure that the appropriate TIF and Non-TIF property information was reported to the state,
- for FY 2005 and FY 2006 verified that the city remitted the appropriate statewide education property taxes to the state by reconciling the information reported on Form 411 to the Department of Education cash flow worksheet³⁰ and the city's general ledger,
- obtained the city's TIF revenue calculation schedule for FY 2005 and FY 2006, recalculated the revenue and agreed the information used in the calculation to underlying support such as tax rates and TIF property reports,

²⁹ Form 411 is the required form that each municipality must use to report property information to the state each year.

³⁰ Department of Education utilizes the cash flow worksheet to calculate the amount of statewide education property tax each municipality owes to its local school district and/or to the state.

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- verified the TIF revenue reported by the city for FY 2005 and 2006 in its revenue calculation schedule to the city's general ledger,
- recalculated the city's TIF revenue since inception of the TIF. Included in the analysis was a calculation of TIF revenue by the SAO using all appropriate tax rates, a summary of TIF revenue calculated and retained by the city, and a reconciliation of both calculations,
- calculated incremental revenue utilized annually and any amounts owed to the State,
- assessed the timeliness of the city's reporting by comparing the dates the reports were delivered to the report deadlines, and
- assessed the accuracy of the city's reports by comparing the information reported to the city's source documents and to our audited schedules.

We consulted with the AG and obtained legal opinions from the AG regarding 1) the applicability of statutory amendments to TIF districts that were established prior to the amendments, 2) the appropriate date for municipalities to establish OTV, 3) whether municipalities have the discretion to determine how much statewide education increment may be retained, 4) whether municipalities must adjust OTV as a result of reappraisals, 5) whether municipalities may exclude tax rates from the calculation of incremental property tax revenue, 6) whether refinanced debt may be paid with incremental property tax revenue if the original debt occurred prior to the creation of the TIF district and 7) whether statute includes remedies to address instances when a municipality does not remit appropriate funds to the state education fund.

Finally, in order to ascertain whether the city has owned the property known as the Urban Reserve since 1991, we engaged external legal services to review certain financing documents and perform a title search for this property. We also reviewed financing and other documents provided by the city related to the purchase and refinancing of the Urban Reserve. Further, we reviewed various documents to assess 1) the ownership and 2) the city's exemption from taxation of the 75 Cherry Street property, including lease and sublease agreements, warranty deed, property transfer tax return, property reports, and property tax abatement correspondence. In addition, we engaged external legal services to review certain documents and perform a title search for this property. We also requested an opinion from the AG regarding

Appendix I

Scope and Methodology

whether the city had the authority to exempt this property from taxation in the terms and conditions of its lease and sublease agreements.

Our audit approach to the third objective began by identifying and reviewing sources of information for best practices related to performance monitoring of TIF district financing. We made inquiries of city officials to determine if the city established performance measures for the TIF district or if there were any periodic reviews or mechanisms in place to monitor the actual performance of the TIF district. We also reviewed the TIF district and waterfront planning documents to ascertain if there were performance measures considered during the TIF's establishment.

We considered internal controls and information systems controls to the limited extent to which they related to our objectives. For example, we interviewed several members of city's staff (i.e., the TIF accountant, city assessor, project manager) to determine the levels of accounting and general data controls related to TIF district administration.

Our audit fieldwork was performed between May 2011 to February 2012 at the city offices in Burlington and at the state auditor's office in Montpelier. Except for the exception described below, we conducted this performance audit in accordance with generally accepted government auditing standards, which require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The standard that we did not follow requires that our system of quality control for performance audits undergo a peer review every three years. Because of fiscal considerations, we have opted to postpone the peer review of our performance audits. Notwithstanding this exception, we believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

The following summarizes the additions and amendments to TIF statutes that were made subsequent to the enabling legislation. The enabling legislation is summarized in the background section of the report.

Act 60, 1997 session

EXEMPTION OF TIF DISTRICT INCREMENTAL PROPERTY VALUE FROM EDUCATION PROPERTY TAX LIABILITY

Added: The incremental value of TIF properties for those municipalities with TIF districts³¹ established prior to June 10, 1997 is exempt from the determination of a municipality's education property tax, owed to the state, to the extent the taxes generated on the incremental property value are pledged and appropriated for repayment of bonded debt or prefunding future TIF district debt. [32 VSA §5401((10)(E)]

EXPANSION OF EXISTING TIF DISTRICTS

Added: Municipalities with existing TIF districts may expand those districts by June 30, 1997 and collect all state and local property taxes on properties within the TIF district and apply those revenues to repayment of debt issued to finance improvements with the TIF district. [32 VSA §5404a(c)]
Effective date: 1/1/98

Act 71, 1998 session

EXEMPTION OF TIF DISTRICT INCREMENTAL PROPERTY VALUE FROM EDUCATION PROPERTY TAX LIABILITY

Amended: The incremental value of TIF district properties is exempt from the determination of a municipality's education property tax liability to the extent approved by VEPC upon application by the district under procedures established for the approval of tax stabilization agreements under 32 VSA §5404a. [32 VSA §5401(10)(E)]

EXPANSION OF EXISTING TIF DISTRICTS

Amended: Municipalities with existing TIF districts must apply to VEPC for approval of the expansion those TIF districts following procedures used to approve tax stabilization agreements under 32 VSA §5404a . [32 VSA §5404a(f)]

RETENTION OF INCREMENTAL PROPERTY TAX REVENUE

Amended: To the extent approved by VEPC, the incremental revenue may be retained for the duration of the agreement up to a maximum of 10 years. [32 VSA §5404a(b)]

³¹ Limited to TIF districts established under subchapter 5 of chapter 53 of Title 24.

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Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

Effective dates: 32 VSA §5401(10)(E) is effective 6/26/97. 32 VSA §5404a(f) and 32 VSA §5404a(b) are effective 3/11/98.

Act 159, 2000 Session

TAX INCREMENT FINANCING – CITY OF WINOOSKI (Sec. 37 and 38 of Act 159 (2000)).

APPROVAL AND AUTHORIZATION

Added: General Assembly found that a TIF district in the city of Winooski, when more particularly defined and created as a TIF district pursuant to 24 VSA §1892, will provide multiple public benefits including, revitalization and improvement of a significant downtown area and enhanced employment opportunities within the city of Winooski and surrounding region. [Section 37 of Act 159, 2000 Session]

EXEMPTION FROM VEPC APPROVAL REQUIREMENT

Provisions of 32 VSA §5401(10)(E) and 32 VSA §5404a shall not apply to the city of Winooski TIF district. The general assembly intended that Sec. 37 and Sec. 38 of Act 159 (2000) substitute for the provisions of 32 VSA §5401(10)(E) and 32 VSA §5404a. [Section 38 paragraph 5 of Act 159, 2000 Session]

PROJECT REQUIREMENTS

Added: At least 10% of the housing in the TIF district shall at the time of initial occupancy be affordable housing. [Section 38 paragraph 8 of Act 159, 2000 Session]

FINANCING

Added: Bonds must be issued pursuant to 24 VSA §1897 and within five years of July 1, 2000. Maximum term for repayment of bonds is 20 years. Total principal may not exceed \$30,000,000. [Section 38 paragraph 1 of Act 159, 2000 Session]

EXCESS VALUATION

Added: Excess valuation means the difference between the current grand list value and the grand list value at commencement of development. [Section 38 paragraph 3 of Act 159, 2000 Session]

UTILIZATION OF TAX INCREMENT

Added: In addition to uses specified in 24 VSA §1897 (e.g. bond repayment), tax increment revenue shall be used to fund reserves and accounts necessary to repay or defease bonds. [Section 38 paragraph 2 of Act 159, 2000 Session]

Added: 5% of the education taxes imposed annually on the excess valuation of the residential property within the TIF district shall be paid to the education fund. [Section 38 paragraph 3 of Act 159, 2000 Session]

Added: Until bonds are paid in full or defeased through fully funded reserves, 100% of the municipal taxes assessed against the excess valuation of TIF district property shall be

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

pledged and appropriated for debt service on bonds. [Section 38 paragraph 3 of Act 159, 2000 Session]

EXEMPTION FROM EDUCATION PROPERTY GRAND LIST

Added: Excess valuation of property within TIF district shall not be included in the education property grand list as taxable property under 32 VSA §5402 or 32 VSA §5404 until bonds issued to finance TIF district improvements are paid or fully reserved. [Section 38 paragraph 3 of Act 159, 2000 Session]

REPORT

Within 60 days of issuing bonds, the city of Winooski shall provide to the joint fiscal committee a comprehensive cost-benefit analysis and financing data. [Section 38 paragraph 9 of Act 159, 2000 Session]
Effective date: 7/1/2000

Act 184, 2006 session

DEFINITION OF IMPROVEMENTS

Amended: Includes brownfield remediation and infrastructure for transportation, telecommunications, wastewater treatment and water supply. [24 VSA §1891]

DEFINITION OF ORIGINAL TAXABLE PROPERTY

Added: All the taxable real property located within the district on the day the district was created. [24 VSA §1891]

DEFINITION OF RELATED COSTS

Added: Related costs are expenses, excluding actual cost of constructing and financing improvements, directly related to creation of the TIF district and to attaining the purposes and goals of the TIF district. Includes reimbursement of sums advanced by municipalities relative to creation of TIF districts. [24 VSA §1891]

PURPOSE

Amended: Includes generation of incremental revenue to pay for related costs and expanded one of goals to encompass redevelopment of TIF districts, rather than just development. [24 VSA §1893]

APPROVAL

Added: Established criteria for VEPC to approve TIF districts pursuant to 32 VSA §5404a(h).

BORROWING PERIOD

Amended: A municipality may incur debt against the revenues of the TIF district for a period of up to 20 years following the creation of the district. [24 VSA §1894(a)]
Added: If debt is not incurred within the first five years following the creation of the district, the district must request reapproval from VEPC. [24 VSA §1894(b)]

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

DEBT AGREEMENTS

Added: Municipality's debt financing agreements must specify that, in the event the tax increment received by the municipality from property taxes is insufficient to pay the principal and interest on debt in any year, the municipality shall remain liable for full payment of bond principal and interest. [24 VSA §1897(b)]

CALCULATION OF TAX INCREMENTS

Added: The original taxable value must be adjusted by a multiplier³² upon a reappraisal of 20% or more of all parcels in a municipality. [24 VSA §1896(b)]

UTILIZATION OF TAX INCREMENT

Amended: For tax increment utilization approved pursuant to 32 VSA §5404a(g), no more than 75% of the state property tax increment from properties contained within the TIF district and no less than 75% of the municipal tax increment from properties contained within the TIF district may be used to service debt issued for improvements wholly or partly within the TIF district and for related costs. [24 VSA §1897(a)]

DISTRIBUTION OF INCREMENTAL TAX REVENUE

Amended: Any excess municipal tax increment³³ received in any tax year shall be distributed to the city, town or village in proportion that each budget bears to the combined total of budgets. Any excess statewide education tax increment received in any tax year shall be used only for debt prepayment, placed in escrow for bond payment or otherwise used for defeasance of bonds. [24 VSA §1900]

RETENTION OF INCREMENTAL PROPERTY TAX REVENUE

Amended: Allowed tax increments to be retained for payment of related costs. [24 VSA §1896(a)]

Amended: Municipalities that establish TIF districts³⁴ and obtain VEPC approval may apply no more than 75% of the statewide education increment, and no less than 75% of the municipal increment to repay debt issued to finance improvements and related costs for up to 20 years. The 20-year period commences April 1 of the year following VEPC approval. [32 VSA §5404a(f) and (g)]

EXPANSION OF TIF DISTRICTS

Deleted: Eliminated municipalities' ability to apply to VEPC for expansion of TIF districts. TIF districts may no longer be expanded. [Act 184 section 2h, 2006 session]

³² The denominator for the multiplier is the municipality's education property grand list *for the TIF district properties* in the year prior to the reappraisal and the numerator would be the municipality's reappraised education property grand list *for the TIF district properties*. Items in italics are an amendment in Act 66 of 2007 which was effective July 1, 2006.

³³ Excess means incremental tax revenue received in any tax year that exceeds amounts pledged for payment on TIF district bonds and related costs.

³⁴ Applies to municipalities that establish TIF districts under subchapter 5 of chapter 53 of Title 24.

