Report of the Vermont State Auditor

December 31, 2012

TAX INCREMENT FINANCING DISTRICTS

Statutory Changes Could Clarify Municipal Requirements and Enhance State Oversight

Thomas M. Salmon, CPA, CFE
Vermont State Auditor
Rpt. No. 12-08

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THOMAS M. SALMON, CPA, CFE
STATE AUDITOR

STATE OF VERMONT
OFFICE OF THE STATE AUDITOR

December 31, 2012

Addressees (see next page)

Dear Colleagues,

Our recently completed tax increment financing (TIF) district audits showed that four municipalities retained $13 million of statewide education property taxes and almost $6 million of this amount should have been remitted to the state's education fund. These errors in TIF district administration resulted, in many instances, from misinterpretation of the TIF statutes. Additionally, our audits highlighted some ambiguities in the TIF statutes which could result in less statewide education property taxes remitted to the education fund than was intended by the legislature.

Given these results, we undertook an audit to summarize the results of the four TIF district audits and to determine whether statutory changes could be made to improve municipal administration and state oversight of TIF districts.

We concluded that some statutory amendments have served to clarify legislative intent and added a limited state oversight role, but ambiguities and inconsistencies remain in the TIF statutes. To the extent these are not addressed, municipalities may err in managing TIF districts as we found in our TIF district audits. Furthermore, limited state oversight exacerbates the risk that municipalities will make errors in administering TIF districts. Given the results of the four TIF district audits, stronger state oversight is justified.

This report includes recommendations designed to clarify TIF statutory provisions for TIF district administration and to enhance the state's oversight role. For example, we recommend that the legislature consider designating a state agency, such as the Vermont Economic Progress Council and/or the Vermont Department of Taxes, with TIF oversight responsibilities, including enforcement of compliance with approved TIF district plans, and authority to interpret and enforce statutory requirements.

I would like to thank the staff of the Vermont Attorney General's Office, Vermont Department of Taxes, Agency of Commerce and Community Development and Vermont Economic Progress Council for their input, 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 tom.salmon@state.vt.us.

Sincerely,

Thomas M. Salmon CPA, CFE

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Introduction

TIF districts are used by municipalities to finance public infrastructure improvements in support of economic development by retaining for a statutorily defined time period a portion of property taxes collected from the district. Because Vermont funds public education through a statewide property tax, TIF districts affect how much a municipality contributes to the state education fund since municipalities with TIF districts retain monies that otherwise would have been remitted[1] to the state.

Our recently completed performance audits[2] of municipal TIF districts found common problems with municipal administration of TIF districts due in part, to misinterpretations of TIF statutes. In addition, the audits highlighted certain ambiguities that exist in the TIF statutes.

Accordingly, this capstone report addresses two objectives, 1) to summarize results of four TIF district audits and 2) to determine whether statutory changes could be made to improve municipal administration and state oversight of TIF districts. To meet our objectives, we compiled the results of the four TIF district audits. We analyzed current statute and obtained the views of state officials to determine whether statutory changes could improve municipal administration and state oversight. Based on our statutory analysis and interviews with state officials, we compiled a list of statutory provisions containing ambiguities and inconsistencies and obtained comments from the Attorney General's Office (AG) regarding the list. We also sought the perspective of nine municipalities (ones with active, approved, or pending TIF district applications) with regard to whether TIF statutes contain ambiguities, inconsistencies, or elements that are unclear, but no comments were provided. A complete description of our scope and methodology can be found in appendix I. Abbreviations used in this report are in appendix II.

[1]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. For simplification purposes, in our report we refer solely to remitting payments to the state.

[2]*Tax Increment Financing: City of Newport Generally Complied with Statutes, But Miscalculated Payments to State* (Rpt 11-03, June 30, 2011), *Tax Increment Financing Districts: Town of Milton Appropriately Established Districts, but the Administration Was Flawed* (Rpt 12-01, January 19, 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* (Rpt 12-03, June 4, 2012), *Tax Increment Financing District: Winooski Made Errors In Administering the TIF District and Underpaid the State* (Rpt 12-06, October 18, 2012).

Highlights: Report of the Vermont State Auditor

Tax Increment Financing Districts: Statutory Changes Could Clarify Municipal Requirements and Enhance State Oversight

(December 31, 2012, Rpt. No. 12-08)

Why We Did This Audit

Our prior four audits of TIF districts found common problems with their administration due, in part, to misinterpretations of TIF statutes. These audits also disclosed ambiguities in the TIF statutes. As a result, our objectives were 1) to summarize the results of four TIF district audits and 2) to determine whether statutory changes could be made to improve municipal administration and state oversight of TIF districts.