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

REPORTING

Added: VEPC and Department of Taxes shall report to certain legislative committees regarding existing TIF districts on or before January 15 each year. Report must include items such as year of approval, scope of planned improvements, original taxable value of TIF districts property, tax increments and annual amount of tax increments utilized. [32 VSA §5404a(i)]

EXTENSION OF MILTON TIF DISTRICT

Added: Upon application to VEPC, the Milton Husky and Catamount TIF districts may be extended for an additional ten years beyond the initial 10 years originally approved by VEPC. May use OTV established at the initial approval of the TIF district to calculate incremental property tax revenue and may retain 75% of the incremental property tax revenue to repay debt issued to finance improvements within the TIF district and for related costs. [Sec. 2j of No. 184 of the Acts of the 2005 Adj. Sess. (2006)]
Effective date: July 1, 2006

Act 190, 2008 session

TYPES OF DEBT

Added: Financing means bonds, Housing and Urban Development Section 108 financing instruments, interfund loans within a municipality, State of Vermont revolving loan funds, and United States Department of Agriculture loans. [24 VSA §1891]

PURPOSE

Amended: Previously limited tax increment financing for those TIF districts improvements located wholly or partly within the TIF district. Amended to improvements that serve the TIF district. [24 VSA §1893]

APPROVAL OF FINANCING

Added: Prior to requesting municipal approval to secure financing, the municipality shall provide VEPC with all information related to proposed financing necessary for approval and to assure its consistency with the plan approved pursuant to 32 VSA §5404a(h). [24 VSA §1894(c)]

Added: Legal voters of a municipality, by a single vote, shall authorize the legislative body to pledge the credit of the municipality up to specified maximum dollar amount to be financed with statewide property tax increment pursuant to approval by VEPC. [24 VSA §1897(a)]

BORROWING PERIOD

Amended: The creation of the district shall occur on April 1 of the year so voted. [24 VSA §1894(a)(1)]

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

PERIOD THAT TAX INCREMENT MAY BE RETAINED BY MUNICIPALITY

Added: For debt incurred within the first five years after creation of the district, or within five years after reapproval by VEPC, the education tax increment may be retained for up to 20 years beginning with the initial date of the first debt incurred. [24 VSA §1894(b)]

UTILIZATION OF TAX INCREMENT

Amended: Municipal legislative body may pledge and appropriate, in equal proportion, state and municipal tax increments received from properties contained with the TIF district for financing improvements and related costs in the same proportion by which the infrastructure or related costs directly serve the district³⁵ at the time of approval of project financing by VEPC.³⁶ No more than 75% of the state property tax increment and no less than an equal percentage of the municipal tax increment may be used to service this debt from the TIF district properties. [24 VSA §1897(a)]

Amended: Tax increment utilizations approved pursuant to 32 VSA §5404a(f) shall affect the education property tax grand list commencing April 1 of the year following VEPC approval and shall remain available to the municipality for the full period authorized under 24 VSA §1894. [32 VSA §5404a(g)]

DISTRIBUTION OF INCREMENTAL TAX REVENUE

Amended: An equal proportion of any excess municipal tax increment and education tax increment³⁷ may be used for the prepayment of principal and interest on financing, placed in escrow for financing payment or otherwise used for defeasance of financing. Any remaining excess statewide education tax increment shall be distributed to the education fund. [24 VSA §1900]

AUDIT

Added: The state auditor of accounts shall audit all active TIF districts every three years. [32 VSA §5404a(k)]

REPORTING

Added: Municipalities with active TIF districts shall:

- (1) Report to VEPC and the Department of Taxes on or before December 1 of each year. Report shall include items such as year of approval, scope of planned

³⁵ The proportionality rule relates to the determination of the proportion of infrastructure improvements or related costs that directly serve the TIF district. Municipal and state tax increments may only be used to repay a proportion of debt incurred for infrastructure or related costs in the same proportion that the improvements or related costs directly serve the district.

³⁶ VEPC shall apply a rough proportionality and rational nexus test in cases where essential infrastructure does not reasonably lend itself to a proportionality formula. Per VEPC guidelines, this means VEPC will use available data from comparable situations to make a proportionality determination. The determination will utilize a matrix of factors, such as location, impact on TIF district and whether it is required for the broad TIF outcomes.

³⁷ Excess means incremental tax revenue received in any tax year that exceeds amounts pledged for payment on TIF district financing and related costs.

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

improvements, original taxable value of TIF districts' properties, tax increments and annual amount of tax increments utilized. [24 VSA §1901]

- (2) Report tax increment financing actual investment, bond or other financing payments, escrow status and related cost accounting to VEPC according to the municipal audit cycle. [24 VSA §1901]

MILTON TIF DISTRICT

Amended: May apply no more than 75% of the statewide property tax increment and an equal percent of the municipal tax increment to repay debt issued to finance improvements that serve the TIF district and for related costs, upon application by Milton. Must apply equal percentages of the statewide property tax increment and municipal property tax increment to debt obligations incurred prior to April 1, 2009 for the Husky and Catamount TIF districts. Proportionality rule of 24 VSA §1897 does not apply to Husky and Catamount TIF districts. [Sec. 68 of No. 190 of the Acts of the 2008 Session]

CITY OF WINOOSKI - FY2008 COMMON LEVEL OF APPRAISAL³⁸

Added: City shall use a common level of appraisal factor of 1.0952 for fiscal 2008 reappraisal. Overpayment of education property taxes from city of Winooski to the education fund in fiscal 2008 shall be credited against the city's 2009 education property tax liability. [Sec. 70 Act 190 (2008)]

CITY OF WINOOSKI –CALCULATION OF EDUCATION TAXES DUE TO THE EDUCATION FUND

Amended: 2% of the education taxes imposed annually on the excess valuation of the property within the TIF district shall be paid to the education fund. [Sec. 38(3) OF No. 159 of Acts of 2000]

CITY OF BURLINGTON - RETROACTIVE APPROVAL OF TIF FINANCING

Added: Retroactive approval to June 30, 1997 for Burlington's use of certificates of participation and HUD Section 108 loans from April 1, 1996 to March 31, 2006 to finance public improvements within the TIF district. Restricted retention of education property taxes for repayment of debt to 20 years from date debt was incurred, including any refinancing. [Sec. 72 of No. 190 of the Acts of the 2008 Session]

Effective dates: upon passage, June 6, 2008, except July 1, 2008 for amendment to Sec. 68

Act 54 of 2009

MILTON TIF DISTRICT (retroactive to July 1, 2008)

³⁸The Common Level of Appraisal is the ratio of a municipality's total grand list value to its corresponding "equalized" value derived through DOT's Property Valuation and Review estimate of market value study. In other words, it is a percentage that compares local assessments to Property Valuation and Review's estimate of market value. The Common Level of Appraisal is based on the relationship between the assessed value and the sale price of a property. For example, if a property is assessed for \$75,000 and sells for \$100,000, the ratio is 75%.

Appendix II

Summary of Select Additions and Amendments to State Statutes Relevant to Establishing and Administering TIF Districts

TYPES OF DEBT

Added: Milton is authorized to use types of debt financing, in addition to those specified in 24 VSA §1891(7) including conventional bank loans; certificates of participation, approved by the state treasurer; lease-purchase, approved by state treasurer; and revenue anticipation notes, approved by state treasurer.

APPROVAL OF FINANCING

Added: Legal voters of Milton may authorize selectboard to pledge credit of Milton for all debt obligations pursuant to 24 VSA §1897(a) in more than one vote.

RETENTION OF EDUCATION TAX INCREMENT

Added: Tax increment may be retained for up to 20 years beginning with the initial date of creation of the district³⁹ or on the date first debt incurred, at Milton's discretion. If Milton elects to start retaining education tax increment more than 5 years beyond initial date of creation, OTV shall be recertified.

BURLINGTON TIF DISTRICT (effective July 1, 2009)

DEBT BORROWING PERIOD

Added: Borrowing period for existing TIF district extended for additional 5 years, commencing January 1, 2010.

SUBMISSION OF INFORMATION TO JOINT FISCAL COMMITTEE

Added: Submit to Joint Fiscal Committee 10 days prior to September 2009 meeting (1) a business plan and projection of new statewide education increment growth anticipated to be financed by debt incurred during 5- year extension and (2) a proposal for payment to education fund in lieu of tax increment which would approximate 25% of new statewide education increment and the mechanism for payment and timing of payment by Burlington to the education fund. If Joint Fiscal Committee approves plan and Burlington incurs new debt in the 5- year extension, then Burlington will pay the education fund the amount approved by Joint Fiscal Committee.

Special Session Act No. 3 (2009)

Technical Corrections of Act 54 of 2009 Session

MILTON TIF DISTRICT

BORROWING PERIOD

Added: Milton shall have ten years after the creation of the district to begin incurring debt.

³⁹ Per 24 VSA §1894(a)(1) creation of a TIF district occurs April 1 of the year the municipal legislative body approved the creation of the district.

Appendix III

Tax Compliance Matter Referred to Department of Taxes

Our audit identified that the land and parking garage at 75 Cherry Street may have been incorrectly excluded from statewide education and municipal property taxes by the city. We are referring this issue to DOT since it is a matter of tax compliance and not significant to our audit objectives. In this appendix, we provide a summary of the information we gathered during the course of our audit, including ownership of the property, tax status of the property and whether taxes were paid for the property. Because DOT has not had time to review this information, we have not drawn a conclusion about the issue.

Ownership of the Property

The 75 Cherry Street property summary record⁴⁰ maintained by the city assessor's office contains information that is not consistent with other information the city provided during the course of our audit. For example, the property summary record for 75 Cherry Street indicates that it includes the land and the parking garage and lists the city as owner. However, a quit claim deed filed with the city clerk shows that the city sold the land to Security Capital Corporation ("Security") in June 1993. In addition, a sublease agreement for the land, between the city and Donohoe O'Brien Burlington Square Associates Limited Partnership ("Donohoe"), acknowledges that the parking garage is owned by Donohoe.⁴¹

Due to the inconsistencies between the property summary record and other data provided by the city, we engaged an attorney to perform a title search for the 75 Cherry Street property and provide a legal opinion as to ownership of the land and the parking garage facility from 1993 through December 31, 2011. We also sought the advice of the attorney with regard to whether a lease (between Security and the city) and the sublease (between the city and Donohoe) of the land would impact ownership. According to the attorney's opinion, Security has had title (i.e. ownership) to the land since purchasing it from the city on June 25, 1993, and the parking facility was been owned by various commercial entities, most recently The Burlington Town Center

⁴⁰ Property summary records are maintained in the city's computer-assisted mass appraisal system and include information such as property owner, sales history, valuation and tax status.

⁴¹ Donohoe assigned the sublease to subsequent owners of the parking garage.

Appendix III

Tax Compliance Matter Referred to Department of Taxes

LLC (BTC). In addition, the attorney concluded that the lease and sublease does not impact ownership of the land.

See table 5 for a listing of the owner, lessee, and sub-lessees of the land and the owners of parking facility from June 25, 1993, to December 31, 2011.

Table 5: History of Ownership and Leases for 75 Cherry Street from 1993 - 2011

Land				Parking Facility	
Owner	Lessee	Sub-lessee	Period	Owner	Period
Security	Burlington	Donohoe	1993 – 2000	Donohoe	1993 - 2000
Security	Burlington	DKB	2000 - 2004	DKB	2000 - 2004
Security	Burlington	BTC	2004 - 2011	BTC	2004 - 2011

Tax Status

The land and parking garage are owned by commercial entities and, as real property, would generally be taxable to the owner of record as of April 1 of the tax year. However, records maintained by the city, including tax abatement correspondence addressed to Security Capital Corporation (“Security”) and the property summary record maintained by the city assessor’s office, indicate that the land and the parking facility (the “property”) at 75 Cherry Street have been exempt from property tax since 1995.

The classification of the property as tax exempt may be due to the terms and conditions of the lease and sublease arrangements for the land. According to the terms of the lease between Security and Burlington, the city is responsible for all real estate taxes. In addition, the terms of the sublease arrangement between the city and Donohoe exempt Donohoe from paying property taxes on the land and the parking garage facility during the term of the sublease.

We consulted with the AG’s office regarding municipal authority to provide tax exemptions to commercial entities. Per the AG’s

Tax Compliance Matter Referred to Department of Taxes

office, 24 VSA §2741⁴² provides a mechanism for municipalities to enter into tax stabilization contracts that affect the tax liability of certain property owners, including owners of commercial real estate. However, the AG's office was not aware of any tax stabilization agreement that would apply to this property and noted that unless the city has documents to show that the property is tax exempt under this or other state statutes, we should assume that the property is taxable to the owner of record. The city has not provided evidence that it has utilized the tax stabilization mechanism set forth in 24 VSA §2741 to gain the authority to negotiate tax stabilization contracts such as the tax exemptions provided in the lease and sublease agreements.