What We Recommend

We recommend that the legislature consider clarifying provisions that are ambiguous; designating a state oversight authority; specifying remedies in the event of non-compliance by municipalities; and requiring municipalities to establish performance measures with targets, monitor actual results and report results annually to a state oversight entity and the legislature.

Findings

Burlington, Milton, Newport and Winooski substantially complied with statutory requirements pertaining to the establishment of their respective TIF districts, however each of the municipalities made errors in the calculation of incremental property tax revenue and/or the amount of statewide education increment they could retain. As a result of these errors, the municipalities collectively retained almost $6 million in incremental property tax revenue that should have been paid to the state's education fund. Further, none of the municipalities consistently established performance measures and/or monitored results against expected targets that would allow an assessment of whether the districts were meeting intended objectives.

Statutory changes to eliminate ambiguities and inconsistencies in the TIF statutes could improve municipalities' administration of TIF districts and facilitate municipal compliance with legislative intent regarding various aspects of administering the districts. For example, it is not clear what date should be used to establish the original taxable value (OTV) of TIF districts' properties so a municipality could choose a date that provides more favorable values (e.g., a date that provides for lower OTV). Since OTV is the baseline for the assessed valuation of all taxable real property within the TIF district, it impacts the amount of incremental property value that is exempt from the calculation of statewide education property taxes owed to the state education fund. Selecting a date that provides a lower OTV will increase the amount of incremental property value that is exempt. As a result, it is possible that depending on the date OTV is established, the education fund may receive more or less education property taxes then the legislature intended.

Further, current statute contains a limited state oversight role. In addition, the TIF statute contains no remedy to recoup money due to the state education fund and there is no requirement for corrective action in the event of non-compliance with the statute. Strengthening the state's oversight role and establishing remedies for non-compliance is warranted given the errors we identified during our TIF district audits. For example, our audits showed that municipalities retained $13 million of statewide education increment and almost $6 million of this amount should have been remitted to the state's education fund. If a stronger state oversight role had been in place, the errors that caused this underpayment might have been prevented or detected earlier. Lastly, the TIF statute does not explicitly require municipalities to establish performance measures with targets and monitor actual results, which hampers the legislature's ability to discern whether the use of education funds to finance improvements in TIF districts is yielding expected benefits.

Background

Appendix III summarizes how a TIF works in general. Vermont's TIF program was complicated by the passage of Act 60 in 1997, which significantly changed the method of funding public education in Vermont by establishing a statewide education property tax rate to be set by the state. Municipalities are required to collect statewide education property taxes 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. Because of this change, municipalities with TIF districts retain monies that otherwise would be required to be remitted to the state for funding public education throughout the state.

Since inception, all but two of the provisions of the original TIF statute have been amended at least once. In some cases, amendments were prospective or applied to all existing TIF districts. One of the changes directs municipalities to apply to the Vermont Economic Progress Council (VEPC) for approval to use statewide education increment[3] to help fund development in new TIF districts. VEPC was named as the authorizing body and given guidelines to aide in the approval process in Title 32.

At this time, 10 Vermont municipalities have 13 on-going or planned TIF districts (see appendix IV for a listing). We have audited five districts at four municipalities, 1) Newport's City Center Industrial Park district, 2) Milton's Husky and Catamount districts, 3) Burlington's Waterfront district, and 4) Winooski's Downtown district (the TIF portion only). Each of these four municipalities had financed their TIF district improvements and had used the financing to fund construction activity for infrastructure improvements at the time of our audit.

TIF District Audits Contained Mixed Results

In general, our audits of five TIF districts concluded that the municipalities 1) substantially complied with statutory requirements pertaining to the

[3]Statewide education increment is a component of incremental property tax revenue which is calculated based on the current property values of the TIF district less TIF district property values at the time the district was established, multiplied by the statewide education property tax rate.

establishment of the districts, 2) retained several million dollars in incremental property tax revenue that should have been paid to the state's education fund and 3) did not consistently establish performance measures and/or monitor results against expected targets that would allow an assessment of whether the districts were meeting all of the intended objectives. Causes included a lack of documented procedures and processes, inadequate documentation, and reliance on a single individual to perform complex calculations without a secondary review. In addition, we found that municipalities were misinterpreting the TIF statutes.