Payment of Taxes

Although the property summary record shows the property is tax exempt and the property is reported as tax exempt to DOT for purposes of statewide education property taxes, the city assessor maintains that the parking facility property has been taxed as part of the Church Street Mall (the "Mall") property, explaining that the valuation of the Mall incorporates the value of the parking facility located at 75 Cherry Street. However, the city has not provided evidence that the value of the 75 Cherry Street parking facility has been incorporated into the Mall property valuation and therefore subject to property tax.

If DOT concludes that the property has been inappropriately excluded from property taxes, we estimate that the city failed to collect approximately \$947,000⁴³ in property taxes, \$532,000 that should have been paid to the state, \$191,000 that should have been retained by the city, and \$224,000 that should have been used to repay or prefund TIF district debt.

⁴² It requires a two-thirds vote of the city voters to authorize municipalities to contract with commercial entities for the purpose of adjusting property taxes applicable to commercial property. Further, the contract term may not exceed 10 years.

⁴³ This estimate is based on the assessed value listed in the property summary record and tax rates in effect from 1997 to 2010.

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May 9, 2012

CITY OF BURLINGTON, VERMONT
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The Honorable Thomas M. Salmon, CPA
State Auditor
132 State Street
Montpelier, VT 05633-5101

Re: City of Burlington's Response to Office of the State Auditor Draft TIF Report

Dear Mr. Salmon,

The City acknowledges receipt of the draft report prepared by your office entitled "Tax Increment Financing District - City of Burlington Did Not Always Administer Its District According to Statutory Requirements and Owes the State \$1 Million". The City's response to the report's conclusions and recommendations, in short, is that:

- **The City's use of incremental property tax revenue for payment of the 1999 certificates of participation related to the refinancing of the purchase of the Urban Reserve was appropriate and legal.**
- **The City's calculation of municipal incremental property tax substantially complied with legal requirements and the City will work with the State to clarify any remaining ambiguities.**
- **The City does not owe any money to the State.**
- **The City substantially complied with its minimal reporting requirements.**
- **The City was not subject to any performance measure requirements.**

We are disappointed that this 46 page report does not highlight the substantial financial successes for both the City and the State which have been derived from Burlington's Waterfront TIF district. The City utilized Tax Increment Financing to build public infrastructure including the reconstruction of Lake Street, the Lakeview and Westlake public parking garages which enabled private economic development, including renovation and revitalization of the downtown mall, and "anchor projects" (Filene's (now Macy's), the Marriott Hotel, and Hotel Vermont (now under construction). There are now 16 residential condos and 40 residential units of affordable housing along Lake Street. There are now 76 businesses in the district. The Grand List assessed value of the district has tripled. The immediate value to the State of Vermont from this success just in terms of direct dollars via rooms and meals tax, sales tax and payroll taxes comes over time to tens of millions of dollars. The long term value to the State is great, particularly when

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Comment 1

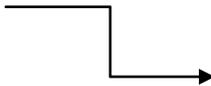
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the district is retired and all the education property tax revenue in the district flows again to the State. The further ripple effect of all these successes on the State economy can not be calculated but is without question worthy of acknowledgement. Failing to highlight these successes reflects a lack of understanding of what the City has accomplished to invigorate the economy, create jobs, build housing and grow the tax base.

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Comment 2



We find the title of your report inflammatory and inappropriate in stating that the City of Burlington owes the State \$1 Million. This statement is incorrect. As discussed in this letter and the accompanying memos, we believe the City’s use of the tax increment has been consistent with applicable law. Even if your conclusion that the district was not always administered correctly is determined to be accurate, the consequence would not be that the City owes the State \$1 million but rather that the City would need to present a new accounting – and in all likelihood the significant prefunding of other TIF debts would be the result. As your report acknowledges, the City was legislatively authorized to reopen it’s Waterfront TIF district for a five year period which runs until 2015. The City could elect to reallocate \$1 million as prefunding for debt payments for other eligible TIF projects in the district. Therefore, we submit the report is inappropriately titled and request that it be re-titled to comport with the format utilized in your earlier reports for Milton and Newport where monetary amounts were not referenced in the titles.¹

With the above being said, we have reviewed the report and its findings, conclusions and recommendations and state the following:

Use of incremental property tax revenue for payment of the 1999 certificates of participation related to the refinancing of the purchase of the Urban Reserve

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The City disagrees with the report’s findings and conclusion that these certificates are ineligible to be repaid with incremental property tax revenue. The City submits that the 1999 Series B Certificates of Participation for the refinancing of the Urban Reserve were legally eligible for the City’s use of incremental property tax funds for the repayment thereof. Attached to this letter and incorporated herein to our official response to this report by this reference is the City’s Memorandum dated February 24, 2012 which presented the City’s legal argument for using incremental property tax revenue for these Certificates of Participation (Exhibit A).

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The City understands that the Attorney General’s office has opined otherwise and that your report has relied on the Attorney General’s opinion. However, reasonable minds can differ, particularly when interpreting financial transactions and statutory provisions and the decisions made attendant to those transactions and decisions 13 years after they were made. With that context, and given the history of the underlying property, the district, the debt, and the history of

¹ “City of Newport Generally Complied With Statutes, But Miscalculated Payments to State” & “Town of Milton Appropriately Established Districts, But Administration Was Flawed”

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interactions between the City and the State relative to this TIF district, the related finding and the recommendation that the City was and should pay the State \$1 million is inappropriate.

The City's position is that:

(1) the State Auditor/Attorney General is reading the statutory definition of improvements too narrowly – particularly given that the City's TIF district predates Act 60 and the State Education Tax and that municipalities were therefore given wide latitude to define what constituted an improvement under the statutes then in place;

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Comment 3

- Your report makes no acknowledgement of the broad, open-ended language which was in effect in 1999 for defining an improvement which could be funded with property tax increment. Indeed your report does not just fail to acknowledge these provisions, it mischaracterizes the definition for improvements. It states in footnote # 5 on page 6 of the report that "[i]mprovements **means** installations, construction, or reconstruction of streets, utilities, parks, playgrounds, land acquisition, parking facilities and other public improvements necessary for carrying out the objectives of the TIF district." The word "means" is restrictive. It establishes that the improvement must fall within the definition provided. All available statutory language when Burlington created its TIF district allowed the municipality to designate what constituted an improvement using provisions in which the definitions for "improvements" indicated examples. The law stated that improvements "shall include" items from a provided list but clearly were not limited to the list.

Comment 4

- As the City was creating its Waterfront TIF district, a 1996 public ballot question passed by Burlington voters explicitly authorized the City to use incremental property tax revenue from the Waterfront TIF district for the refinancing of the urban reserve debt. (Attached hereto as Exhibit B)

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- Your report at page 17 references that "the AG advised that TIF districts are authorized for the purpose of funding expenditures such as acquisition of property that will stimulate development or redevelopment within the TIF district." 24 V.S.A. § 1893 provides broader language to define the purpose of a TIF district, and the City addresses this issue in its attached Memorandum (Exhibit A). The AG and, in turn, your report have read authorizing statutory language too narrowly. Your report states, at page 17, that "[i]f an investment has already occurred as it has in this instance (with the purchase of the land), the creation of a TIF district at a subsequent date does not serve the purpose of motivating the investment." That was simply not true in this case. The City did acquire the property in 1991, but did not have the means to enter into a financial transaction which would secure the property permanently for the City. The City had to twice enter into short-term financial transactions which included options to purchase the land to the Trust for Public Lands and to the Burlington City Employees' Retirement System respectively. The City specifically articulated its intent to refinance the Urban Reserve utilizing TIF revenue in its 1996 Ballot Question concerning the Waterfront because of

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the City's desire to secure the Urban Reserve permanently for the benefit of its citizens, to promote appropriate development and use of the Waterfront TIF district. The alternative would have been to allow the option to be exercised and to relinquish the Urban Reserve land.

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Comment 5

Comment 6

(2) in 2008 the State Legislature retroactively approved Burlington's use of COPs in its Waterfront TIF District under broad language which encompassed all of the COPs previously issued including these for the Urban Reserve:

- The City of Burlington issued Certificates of Participation in reliance on the 1996 public referendum and the 1997 legislation grandfathering Burlington's pre-Act 60 TIF district.
- The Certificates themselves present in their Official Statements the clear history of the City's purchase of, and the subsequent refinancing of this Urban Reserve land, with specific reference to the use of TIF funds for repayment
- These Certificates have always been available for public inspection; including inspection by any State entity that wanted to do its due diligence on Burlington's administration of its Waterfront TIF district since their issuance in 1999 and with respect to the legislative issues addressed in 2008 and subsequent years.
- In 2008, the legislature retroactively authorized all of the City's Certificates of Participation by way of section 72 of Act 190 in order to settle a dispute between the City and the Tax Department over whether Certificates of Participation were legal at all for use in a TIF district.²

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(3) even if the State disagrees with the City's position on defining improvements or retroactive authorization, the State should be estopped from asserting any legal action against the City to collect any funds. The City has openly presented and reported the use of TIF increments to refinance the urban reserve debt to the Tax Department over the years, dating back in this case to the ballot question in 1996 which the City voters passed authorizing the use of TIF increment for refinancing the urban reserve debt.

- The Urban Reserve lands were deeded to the City in 1991 in a public manner, after years of litigation, by way of agreements to which the State of Vermont itself was a party.
- The City has willingly cooperated with all State entities relative to any concern regarding the Waterfront TIF district, including the Tax Department, the Vermont Housing and Conservation Board, the Agency of Commerce and Development and the Joint Fiscal Office.
- In 1999, the City was awarded a \$2.5 million Downtown Board Grant to be utilized for the Burlington Square Mall parking facility over a ten year period by Vermont's Agency of Commerce and Community Development. The parking facility was otherwise

² Indeed, the City submits that the legislature gave such broad retroactive approval to the City's Certificates of Participation that, independent of all other legal analysis, the Urban Reserve Certificates were authorized under the language of that provision. The analysis for this is presented in the above referenced City Memorandum attached to this response letter.

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- substantially financed by the 1999 Series A Certificates of Participation which were issued along with the 1999 Series B COPs which issued for the Urban Reserve.
- On January 10, 2001, the Vermont Agency of Administration and the Department of Taxes issued a report "Tax Increment Finance Districts and Tax Stabilization Agreements (Act 159 of the 2000). Act 159 had specified that "the secretary of administration shall study and report to the house committee on ways and means and the house committee on commerce recommendations concerning the projected long-term effect of tax increment financing and tax stabilization agreements on the education fund." Burlington's Waterfront TIF district was not even referenced in the report.
 - Throughout 2007 and into 2008, the Department of Taxes, while challenging Burlington's right to use Certificates of Participation as debt instruments for tax increment financing, certainly had the opportunity to review the COPs and the City believed the Tax Department knew the purpose for which the COPs were issued.
 - The aforementioned 1996 ballot question has been presented to VEPC, the legislature and the tax department in the past without any questioning of the propriety of using the TIF increments to refinance the urban reserve debt.
 - There is a history of thirteen years of good faith administration of Burlington's Waterfront TIF district in an open and public fashion. The City of Burlington was and is right to rely on the State's support, and/or acquiescence and acceptance of the uses to which the City employed incremental property tax revenues within its Waterfront TIF district.

Calculation of incremental property tax revenue

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The City maintains that its municipal tax increment calculation is and has been correct, and denies that any money is owed to the State by virtue of the manner in which Burlington has calculated its municipal increment. Please accept and incorporate herein the attached City Memorandum dated February 23, 2012 which presents the City's legal analysis relating to its determination of municipal increment (Exhibit C). For the reasons stated in the City's memorandum, Burlington rejects any attempt to impose a proportionality formula based on an application of 32 V.S.A. § 5401(1)(E).

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That said, the issue of calculating Burlington's municipal increment is an incredibly complex matter in which the City will be seeking to work cooperatively with the Tax Department, VEPC, the Legislature and the Attorney General's Office to better understand and clarify the issues involved with respect to new projects and financings. This will need to be resolved as the City begins to move ahead with its new Downtown TIF district. We expect that the issues will be of some significance to calculating municipal increment for other municipalities as well.

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The City does not agree in all particulars with the analysis of the Attorney General and notes that the Attorney General opines that such calculation is difficult to determine given that the legislative intent with respect to these calculations is ambiguous. We are surprised then that

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this report would have us abandon our methodology and accept the Attorney General analysis without further effort to reach a consensus determination as to how to conduct such calculations. We feel that the appropriate course here will be to work cooperatively with any and all relevant State entities (VEPC, Tax Department, AG’s Office) to reach an understanding of how to treat taxes which seem to be specifically dedicated and other ambiguous matters like a county tax or the Chittenden County Transportation Authority tax.

Comment 8

These are matters about which the City made determinations which have never been questioned until now. The City’s methodology is described without objection in the “2009 Tax Increment Financing in Vermont” report issued by the Department of Taxes and Legislative Joint Fiscal Office. The City believes that it would take further legislation or rules in order to completely clarify which components of a municipal tax are in fact permitted and/or required for inclusion/exclusion of a municipal increment calculation. As the Attorney General advised, trying to ascertain the legislative intent to treat certain assessments as special and at the same time give some meaning to the “all taxes” mandate is no easy task and at this point requires further time and effort. The City will work with the various entities of the State needed to clarify these issues and will then proceed in a manner consistent with those clarifications.

City does not owe any money to the State

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Comment 2 

The City disagrees with recommendation # 3 that the City arrange to pay the \$1,000,000 of statewide education increment owed to the State. For all the reasons presented above, and the attached City Memorandums (Exhibits A and C), the City denies owing anything at all to the State. Furthermore, the City objects to a recommendation which is presented as a demand to pay \$1 million dollars to the State. Even if there were a determinative finding that was enforceable against the City that State education tax increment had been misapplied, the City would not be placed in a position of paying these funds to the State. Instead, the City would be placed in a position of conducting a reaccounting of its expenditures.

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The State education property tax moneys which the City has collected from its Waterfront TIF district above the original taxable value of the district were and are and for as long as the district survives available for the City to use for the repayment of TIF eligible debt.³ The point, therefore, is that even if a TIF expenditure were determined to be disallowed, the City would not refund the money to the state but, instead, could and would prefund other TIF eligible debts.

Comment 9

The report trumpets the need to “pay \$1,000,000 of statewide education increment owed to the state” repeatedly. Yet the report acknowledges, albeit only once, and only in passing in the last sentence of its conclusion, that Burlington needs to correct its approach to administering

³ Subject to the provision going forward for the City to make a payment to the education fund in lieu of tax increment which would approximate 25 % of new state education property tax increment resulting from growth within the district subsequent to April 1, 2010 excluding two hotel properties which had already been permitted for construction at that time.

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Comment 8

the Waterfront TIF district, because “[w]ithout such a correction, Burlington could continue to retain property taxes that should be remitted to the state or used to prefund debt repayment.” After finally demonstrating an acknowledgement of prefunding as an available mechanism to the City for state education increment moneys on page 30 of the report, it seems inappropriate to demand payment to the State as the only proffered remedy available to the City (as referenced in the recommendations at the top of page 31 of the report) for any supposed errors which the audit alleges the City committed.

Reporting Requirements

See report section
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It is important to note that most TIF reporting requirements do not apply to the City’s Waterfront TIF district as those requirements were imposed after its creation and implementation. To the extent that there were any reporting requirements which the City failed to adhere to (e.g. the failure to annually certify the assessed value of the Waterfront TIF district to the Burlington City Council), the failure appears to have been more a technical than a substantive omission. The City has always included TIF financial information in its Annual City Reports and the City has regularly kept track of, and made statements to the public, VEPC, the Tax Department and the Legislature, about the growth of the assessed value of the Waterfront TIF district.

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Similarly, with regards to the issue of compliance with the 24 V.S.A. § 1901 requirements adopted by the legislature in 2008, there is some question as to whether this isn’t also an issue of putting form over substance. Because of the Waterfront TIF district’s “grandfathered” status (having been created before Act 60 and not subject to the VEPC approval process), the City and, City believes, VEPC have both operated with an understanding that the VEPC reporting and approval requirements did not apply to the City’s Waterfront TIF district. Nevertheless, the City, VEPC and the Tax Department have maintained an informal and respectful discourse over the years regarding the Waterfront TIF district. The City has never been informed by either VEPC or DOT that it has been anything other than forthcoming and cooperative in providing any and all information requested by either entity.

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That said, the City has no objection to Recommendation # 4 – Designate a city official to be responsible for reviewing the statutory requirements for reporting and to document policies and procedures to ensure timely and accurate reporting. The City will be reaching out to all relevant State entities to ensure that it remains fully compliant with all legal requirements for each of its TIF districts going forward.

Performance Measures

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As a “grandfathered” TIF district, there are no legal requirements for establishing and monitoring a set of performance measures for Burlington’s Waterfront TIF district. With respect to Recommendation # 5: Designate a city official to establish and monitor a set of

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performance measures, including numerical targets for all measures, the City has no objection with respect to its applicability to the new projects and financing in the Waterfront TIF District or the new Downtown TIF district which are subject to all of the various statutory reporting requirements, including performance measures.

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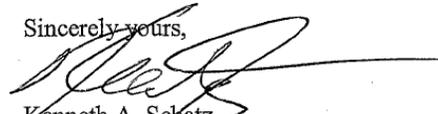
Having said that, we do not understand and disagree with Table 4 that indicates that actuals were not monitored for construction of parking facilities, creation of affordable housing on waterfront, etc. As no formal performance measures were required, the City did not update a formal performance measure document, but City officials can certainly identify the number of additional parking facilities constructed, etc. The City could conceivably work with State entities to produce or reproduce data for measuring the success of the Waterfront TIF district

Conclusion

In summary, the City submits that Burlington's Waterfront TIF district successfully stimulated significant development within the TIF district and provided substantial economic benefits to the City and State. As a grandfathered district, Burlington was in the position of implementing and administering its Waterfront TIF district as the first TIF district in the State of Vermont. Burlington made reasonable legal and administrative decisions and actions and substantially complied with statutory requirements for the establishment and the administration of its Waterfront TIF district. The City acknowledges the efforts the State has made to make TIF laws clearer and administration of TIF districts more understandable and predictable. Legislative amendments over the years have facilitated the process and the City of Burlington has worked hard to participate in and contribute to many of the changes. Municipalities now work closely with VEPC and other State entities to address problems before they arise. Burlington remains committed to continuing to do so.

We hope that the final report by the Auditor will highlight the successes of the Waterfront TIF district. To the extent that there are disagreements or ambiguities regarding requirements for administration of a TIF district, we hope that the focus of the Auditor's report will be recommendations on how to clarify those issues.

Sincerely yours,



Kenneth A. Schatz
City Attorney and Corporation Counsel

cc: Miro Weinberger, Mayor

lb/KAS 2012/Thomas Salmon, State Auditor re Response to TIF Audit

Appendix IV

Reprint of the City of Burlington's Management Response and Our Evaluation

The following table contains our evaluation of remarks made by the Burlington city attorney:

Comment 1.	Our audit objectives primarily focused on compliance with state statute related to establishment and administration of the TIF district. Although we also assessed the extent to which Burlington established performance measures and monitored actual results, our scope did not include validating whether any actual results represented in these performance measures were accurate. However, the background section of our report includes some of the data that the city cites in its response, including the infrastructure improvements related to Lake Street and the Lakeview and Westlake garages, and the number of residential condos and units of affordable housing constructed along Lake Street.
Comment 2.	At various points in its response, the city states that even if our conclusion (the city inappropriately used incremental property tax revenue to pay for Urban Reserve debt) is correct, there are various remedies it could avail itself of such as 1) presenting a new accounting with the result being significant prefunding of other TIF debts (p. 2 of response), 2) conducting a reaccounting of its expenditures (p. 6 of response) or 3) reallocating \$1 million as prefunding for debt payments for other TIF eligible projects (p. 2 of response). However, the city failed to provide specifics or documentary evidence about how a new accounting, reaccounting or reallocation would address their inappropriate use of incremental property tax revenue. The accounting remedies suggested by the city do not appear to be viable options to resolve its \$1 million shortfall in payments to the education fund. The city's records, including its audited financial statements, show that the city used \$1.2 million of tax increment to pay for the Urban Reserve debt and the balance in the account that the city uses to account for TIF district activity is \$277,000 at June 30, 2010. The city's transactions cannot be rolled back merely by altering the accounting for the transactions. It seems doubtful that presenting a new accounting or a reaccounting of its expenditures would enable the city to show that it in fact has \$1.5 million in its TIF account, as if it did not use \$1.2 million to pay for the Urban Reserve debt.
Comment 3.	We disagree that our report mischaracterizes the definition of improvements since the findings section of our report, specifically footnote 12 on page 17, notes that improvements "include" land acquisition and construction of streets and utilities. However, as the city points out, we used "means" rather than "includes" in footnote 5 in the background section of the report to describe types of eligible TIF district improvements. We have amended footnote 5 to remove the term "means" and replaced it with "includes." Nonetheless, our conclusion regarding the Urban Reserve debt remains the same. We consulted with the AG's office and the AG advised that the

Reprint of the City of Burlington's Management Response and Our Evaluation

	refinancing of the Urban Reserve debt was not an improvement since it is the original debt that facilitated the acquisition of this property in 1991 that is the relevant debt to measure against the statutorily allowed borrowing period (April 1, 1996 through March 31, 2006).
Comment 4.	According to advice of the AG's office, Burlington voters may not provide authorization to the city to use incremental property tax revenue in a manner that contradicts eligible uses specified in state statute. Since the AG also advised that the repayment of the Urban Reserve debt is not an eligible use of incremental property tax revenue, we concluded that the authorization by Burlington voters does not usurp state law.
Comment 5.	The 1997 legislation that the city states it relied upon when it issued its COPs does not address allowable TIF financing mechanisms, rather it allowed for the expansion of the boundaries of Burlington's TIF district and allowed Burlington's TIF district to continue post-Act 60. At the time of the passage of this Act, the TIF statutes that governed the types of debt authorized for TIF districts only allowed for general obligation and revenue bonds, so it is not clear how the city's reliance on the 1997 legislation related to its issuance of COPs at all.
Comment 6.	The city asserts that the official statement of the 1999 COPs presents the clear history of the city's purchase and subsequent refinancing of the Urban Reserve land, with specific references to the use of TIF funds for repayment, however the city does not state that it provided this information to the legislature, so it is not clear how this supports their contention that the legislature has specifically approved the 1999 COPs. Further, during its 2008 legislative testimony to the Senate Finance Committee, the city did not mention the Urban Reserve 1999 certificates of participation.
Comment 7.	The 2001 report issued by the Agency of Administration and DOT was responsive to two sections of Act 159 (2000), 17 and 39. Section 17 required the Secretary of the Agency of Administration to make recommendations concerning the long-term effect of tax increment financing and tax stabilization agreements on the education fund. Section 39 required the secretary of the Agency of Administration, commissioner of Taxes and commissioner of Housing and Community Affairs to provide recommendations for the replacement of foregone revenues as a result of the Winooski redevelopment project and similar projects and to propose criteria and a process to formalize an application process for municipalities to submit TIF district proposals. This was a policy report and individual TIF districts, except for an issue related to Winooski, were not the subject of the report.
Comment 8.	The city states that its determination on how to treat its municipal tax rates in the calculation of incremental property tax revenue has not been questioned until now and that disclosure of its methodology in the joint DOT/JFO 2009 tax increment financing report did not

Appendix IV

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	<p>generate objections. While we agree that the methodology is described in a footnote to Table 1 in the 2009 report, we believe that the city appears to ascribe greater weight to this disclosure as if it represents DOT's and JFO's scrutiny and approval. In fact, this same legislation that required the 2009 report (Act 190) added the requirement for the auditor's office to audit all active TIF districts. This seems to distinguish the legislature's request for certain data about the TIF districts (limited review by DOT/JFO) from their desire for scrutiny of the appropriateness of the active TIF districts' operations (audit conducted by State Auditor's Office).</p>
Comment 9.	<p>We have clarified the last sentence of our report and removed the reference to prefunding since our point was to indicate the continuing effect of Burlington's ineligible use of tax increment - to the extent the city continues to use tax increment for ineligible purposes, it will continue to retain statewide education increment that should be paid to the state.</p>

Appendix V

Reprint of the City of Burlington's Exhibits to Its Management Response

Page 18 of the report contains our disagreement with some of the facts presented in this memo.



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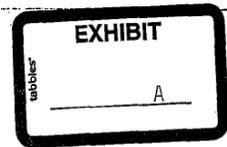
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MEMO - Confidential

TO: Jeffrey Kellar, Audit Supervisor, Office of the Vermont State Auditor.
Tanya Morehouse, Chief Auditor, Office of the Vermont State Auditor

FROM: Richard Haesler, Assistant City Attorney, City of Burlington, Vermont

RE: Response to 12/12/11 Attorney General Opinion re Tax Increment Financing Districts - Refinanced Debt

DATE: February 24, 2012

This is a memorandum to address the preliminary position articulated by the Office of the Vermont State Auditor with regard to the of City of Burlington's inclusion amongst the debt instruments used in its Waterfront TIF district of the Series 1999B Certificates of Participation (COP) issued in 1999 relative to the financing of Burlington's Urban Reserve land within its Waterfront TIF District.

Specifically, Burlington was informed via email on January 18, 2012 that the State Auditor's Office will be relying on an Attorney General (AG) opinion issued on December 12, 2011 which proffers the opinion that the above referenced debt should be characterized as a refinancing of original debt under circumstances such that these COPs "may not be paid with incremental property tax revenue."

Burlington submits that its Series 1999B COPs relative to the financing of Burlington's Urban Reserve land within its Waterfront TIF District are properly being paid with incremental property tax revenue for three (3) reasons: (1) The Legislature's retroactive approval of Burlington's COPs encompassed the circumstances of the Series 1999B COPS, (2) Burlington has openly held out its refinancing of the urban reserve as a TIF debt for 13 years and the State of Vermont has known and not objected to its inclusion as a TIF debt such that Burlington has effectively relied on State acceptance of said inclusion,

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and (3) the ballot referendum passed by the voters of Burlington authorized the inclusion of what ultimately was determined to be the Series 1999B COPs as a TIF debt under circumstances such that Burlington's refinancing of the urban reserve lands constituted an "improvement" as statutorily defined and permitted at the time that the debt was incurred.

First and foremost, Burlington's position is that it has already resolved State concerns regarding its use of these instruments. Specifically, in 2008, the State Tax Department disputed Burlington's use of COPs as debt instruments for improvements within its Waterfront TIF district. The Tax Department maintained that subchapter 5 of Chapter 53 of Title 24 only permitted the use of bonds which pledged the full faith and credit of the municipality. Burlington disagreed. Burlington had at that point been very public about its use of COPs for nearly ten years. In order to resolve the dispute, the legislature passed within Act 190:

Sec. 72. RETROACTIVE APPROVAL OF BURLINGTON TIF FINANCING

Municipalities that expanded tax increment financing districts under subchapter 5 of chapter 53 of Title 24 by June 30, 1997, as authorized by No. 60 of the Acts of 1997, shall have authority to apply those state and local property taxes assessed on properties within the tax increment financing district to repayment of certificates of participation and HUD Section 108 financing issued to finance public improvements within the tax increment financing district. This authority is retroactive to June 30, 1997, and is applicable to certificates of participation and HUD Section 108 financing instruments issued after April 1, 1996, and on or before March 31, 2006. State education property taxes may be used in accordance with this provision for a period of no more than 20 years from the date the debt was incurred. Refinancing such debt shall not extend the 20-year period for any portion of the debt.

The language of this retroactive approval is clear. Consequently, Burlington's Series 1999B COPs are clearly authorized retroactively by this approval because:

- (a) Burlington is a Municipality that expanded its tax increment financing district under subchapter 5 of chapter 53 of Title 24 before June 30, 1997, as authorized by No. 60 of the Acts of 1997.
- (b) Burlington has applied those state and local property taxes assessed on properties within the tax increment financing district to repayment of certificates of participation issued to finance public improvements within the tax increment financing district. (Note that this authorization does not indicate any requirement that the COPs be issued to finance improvements pursuant to the any specific provisions of law separate and aside from the fact that the district itself was expanded pursuant to the provision referenced above).

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(c) The Series 1999B COPs were issued by the City of Burlington for the acquisition of land (Urban Reserve) which is wholly or partly within its Waterfront TIF District, which acquisition constitutes an "improvement." See 24 V.S.A. § 1891.

(d) The specific language of 24 V.S.A. § 1891 at the time of the creation of Burlington's Waterfront TIF District reads as follows:

"(3) "Improvements" shall include its ordinary signification, such as installations, construction, or reconstruction of streets, utilities, parks, playgrounds, land acquisition, parking facilities and other public improvements necessary for carrying out the objectives of this chapter."

(e) The Series 1999B COPs were issued in 1999 which is "after April 1, 1996, and on or before March 31, 2006."

(f) Burlington will be using State education property taxes in accordance with this provision for a period of no more than 20 years from the date the debt was incurred.

Burlington's Series 1999B COPs for the urban reserve have satisfied each and every element required by this authorization. Burlington submits that this authorization is clear and unambiguous and dispositive of the issue. Furthermore, Burlington submits that this authorization is supported by all of the circumstances under which it was given. The State Tax Department, in reviewing the administration of Burlington Waterfront TIF district had concerns that COPs were not authorized debt instruments for use within a TIF district. Burlington's portfolio of Waterfront TIF debt instruments was made fully available first to the Tax Department during its inquiry, and then to the legislature during the legislative session leading up to the passage of Act 190. Burlington maintained then and maintains to this day that debt instruments other than bonds requiring a pledge of the full faith and credit of the city were permissible for it to use as TIF debt instruments based on the existing statutory authority at the time of the creation of Burlington's Waterfront TIF district in 1996. That issue is not relevant to this memorandum, but the circumstances of the passage of ACT 190 are relevant because, similar to the issues of apportionment of the state and municipal increment, they provide another example of Burlington openly presenting the administration of its Waterfront TIF district to governmental entities of the State of Vermont, and then, years later, having another governmental entity of the State of Vermont, the State Auditors office re-examine aspects of Burlington's administration of its district and reach a conclusion that errors were made. This re-examination has come years after Burlington has been conducting its affairs; i.e. servicing this debt, under certain interpretations of statutory provisions with a reasonable understanding that all relevant information concerning same has been provided to relevant governmental entities of the State of Vermont who have either agreed with Burlington's interpretations or, at the very least, raised no objection.

The Burlington City Council created the Waterfront TIF District on January 22, 1996. On that same date the Burlington City Council passed a resolution authorizing the placement on the ballot of the 1996 Annual City Meeting a Referendum for voter consideration of the following question:

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"Shall the City Council be authorized to use **HUD Section 108 financing or another equivalent financing source** for waterfront revitalization projects pursuant to the Waterfront Urban Renewal Plan, including but not limited to Lake Street reconstruction, Moran Plant redevelopment, Lake Champlain Basin Science Center improvements, waterfront/Downtown linkages and **retirement and/or refinancing of the urban reserve debt**; it being understood that **tax increments received from properties within the waterfront tax increment financing district shall be pledged and appropriated** for the payment of principal and interest on any bonds or notes issued for the purpose of accomplishing such waterfront revitalization projects?"

The question passed by a vote of 4,311 to 3,152. This happened before Act 60. At that point in time, no governmental entity of the State of Vermont had a stake in Burlington's TIF district. In this referendum, the relevant stakeholders in Burlington's TIF district expressly authorized Burlington's City Council to refinance the urban reserve debt using appropriate financing which would then be repaid with tax increments from the TIF district. This vote was, put simply, Burlington's citizens' determination that "refinancing" the urban reserve debt constituted an "improvement" consistent with the purpose of accomplishing waterfront revitalization projects and consistent with the purpose of Burlington's TIF district.

There certainly were many justifiable reasons for them to make that determination. The history of transactions relative to Burlington's urban reserve supports the decision:

- (1) On September 6, 1991, Burlington executed a Purchase and Sale contract with the Trust for Public Land (TPL) providing that TPL would deposit \$820,000.00 with Burlington to help Burlington fund the purchase of approximately 45 acres of waterfront property (i.e. urban reserve lands) from the Central Vermont Railway.
- (2) The Purchase and Sale contract with TPL also provided that TPL had the right, upon payment of an additional \$328,000.00 to Burlington to take title to a specific portion amounting to approximately 25 acres of the 45 acre site, unless Burlington paid TPL the sum of \$1,148,000.00 on or before October 15, 1993 to extinguish TPL's interest in the property.
- (3) In October, 1993, the Burlington City Employees Retirement System entered into a Purchase and Sale contract with Burlington, substituting itself for TPL as the holder of an option to purchase the approximately 25 acres of urban reserve lands. The option was structure to last for five (5) years.
- (4) On December 7, 1998, the Burlington City Council authorized issuance of \$1,390,000.00 of Certificates of Participation, 1999 Series B, for the purposes of refinancing the acquisition of "approximately 45 acres of waterfront property in the City which was acquired from the Central Vermont Railroad." That refinancing extinguished all existing options on the property, thereby removing another entity's (the Burlington City Employees Retirement System) legal interest in the property. The removal of said option, which was potentially both imminent and viable, constituted and "improvement" that was being made to Burlington's

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waterfront, consistent with its Waterfront Urban Renewal Plan, the purposes of its Waterfront TIF district and consistent with the 1996 voter referendum.

Burlington submits that the AG opinion dated December 12, 2011 from the Vermont Attorney General's Office takes an improperly narrow reading of the definition of "improvements" when it determines that the relevant "improvement" relative to Burlington's 1999 refinancing of its urban-reserve-lands was the original Purchase and Sale contract with the Option Agreement entered into with TPL in 1991. The AG opinion gives minimal analysis to the definition of "improvements". It states in its opinion at page 2 that "[t]he term 'improvements' is broadly defined to include 'land acquisition,' 24 V.S.A. § 1891." The AG opinion then determines that the "relevant debt in this instance was the 1991 loan from the Trust for Public Land to Burlington in 1991, and not the refinancing of that loan through the issuance of Certificates of Participation in 1999. The Certificates simply refinanced the original debt that was incurred to purchase the 'improvement' in question."

Burlington takes issue with this analysis because the definitions for "improvements" is substantially broader than presented by this opinion. Where the AG opinion cites only 24 V.S.A. § 1891, the latitude given to municipals whose TIF districts were "grandfathered" by Act 60 was, in fact, enormous. The AG opinion cites 24 V.S.A. § 1891, which was presented above, but is repeated again here with emphasis added:

"(3) 'Improvements' shall include its ordinary signification, such as installations, construction, or reconstruction of streets, utilities, parks, playgrounds, land acquisition, parking facilities and other public improvements necessary for carrying out the objectives of this chapter."

The first point of emphasis is that the definition was not limiting "improvements" to only the specific items named in the provision. Implicit in the words "shall include" is the concept that the named items cannot be excluded but that additional items are possible for inclusion. In fact, the definition was substantially supplemented by the definition provision for the chapter as a whole (Chapter 53 of Title 24); see 24 V.S.A. § 1751 (3):

"Improvement," as used in this chapter, shall include, apart from its ordinary signification, the acquiring of land for municipal purposes, the construction of, extension of, additions to, or remodeling of buildings or other improvements thereto, also furnishings, equipment or apparatus to be used for or in connection with any existing or new improvement, work, department or other corporate purpose, and also shall include the purchase, or acquisition of other capital assets, including licenses and permits, in connection with any existing or new improvement benefiting the municipal corporation, and all costs incurred by the municipality in connection with the construction or acquisition of the improvement and the financing thereof, including without limitation capitalized interest, underwriters discount, the funding of reserves and the payment of contributions to establish eligibility and participation with respect to loans made from any state revolving fund, to the extent such payment is consistent with federal law."

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Again, the words "shall include" appear and, again, implicit in the words "shall include" is the concept that the named items cannot be excluded but that additional items are possible for inclusion.

Ordinary signification for the word "improvement" is presented in Webster's New Collegiate Dictionary, G. & C. Merriam Company, Springfield, Massachusetts (1981), as:

"*N* : 1 : the act or process of improving. 2 *a* : the state of being improved; *esp* : enhanced value or excellence *b* : an instance of such improvement : something that enhances value or excellence"

Finally, it is important to note the broad, supportive and encouraging language of the "Purpose" provision of the original TIF statutes, 24 V.S.A. §1893 – Purpose, which read as follows:

"The purpose of tax increment financing districts shall be to provide revenues for improvements located wholly or partly within the district which will encourage development, provide for employment opportunities, improve and broaden the tax base, or enhance the general economy of the municipality, the region, or the state."

The language is encouraging municipalities to creatively utilize the generated revenues to accomplish broadly defined economic goals. Burlington in retiring a short-term loan with an option to 25 acres made a decision in 1999 to, in part, finance its 1991 acquisition of waterfront public trust lands, through the issuance of COPs in the amount of \$1,390,000 wherein the land itself served as the collateral for the Certificates and the debt could be retired utilizing TIF revenues. This financing was done for the express purpose of accomplishing the purposes as set out in 24 V.S.A. § 1893 and helped to allow Burlington to develop its Waterfront as evidenced today.

It should also be noted that the Vermont state legislature has since narrowed the definition of "improvements" for purposes of limiting exactly what may constitute an "improvement" eligible for inclusion in TIF eligibility. See 24 V.S.A. § 1891 as it now read as a result of amendments made in 2005 (and therefore do not apply to these Burlington 1999 Series B COPs):

"Definitions.

When used in this subchapter:

(4) "Improvements" means the installation, new construction, or reconstruction of streets, utilities, and other infrastructure needed for transportation, telecommunications, wastewater treatment, and water supply, parks, playgrounds, land acquisition, parking facilities, brownfield remediation, and other public improvements necessary for carrying out the objectives of this chapter.

The reference to "other public improvements" can and should be read to allow still for a broad reading of what constitutes a public improvement, but it should be noted that the TIF districts to which this language applies are subject to VEPC approvals and therefore

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the determination as to what constitutes an "improvement" for inclusion in the TIF of a district becomes part of the VEPC approval process.

Because Burlington's Waterfront TIF district predates Act 60, and was not subject to VEPC approval, the power to make reasonable judgments and determinations as to what constituted an "improvement" for inclusion in Burlington's TIF resided with Burlington itself and was accomplished in its 1996 ballot referendum approved by its voters as outlined above.

For all of the above reasons, Burlington submits that its Series 1999B COPs relative to the financing of Burlington's Urban Reserve land within its Waterfront TIF District are properly being paid with incremental property tax revenue.

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3-3-96

ANNUAL CITY MEETING	
INSTRUCTIONS TO VOTER TO VOTE, completely fill in the OVAL to the RIGHT of your choice(s), like this: <input type="radio"/>	
<p>CHARTER CHANGE — CREATION OF DEDICATED SCHOOL TAX FOR TECHNOLOGY IMPROVEMENTS</p> <p>1. Shall Section 102C be added to the City Charter to permit an annual assessment not exceeding two cents upon the dollar of the property grand list for technology improvements to the Burlington school system?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>CHARTER CHANGE — REAL ESTATE TAX ASSESSMENT AND APPEAL PROCESS</p> <p>7. Shall the City Charter be amended to provide that the City Assessor shall be the Chair of the Board of Assessors which shall continue to determine valuation of properties for real estate tax purposes and that appeals from the Board of Assessors be to a new Tax Appeals Board rather than to the Board of Civil Authority; that further appeals to the Board of Civil Authority be at the discretion of such board; that the Tax Appeals Board be given power to inspect property and to demand the production of appropriate records; and that the consideration of appeals by the Tax Appeals Board be completed by December 31 of each year?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>BOND FOR SCHOOL CAPITAL IMPROVEMENTS AUTHORIZED</p> <p>2. Shall the City Council be authorized to issue general obligation bonds or notes in an amount not to exceed Four Million Two Hundred Thousand (\$4,200,000.00) Dollars for the purpose of making capital additions and improvements to the City's school system?</p> <p>Total Estimated Project Cost: \$4,200,000.00 Estimated City's Share: \$2,940,000.00</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>CHARTER CHANGE — CHANGE IN CITY MEETING DATE</p> <p>8. Shall Sections 3 and 4 of the City Charter be amended to change the date of the Annual City Meeting from the first Tuesday in March to the third Tuesday in May beginning in 1997?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>CHARTER CHANGE — LOCAL REGULATION OF RATES AND CHARGES FOR SERVICES PROVIDED BY THE BURLINGTON ELECTRIC DEPARTMENT</p> <p>3. Shall Section 4d. of the related laws to the City Charter be amended to transfer from the Vermont Public Service Board to the Burlington Electric Commission, subject to veto by the City Council with Mayor presiding, the responsibility for setting the rates and charges of the Electric Department; to permit the Electric Commission to consider the financial circumstances of low income customers when setting such rates and charges; to authorize the Electric Commission and the City Council to employ necessary staff and consultants and to exempt the Electric Department from that portion of the utility gross receipts tax related to the regulation of rates and charges?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>CHARTER CHANGE — REFERENDUM APPROVAL REQUIRED FOR FRANCHISE FEE AMENDMENTS</p> <p>9. Shall Section 48XL of the City Charter be amended to provide that the City Council shall not have the authority to increase the amount of any franchise fee without first receiving approval from a majority of the City voters at an annual or special election called for this purpose?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>CHARTER CHANGE — LOCAL REGULATION OF SPECIAL CONTRACTS AND POWER PURCHASE CONTRACTS ENTERED INTO BY BURLINGTON ELECTRIC DEPARTMENT</p> <p>4. Shall Sections 4d. (c) and 7 of Article 4 of the related laws to the City Charter be amended to transfer from the Vermont Public Service Board to the Board of Electric Commissioners the responsibility for approving contracts by the Electric Department for the wholesale purchase of power and energy and for approving special contracts with its customers for the sale of power and energy?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>CHARTER CHANGE — FEE FOR FILING AND CERTIFIED COPIES OF RECORDS</p> <p>10. Shall Section 140 of the City Charter be amended to provide funding for the preservation and restoration of the City's official records by adding a charge of up to \$1.00 to the cost of filing land records and/or obtaining certified copies of records?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>CHARTER CHANGE — CLARIFICATION OF BURLINGTON ELECTRIC DEPARTMENT ENABLING AUTHORITY</p> <p>5. Shall Section 1(d) of Article 4 of the related laws to the City Charter be amended to authorize the Electric Department to own, operate and utilize cable television, fiber optic cable and other telecommunications applications?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>CHARTER CHANGE — VETO POWER OF THE MAYOR</p> <p>11. Shall Sections 46 and 47 of the City Charter be amended to provide that a mayor's veto of any ordinance, by-law, resolution or other vote of the City Council must be made at the next meeting of the Council, provided that the mayor shall not have less than two weeks to consider such ordinance, by-law, resolution or vote and that if no veto is made at that time, the same shall become valid without the mayor's approval, rather than allowing the mayor to wait to exercise a veto until the next regular meeting of the Council usually held on the first Monday of the month?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>REFERENDUM — HUD SECTION 108 AND TAX INCREMENT FINANCING FOR WATERFRONT REVITALIZATION PROJECTS</p> <p>6. Shall the City Council be authorized to use HUD Section 108 financing or another equivalent financing source for waterfront revitalization projects pursuant to the Waterfront Urban Renewal Plan, including but not limited to Lake Street reconstruction, Moran Plant redevelopment, Lake Champlain Basin Science Center improvements, Waterfront/Downtown linkages and retirement and/or refinancing of the urban reserve debt, it being understood that tax increments received from properties within the waterfront tax increment financing district shall be pledged and appropriated for the payment of principal and interest on any bonds or notes issued for the purpose of accomplishing such waterfront revitalization projects?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>	<p>REFERENDUM — AUTHORIZATION OF EXPENDITURE FOR BURLINGTON TECHNICAL CENTER CAPITAL IMPROVEMENTS</p> <p>12. Shall the expenditure of \$360,000.00 for the purpose of making capital improvements to the Burlington School Department Technical Center be authorized, but subject to the limitation that no commitment may be made for the expenditure of such funds by the Board of School Commissioners without first receiving written verification that 100% of such expenditure shall be reimbursed by the State of Vermont?</p> <p>YES <input type="radio"/></p> <p>NO <input type="radio"/></p>
<p>NOTICE TO VOTER: VOTE BOTH SIDES OF BALLOT</p>	

EXHIBIT

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3150

Appendix V

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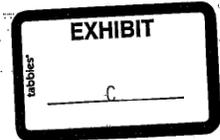
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MEMO - Confidential

TO: Jeffrey Keller, Audit Supervisor, Office of the Vermont State Auditor
Tanya Morehouse, Chief Auditor, Office of the Vermont State Auditor

FROM: Richard Haesler, Assistant City Attorney, City of Burlington, Vermont

RE: Response to 10/4/11 Attorney General Opinion re Apportionment of State
and Municipal Increment

DATE: February 23, 2012

Introduction

This memorandum addresses the preliminary position articulated by the State Auditor's Office with regard to utilization of state education property tax increment ("state increment") and municipal tax increment ("municipal increment") for the repayment of debt in connection with the City of Burlington's Waterfront Tax Increment Financing ("TIF") district. In response to your request, this is a confidential document pending the finalization of your report. The City of Burlington ("Burlington") was informed via email on January 18, 2012 that it is the position of the State Auditor's Office that "[i]f all of the incremental property tax revenue is not used for repayment or prefunding TIF district debt, then a portion of the statewide education increment is owed to the state. The relevant statute cited by the AG is 32 VSA § 5401(10)(E). This impacts Burlington as not all of the municipal increment was utilized to repay or prefund TIF district debt."

The State Auditor, in arriving at this position, relied on an opinion issued by the Office of the Attorney General ("AG") on October 4, 2011. This October 2011 opinion was issued

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in response to a request for legal advice from the State Auditor's Office concerning "whether the TIF statutes allow municipalities (and specifically, the Town of Milton) to carve up incremental tax revenue into two components, municipal and state education property tax revenue, and determine how much of each component may be used for repayment of debt in connection with a TIF district."

Simply put, Burlington submits that it has unique status as a "grandfathered" TIF district municipality under the provisions of Act 60 that allowed Burlington great autonomy in administering its TIF district. This substantially distinguishes Burlington from Milton. For example, no VEPC approval requirements apply to Burlington. Burlington has administered its Waterfront TIF district openly and presented evidence to both the State Tax Department and the Legislature of its apportionment of municipal and state increments. Burlington has serviced its TIF debt for thirteen years in reliance of its interpretation of the applicable TIF provisions and its justifiable reliance on the fact that no State governmental entity objected to Burlington's methodology regarding apportionment of increment. Burlington further submits that it was appropriate for it to set aside dedicated, non-discretionary funds from its municipal increment calculation and regard subsequent pledge and appropriation of the resulting increment totals as appropriate utilization of both state and municipal increment. Alternatively, Burlington submits that even using the AG opinion analysis that interprets Burlington municipal increment as a use of less than 100 % of its municipal increment by such percentage as is comprised of the excluded funds, Burlington was not subject to exact proportionality requirements in its use if its municipal and state increments and was in complete compliance with the relevant statutory provisions to which it was subject.

This memorandum will set out the analysis in support of Burlington's legal position with regard to its apportionment of municipal increment under each of the alternative scenarios. In so doing, Burlington will be submitting that (a) there are issues of analysis in the AG's Milton opinion which should be reconsidered; (b) there are conclusions made in the AG's Milton opinion which should be reconsidered; and (c) there are facts and circumstances in how Burlington has utilized its municipal increment and its state increment which are distinguishable from the facts and circumstances in Milton and consideration of these facts and circumstances should, likewise, result in reconsidered conclusions. It is the hope and desire of the City of Burlington to work with the State Auditor's Office to address and resolve these issues in advance of any public report.

What Burlington Did

In January 1996, Burlington's City Council approved the creation of the Waterfront TIF District. The District was established pursuant to the version of the TIF legislative authority then in place, 24 V.S.A. § 1897, which allowed a municipality "to pledge and appropriate **any part or all** [emphasis added] of the tax increments received from the properties contained within the tax increment financing district..."

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The use of this authority by Burlington was 'grandfathered' and specifically affirmed by the Legislature when it passed Act 60 of 1997. See then 32 V.S.A. § 5404a(c) which read:

Municipalities which have existing tax increment financing districts under subchapter 5 of chapter 53 of Title 24 shall have the authority to expand those districts by June 30, 1997, but not thereafter, and to collect all state and local property taxes on properties within the tax increment financing district and apply those revenues to repayment of debt issued to finance improvements within the tax increment financing district.

(Act No. 60, 1997, § 45)

Burlington did in fact avail itself of the opportunity to expand its district under this provision in June 1997, thereby expanding to the boundaries which remain in place presently.

Burlington began to incur debt within its district in 1999 (See: Section 108 Loan for Lake Street; Certificates of Participation (COPs) for the Lakeview Garage; and COPs for the Urban Reserve). In 2000 additional debt was incurred by way of further COPS issued for the Fishing Pier project. Around this time, the district began to produce tax increment. For Burlington, based on its 'grandfathered status', the original version (1985) of, 24 V.S.A. §1896 provided for a calculation of increment by the following methodology (which is simply an enumerated recitation of the provision's component parts):

- (1) The lister or assessor shall include no more than the original taxable value of such real property in the assessed valuation upon which he computes the rates of all taxes levied by the municipality, the school district and every other taxing district in which the tax increment financing district is situated.
- (2) He shall extend all such rates so determined against the entire assessed valuation of such real property for that year.
- (3) In each year for which the assessed valuation exceeds the original taxable value, the municipality treasurer shall hold apart, rather than remit to the taxing districts, that proportion of all taxes paid that year on the real property in the district which such excess bears to the total assessed valuation.
- (4) The amount so held apart each year is referred to in this act as the "tax increment" for that year.

With that as the framework for defining increment, the legislative body of the municipality could pledge and appropriate any part or all of the tax increments received. It appears that Burlington made various annual determinations during the initial years of the district as to what portions of the municipal increment would be pledged and appropriated to the repayment of TIF debt, but by 2002, Burlington settled on a methodology whereby the municipal increment was comprised of the following accounts: General City, Highway, Police/Fire, Parks & Streets.

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Burlington's Legal Basis for its Method

Despite this broad discretion authorized by the statute, Burlington utilized as much increment, both state and municipal, as it could because in many years the cost to service its TIF debt exceeded available increment and Burlington had to utilize General Fund monies in order to meet the financial responsibilities attendant to its Waterfront TIF debts.

Burlington reached its determination as to which funds were permissible and appropriate for inclusion in its municipal increment after identifying that certain funds were dedicated and non-discretionary taxes with no nexus to TIF debt and determining that such funds were not appropriate sources for TIF debt reimbursement.¹

Basically Burlington's analysis was that taxpayers can and should expect that, upon the various authorizations attendant to creating a TIF district and incurring debt within that district, municipal tax dollars will be appropriated for the repayment of said debt. There seemed to be no basis, however, for including certain types of assessments. The CCTA (Chittenden County Transportation Authority) tax, for example, was clearly an assessment dedicated to a precise use. Given 24 V.S.A. § 1897's language that a municipality could pledge any part or all of available increment, Burlington made a determination not to include this part of the available increment. Burlington made this type of determination for several taxes and ultimately determined that a distinction needed to be made where a tax was dedicated and non-discretionary and used for a purpose or a department which had no nexus to the Waterfront TIF District or the improvements to that District (aside, obviously, from the fact that they are all related to the City of Burlington). With that understanding, Burlington has excluded CCTA, County Tax, Retirement, Debt Service, Library, Open Space & Housing Trust funds from its municipal increment. This analysis and documents in support thereof was provided to the State Auditor's Office in Burlington's October 6, 2011 memorandum on municipal increment calculation, and is included here again as an attachment to this document.

Burlington's first line of argument regarding apportionment of its municipal increment is that Burlington takes the legal position that it uses all of its available municipal increment. Burlington can find no legal basis for it to access dedicated, non-discretionary

¹ For example, the CCTA tax levied against all towns within the County did not seem to Burlington to be a tax which could or should be utilized for repayment of TIF debt. Under 24 V.S.A. § 5108, each year, the treasurer of the Chittenden County Transportation Authority, utilizing the statutorily prescribed formula for apportionment, presents the City of Burlington with its annual CCTA assessment and the statute directs that the City of Burlington "shall add such assessment to its own budget and shall assess such tax as is necessary to raise the amount of the assessment." Burlington has maintained and continues to maintain that to assess the CCTA tax on all properties but then hold apart a portion of that assessment as a permissible taking for TIF increment is simply inappropriate and, Burlington submits, possibly not legal. Discretionary taxes provide the requisite discretion. Use of state increment is authorized by statute. Burlington here questions whether it has any legal authority to access dedicated tax funds for any purpose other than that for which the dedication authorized.

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funds for any purposes other than as provided within the City Charter and other authorizations (see City's October 6, 2011 memo attached). Therefore, the City calculates increment based on available funds and has annually pledged and appropriated that full calculation as municipal increment:

~~Alternatively, Burlington maintains that even under an interpretation that would require Burlington to include even those dedicated, non-discretionary funds in its municipal increment calculation, Burlington has still, nevertheless, complied with all statutory requirements relative to its apportionment of the municipal and state increments.~~

The analysis of how that compliance has been accomplished is set forth in turn through out the remainder of this memorandum. However, preliminary to that analysis and by way of concluding this section of this memorandum concerning the legal basis for these calculations in the alternative, Burlington references that early discussions with the State Auditor's Office regarding proportionality focused on the provisions of 24 V.S.A. § 1900. The pre-Act 60 version of 24 V.S.A. § 1900 to which Burlington is subject may look at first impression as though it requires proportionality but Burlington maintains that it does not. The language of that provision provides no role for the state education tax fund, nor for VEPC, nor for any entity of the State. It reads:

Any tax increment received which in any tax year exceeds the amount pledged for the payment on principal and interest on the bonds issued for improvements in the district shall be distributed to the city, town or village budget and school district budget, in proportion that each budget bears to the combined total of both budgets unless otherwise negotiated by the city, town or village and school district.

In practical terms, for purposes of addressing § 1900, when Burlington does not include certain funds in its TIF increment calculation, those funds, to the extent they can be considered potential increment², become "tax increment received in a year not pledged or appropriated" and, by not having taken those funds for increment calculation, those potential increment monies are, in fact, excess increment which has been "distributed" not "in proportion that each budget bears to combined total[s]" but "as otherwise negotiated" by the city and its school district. This "negotiated" distribution occurs annually when the City budget and the school budget is put forward and subsequently passed within the City of Burlington. Burlington submits that the State did not have a seat at this distribution of excess increment table until, during the legislative process pursuant to Act 54 of 2009 when Burlington was authorized to reopen its Waterfront TIF district for an additional five (5) year period, Burlington agreed that at the close of the

² This is actually a whole other issue which Burlington will need to work out with VEPC relative to Burlington's new Downtown TIF District. The aforementioned analysis around fund which are dedicated and non-discretionary will be part of the conversation with VEPC in order to determine how to apportion Burlington's municipal increment within that district. Interestingly, it appears that VEPC and municipalities subject to the 2007 amendments actually have considerable discretion with how to apportion which could well accommodate Burlington's needs here despite the characterization by the Attorney General opinion that these requirements demand strict proportionality between all funds.

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district's life it would release any excess increment attributable to state education tax increment to the State Education Tax Fund.

What the Auditor Claims Burlington Did Wrong

It is unclear whether the State Auditor is suggesting that Burlington is subject to the 2008 amendments, including most significantly 24 V.S.A. § 1897 (2007, Adj. Sess., No. 190) as referenced in the Attorney General's Milton opinion. Clearly, however, Burlington is not. § 102(14) of that Act provides: "[t]he provisions of Sec. 58 of this act pertaining to proportional use of education and municipal tax in TIF financing shall apply to tax increment financing districts approved pursuant to 32 V.S.A. § 5404a." Burlington's Waterfront TIF District was not "approved" pursuant to 32 V.S.A. § 5404a. Burlington's TIF pre-existed the adoption of 32 V.S.A. § 5404a and the approval provisions referencing VEPC approvals do not apply to Burlington.

Because the 2008 amendments do not apply to Burlington, the entire issue of Burlington's use apportionment of state and municipal increment should not be an issue. Sadly, however, this does not appear to be the case. Burlington is being informed by the State Auditor that it failed to administer its TIF District properly relative to another provision of state law that did not exist when Burlington's TIF district was created. That provision is referenced in a footnote on page 3 of the AG's Milton opinion. There much is made of 32 V.S.A. § 5401(10)(E) which provides the following as an exception from the definition of nonresidential property:

(E) The excess valuation of property subject to tax increment financing in a tax increment financing district established under subchapter 5 of chapter 53 of Title 24 prior to June 10, 1997 to the extent that the taxes generated on the excess property valuation are pledged and appropriated for interest and principal repayment on bonded debt or prefunding future tax increment financing district debt.

In examining the Town of Milton's TIF Audit Report, where no municipal increment was pledged and appropriated, the practical effect of following the AG opinion was that the statute required the municipality to determine the percentage of possible increment which is used in total by (1) performing separate calculations for both the state increment and for the municipal increment. The municipality must then (2) add these figures together and determine the percentage of the total possible increment used and then (3) recalibrate both to create balance; i.e. proportionality. This then (4) becomes the refigured calculation of the increment to be excluded from nonresidential property calculations for the education grand list. The AG opinion is that this entire formula is clear and this is somehow all located in the language of § 5401(10)(E).³

³ Interestingly, the Attorney General opinion goes to great lengths to lay out the history of the Title 24 amendments relative to Milton's TIF before concluding that proportionality cannot be identified as clear and unambiguous requirement of the TIF statutes until the Act 190 amendments in 2008. The conclusion

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To follow the logic of the AG's opinion then, a municipality back in 1997 (i.e., in this case, Burlington) should have noted this provision and deduced all of that which was described above. The Attorney General's opinion is that this Act 60 definition, subsequently located in Title 32, effectively directs a municipality in clear and unambiguous terms to administer a TIF district with equal apportionment of state and municipal increment. It should be noted, however, that the TIF district grandfathering provision, § 5404a(c) Act No. 60, 1997, § 45 makes no reference to any substantive change to a municipality's administration of its pre-existing TIF district as a result of this definition. So the AG's opinion would seem to be that back in 1997, the legislature's addition of § 5401(10)(E) in the definition section of the Education Opportunity Act was all that was needed to clearly and unambiguously guide municipalities forward in understanding how to administer a TIF District relative to apportionment of state and municipal increment. This would have to be true because there were no contemporaneous changes made to any of the actual TIF statutes, which are all located entirely in Title 24, in order to support or supplement this directive. However, these Title 24 TIF statutes have since required multiple amendments because so much was unclear and ambiguous. In fact, even the AG's opinion concludes that those amendments could not be said to establish a clear and unambiguous requirement of proportionality for the Town of Milton until 2008 and, therefore, could not be applied retroactively. But then that same AG opinion finds that proportionality of increment is effectively achieved by way of the backdoor through this definition provision.

This was the conclusion found in the State Auditor's report on Milton's TIF District; that: "[t]o the extent Milton's tax increment was not pledged or appropriated for TIF-related debt, the underlying property should have been included in Milton's nonresidential property subject to the statewide education tax and owed to the state since the inception of the TIFs in 1998."

Burlington is being told by the State Auditor that a similar recalibration will need to be done with Burlington's TIF calculations, but that Burlington's recalibration will not be as severe because Burlington used most of its Municipal increment whereas Milton used none at all. However, Burlington submits that there is no recalibration at all that is appropriate.

Why the Auditor Should Reconsider

The AG opinion's interpretation of 32 V.S.A. § 5401(10)(E) is being used to bootstrap exact proportionality into the requirements for Burlington's administration of its Waterfront TIF district. This interpretation and the consequent effect of such bootstrapping, however, flies in the face of the original TIF provisions themselves, and in

then utilizes the footnote from page three to provide the basis for the opinion that effectively requires proportionality by way of the backdoor through this recalculation of nonresidential property method pursuant to § 5401(10)(E).

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the face of the fact that no supplementary amendments to these original provisions were made when this definition provision was adopted. Finally, it flies in the face all subsequent legislative history as indicated by subsequent amendments to the TIF statutes.

With regard to 32 V.S.A. § 5401(10)(E), it appears that in 1997, when ACT 60 was passed, the legislature attempted to create a definition of nonresidential property which would successfully allow TIF districts to be integrated into the State Education Tax Fund system. It is Burlington's contention that this attempt can only be regarded as unclear and ambiguous like many of the other TIF and Act 60 provisions were that ultimately required amendment.

The first problem was that the use of § 5401(10)(E) created a legal definition for nonresidential property in a TIF District (for purposes of establishing a Education Grand list) which directly conflicts with the statutory directive provided to municipal treasurers under the provisions of 24 V.S.A. § 1896 (defining tax increment) for how they were to go about computing taxes. Municipal treasurers were to "include no more than the original taxable value of such real property in the assessed valuation upon which he computes the rates of all taxes levied by the municipality." So § 5401(10)(E) attempted to supersede 24 V.S.A. § 1896 without expressly so stating when it attempted to redefine what property within a municipality with a TIF district would be used for computing taxes. That is by limiting its TIF exemption from calculation of the Education Grand list to that portion of the increment that had been pledged and appropriated for "interest and principal repayment on bonded debt" or, in the alternative, had been set aside for "prefunding future tax increment financing district debt."⁴

Furthermore, this provision for "prefunding" is not sufficiently supported by the statutory framework upon which this definition was laid. The problem is that this is a category of TIF increment that had no statutory existence anywhere in the TIF statutes of Title 24 in 1997 when Act 60 was passed. It is an example of the fact that TIF legislation generally, and the interplay between TIF legislation and Act 60 specifically, required substantial future amendment and clarification as problems with implementation of the statute became apparent through its use over time. No municipality utilizing a TIF district or regulating a TIF district would find it unreasonable to carry forward a fund balance annually when the debt being serviced requires multiple years of repayment. Any reasonable interpretation of § 1900 in its original state would have read it as authorizing increment as pledged and appropriated for future use beyond the current calendar year if

⁴ Because VEPC was not required to oversee 'grandfathered' TIFs, it appears that it was left to the Tax Department to oversee whether, from the State's point of view, 'grandfathered municipalities were apportioning increment properly. Certainly the Tax Department was aware of Burlington's apportionment as evidenced by the 2009 Tax Increment Financing in Vermont report it issued with the Joint Legislative Counsel which presented at page 9 a table with a breakdown of the funds included and not included in Burlington's municipal increment. In any event, for fourteen years Burlington has filed its 411 to certify its Education Grand list based on calculations which utilize the district's original taxable value and it has always been accepted.

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it exceeded the debt servicing requirements for the year in which it was collected.⁵ Certainly that is the interpretation that Burlington has used in carrying forward its annual excess increment from year to year. To the extent that this was not expressly stated and could be interpreted in differing ways, this statutory omission existed because TIF districts had never been used. Then, in 2005, after a period of years, the statute was amended to reflect this practical real world necessary use because, apparently some person(s) believed that it was not clear that such carrying forward was clearly provided for in § 1900 already.⁶

Therefore, Burlington submits that the prefunding language of 32 V.S.A. § 5401(10)(E) either fails due to the fact that it is not supported by comparable language in 24 V.S.A. § 1900 (and, indeed, also 24 V.S.A. § 1896) or it is superfluous because prefunding was already contemplated by all existing references to "pledged and allocated" increment.⁷ In either case 32 VSA § 5401(10)(E) created more contradiction and ambiguity for interpreting statutes which were already fraught with contradictions and ambiguities.

⁵ This is particularly true when considered within the context of the purpose of the TIF provisions generally; see 24 V.S.A. § 1893 – Purpose – "The purpose of tax increment financing districts shall be to provide revenues for improvements located wholly or partly within the district which will encourage development, provide for employment opportunities, improve and broaden the tax base, or enhance the general economy of the municipality, the region, or the state." It is important to note the broad, supportive and encouraging language of this provision. The language is encouraging municipalities to creatively utilize the generated revenues to accomplish broadly defined economic goals.

⁶ Interestingly, the Attorney General's Office initially advised the State Auditor during its conduct of this audit that TIF districts created prior to the 2005 amendment to 24 VSA § 1900 were not authorized to carry forward annual increment surplus either before or after the amendment. Apparently, in the opinion of the Attorney General, if the legislature in amending 24 VSA § 1900 had intended for pre-existing TIF districts to be able to carry forward annual excess increment, it would have expressly so provided. Therefore, the argument went, only new TIF districts, created after the amendment, would be permitted to carry excess increment forward. The Attorney General now however, according to the State Auditor's Office, has reassessed this advice and is now advising the State Auditor that carry-over is permissible for Burlington and other pre-Act 60 TIF Districts (i.e. Newport) because of the language provided in § 5401(10)(E) which provides for inclusion of prefunding TIF debt in the exclusion from the definition of nonresidential property for the purposes of calculating Educational Property Tax. For the reasons referenced above this interpretation fails to provide much legal satisfaction because that prefunding language for calculation of the Education Property Tax Grand List is not supported by any comparable language within the TIF statutes themselves which would authorize the municipality to compute tax rates for real property within the TIF district with anything other than the original taxable value for said properties. Thus the conflict.⁷ It is conceivable that there will be another AG opinion concluding that the "prefunding future debt" language references the setting aside of increment which is gained by a municipality prior to the incurrence of any debt at all. Burlington, however, submits that the legislature included this language in order to expressly authorize the carrying forward of excess increment from year to year, which should have been understood as implied already as being within the parameters of "pledged and appropriated" where the debt serviced contemplates multiple years of repayment. Burlington submits there is no other reasonable interpretation; not when increment is presumed to be a byproduct of development within the District which occurs after a municipality has made improvements (funded by debt to be serviced with TIF increment) which 'but for' the municipalities having made said improvements, said development would not have occurred.

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Despite, these contradictions and ambiguities, the AG's opinion takes a hard line position with regard to the Town of Milton as if these statutory provisions were clear and unambiguous.

Burlington submits that, under these circumstances, to regard § 5401(10)(E) as having any meaning at all requires an interpretation that the language "to the extent that the taxes generated on the excess property valuation are pledged and appropriated" must be read to mean: to the extent that state education taxes generated on the excess property valuation are pledged and appropriated. Those are the taxes that Act 60 – the Educational Opportunity Act – was addressing. That is the only interpretation that effects any meaningful practical implementation of the language at all. All subsequent legislative history of the amendment to these statutes supports this interpretation. For example, if the legislature had truly intended to § 5401(10)(E) to mean that the calculation for exempting the excess valuation of property subject to tax increment financing was to be determined in the manner suggested by the AG opinion, then § 5404a(g) as it is now amended would read differently. § 5404a(g) now limits application of increment to 75%. This is despite the fact that § 1897 clearly allows for up to 75 % state education tax increment and up to 100 % municipal increment. Under that circumstance, § 5401(10)(E) would be in conflict with § 1897 because § 5401(10)(E) if it means what the AG opinion claims would allow for proportionality adjustments upward from 75 % through proportional offsets.⁸

The history of conduct of the municipalities themselves in administering their districts demonstrated that strict or exact proportionality was in fact not understood to be a requirement by the municipalities who had TIF districts. The legislature demonstrated repeatedly that they, as the authors of these statutes acknowledged and affirmed this understanding by rewriting the legislation repeatedly in order to include provisions to accomplish certain things which now the Attorney General opines were unambiguously provided for all along.⁹

In 2005, (2005 Adj. Sess., No. 184) the legislature amended 1897 to read that:

⁸ For example: Take a scenario in which there is \$100,000 of total available increment and the ratio of state education tax to municipal tax was 60 % and 40 %. Then factor that the municipality utilized 100 % of its increment and 75 % of the state increment as allowed under § 1897. Then utilizing the AG opinion theory for interpreting § 5401(10)(E), the exclusion would consist of 75 % of \$60,000 of eligible state education tax increment plus the full 100 % of municipal increment equaling \$40,000 for a total of \$85,000 of excess valuation. This excess valuation would then be eligible for exclusion from the calculation of "nonresidential property". This in turn, would require the proportional off-sets described in the AG opinion because the Education Grand list would need to be adjusted to reflect this 85 % use which comports with the AG opinion that this would be "the extent" that the excess valuation was be used in the manner required under the statute. The resulting adjustment to the Education Grand List in order to create the proportionality that the AG opinion insists resides in the statute would then result in an 85% exemption in direct contravention of the limitations allowed under 32 V.S.A. 5404a(f) which caps the exemption at 75%.

⁹ Clearly if nothing else the history of § 1897 demonstrates that § 1897 was either not clear with regards to proportionality or it was clear that proportionality was not required. Certainly the only statement upon which all parties should be willing to agree is that 1897 did not clearly and unambiguously require proportional use of municipal increment and state education fund increment.

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- (a) The legislative body may pledge and appropriate in equal proportion any part or all of the state and municipal tax increments received from properties contained within the tax increment financing district for the financing for the payment of the principal of and interest on bonds issued for improvements contained wholly or partly within the district and for related costs; provided, that if any tax increment utilization is approved pursuant to 32 V.S.A. § 5404a(g), no more than 75 percent of the state property tax increment and no less than 75 percent of the municipal tax increment may be used to service this debt. Bonds shall only be issued if the legal voters of the municipality, by a majority vote of all voters present and voting on the question at a special or annual municipal meeting duly warned for the purpose, shall give authority to the legislative body to pledge the credit of the municipality for these purposes.

And again in 2008, the provision was amended again; this time to read that:

- (b) The legislative body may pledge and appropriate in equal proportion any part or all of the state and municipal tax increments received from properties contained within the tax increment financing district for the financing for improvements and for related costs in the same proportion by which the infrastructure or related costs directly serve the district at the time of approval of the project financing by the council, and in the case of infrastructure essential to the development of the district that does not reasonably lend itself to a proportionality formula, the council shall apply a rough proportionality and rational nexus test; provided, that if any tax increment utilization is approved pursuant to 32 V.S.A. § 5404a(f), no more than 75 percent of the state property tax increment and no less than an equal percent of the municipal tax increment may be used to service this debt.

The major point manifested by these amendments is that the legislature knew that proportional use of increment was not occurring based upon existing statutory provisions. The legislature then, protective of the state education tax fund, decided to require a greater contribution of municipal increment going forward from municipalities seeking to utilize state education tax increment.

At first their amendment called for not more than 75% of state education tax increment, and left municipalities with their own authority to utilize municipal increment, so long as it was approved by VEPC and so long as it did not constitute less than 75% of municipal increment. This obviously still allowed for a municipality to utilize a full 100 % of its municipal increment. Therefore, proportionality was not required in the 2005 version of 1897 either.

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After a period of time, the 2005 version of § 1897 was amended. Apparently, further examination of how the TIF statutes actually worked, resulted in a demand for further change to require that equal proportions of state and municipal increments would be required but in the case of improvements which did not lend themselves to proportionality, the council could apply a "rough proportionality and nexus test" so long as "no more than 75 % of state education tax increment and no less than an equal percent of municipal increment" was used to service the debt. This change was obviously prompted by fairness concerns that a municipality under the 2005 amendments might only need 50 % or 40 % of increment to service debt but would be stuck with statutory language which required the municipality to utilize not less than 75 % of its increment.¹⁰

The AG opinion, at page 4, indicate that, "[u]pon discovering that Milton (as well as other municipalities) were disproportionately treating state and municipal tax increment, the legislature amended the TIF statutes to expressly and unambiguously require proportional treatment" [referencing the 2008 amendments].

But the municipalities in question (certainly Burlington anyway) appeared before the legislature, heard legislative concerns, and asserted their understanding as to how these provisions worked and how these municipalities administered them. Furthermore, Burlington consistently cooperated with all State Tax Department inquiries concerning its administration of its Waterfront TIF District. Those inquiries appear to have commenced in 2006 if not earlier, and continued through 2007, and on into 2008. The Burlington TIF District was thoroughly scrutinized. Burlington worked with the Tax Department to resolve any and all issues concerning Burlington's administration of its TIF District. In fact, the Tax Department referred one issue (use of TIF revenues for the "Moran" transfer) to the State Auditor's Office (see letter to Tanya Morehouse from Bill Johnson, dated September 15, 2008). In so doing, Mr. Johnson acknowledged Burlington's assistance in resolving many issues to the satisfaction of the State Tax Department. The Moran transfer issue was subsequently resolved, but at no time was Burlington informed that the State Tax Department was taking a position that it was apportioning municipal and state tax department increments inappropriately.

Also in 2008, pursuant to Section 65 of Act 190, the State Tax Department and the Legislative Joint Fiscal Office were requested to analyze the characteristics of the four (4) TIF Districts then existing in the State of Vermont. Together they issued a report: 2009 Tax Increment Financing in Vermont. That report contains charts and tables that specifically demonstrated exactly how Burlington was calculating its municipal increment and which funds were not being included in calculation of Burlington's municipal increment. See Table 1 (page 9). Neither the State Tax Department nor the Legislature objected to this calculation. Additionally, Appendix A to that report provided a specific column: "Allocation of Increment with the EF [Education Fund] AND Municipal Tax Allocation." The column clearly states that 100% of Increment could go

¹⁰ However, for purposes of illustrating my point, it should be noted that proportionality is still not required. A municipality can still apply 100 % municipal increment and only 75 % (or 50 % or 0 %) of state education tax increment.

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to Tax Increment Financing, 0 % was required to go to the State Education Tax Fund and that Allocation of Increment for Municipal Tax Increment was "not specified."

At some point, all of this action (e.g. passing amendments which grandfather pre-existing TIF districts, while addressing concerns of the legislature for future districts) and inaction (e.g. no agent of the State of Vermont ever claiming that Burlington's use of increment was inappropriate) must be understood to be a recognition and acknowledgement by state government of the municipal interpretations of those statutes such that a municipality can rely on that interpretation as being uncontested by the state. Burlington submits that point of reliance came long before this audit ever started.

Conclusion

Burlington submits that it is prepared to defend its apportionment methods as complying with all applicable Act 60, Title 24 and Title 32 statute provisions relating to its apportionment of municipal increment and state increment for the reasons stated above.

Burlington additionally submits that further findings of this audit should reference that the City of Burlington "substantially complied" with all requisite provisions pertaining to municipal and state increment apportionment for the reasons stated above.

Burlington additionally submits that it is prepared to continue to work with the State Legislature to improve unclear and ambiguous provisions within TIF and TIF-related statutes. There may be a need to clarify how to properly treat dedicated, non-discretionary municipal funds within the context of calculating TIF increment for Burlington's future Downtown TIF District which is to be subject to all of the current TIF provisions. However, Burlington notes that a legal forum for pursuing such clarification may already exist within the present language of 24 V.S.A. 1897, insofar as the Vermont Economic Progress Council (VEPC) is authorized to approve project financing and in so doing may utilize a rough proportionality and nexus test. Depending on how much discretion VEPC believes it has, perhaps some of these future increment calculation concerns can be satisfactorily resolved during the VEPC approval process for that new district.