Establishment of TIF District

Table 1 summarizes the extent to which each of the municipalities complied with statutory requirements related to the establishment of the TIF districts. Although there were a few exceptions, in general the municipalities adhered to the statutory requirements.

Table 1: Municipalities' Compliance with Statutory Requirements for Establishing TIF Districts

Statutory Requirements	Newport	Milton	Burlington	Winooski
Hold publicly warned meeting on proposed TIF district plan, with a description of the TIF district boundaries and properties.	Complied	Complied	Complied	Complied
Hold publicly warned meeting on a financial plan for proposed improvements.	Unable to locate financial plan	Complied	Complied	Unable to locate financial plan
Adoption of TIF district plan and creation of TIF district by legislative body of municipality.	Complied	Complied	Complied	Complied
Record TIF district plan with municipal clerk and lister or assessor.	Complied	Complied	Complied	Unable to demonstrate that a plan with a list of TIF district properties was recorded
Obtain approval of majority of registered voters for general obligation or revenue bonds at a warned special or annual meeting.	Complied	Complied	Complied	Complied
Apply to VEPC for approval to use statewide education increment for TIF district improvements.	Not applicable	Complied	Not applicable	Not applicable

Retention of Incremental Property Tax Revenue

State statute establishes the methodology municipalities are to use to calculate incremental property tax revenue generated by TIF districts and the amount, if any, required to be distributed to the state's education fund. The first calculation is the incremental property tax revenue that is generated by a TIF district. Incremental property tax revenue occurs when municipal financed improvements in TIF districts result in increased property values. The incremental property value growth is multiplied by current state education and municipal property tax rates. The resulting revenue is comprised of municipal increment and statewide education increment. Municipalities with approved TIF districts may retain all or some of the statewide education increment instead of remitting it to the state. The extent to which a municipality may retain the statewide education increment is established by a second calculation, which determines the extent to which the incremental property tax revenue is pledged[4] and appropriated[5] for repayment or prefunding of eligible TIF district debt. TIF district debt is eligible if it is a statutorily approved financing method, including general obligation or revenue bonds, issued within a specified period of time of the creation of the TIF district[6] to finance expenditures related to improvements located wholly or partially within the TIF district.

Each of the municipalities we audited made errors in the calculation of incremental property tax revenue and/or the amount of the statewide education increment it could retain. As a result of these errors, we calculated that almost $6 million was retained by the municipalities that should have been remitted to the state's education fund. Table 2 summarizes the types of errors that we found at three of the municipalities.

[4]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.

[5]Per Vermont statute, appropriations are planned expenditures.

[6]This period has varied because the statutory provisions have changed over time.

Table 2: Municipal Errors in Calculating How Much of the Statewide Education Increment They Could Retain

Calculation/ Type of Error	Municipalities		
	Milton	**Burlington**	**Winooski**
Amount incorrectly retained (should have been remitted to state education fund)	**$3.4 million**	**$1 million[a]**	**$1.5 million[b]**
Incremental property tax revenue calculation			
Incorrect OTV.			X
Misapplication of an adjustment for reappraisals of properties in TIF districts.	X		X
Exclusion of municipal tax rates.	X	X	
Retention of statewide education increment calculation			
Ineligible Use: Underlying expenditure did not meet definition of improvement.			[c]
Ineligible Use: Underlying expenditure for projects outside of the TIF district boundary.	X		[d]
Ineligible Debt: Debt issued outside of borrowing period.	X	X	
Ineligible Debt: Use of a financing instrument other than a general obligation or revenue bond.	X		[e]
Calculation error: Did not decrease the retention percentage to 75 percent starting July 1, 2006.	X		

[a]Our Burlington audit questioned whether the privately-owned land and parking garage at 75 Cherry Street should have been exempted from property taxes. We referred this issue to the Department of Taxes (DOT). If DOT concludes that the property has been inappropriately excluded from property taxes, we estimated that Burlington failed to collect approximately $947,000 in property taxes, of which $532,000 should have been paid to the state.
[b]Winooski mischaracterized three taxable properties as non-taxable. Since the city's property records did not contain assessed values for these properties, we were unable to determine a definite effect on incremental property tax revenue.
[c]A portion of the Winooski TIF revenue bond was used to pay for expenditures that were not TIF district improvements. However, at the time of our audit, Winooski's bond payments exceeded the statewide education increment by more than the ineligible expenditures so the statewide education increment had not yet been used for ineligible purposes.
[d]A portion of the Winooski TIF revenue bond was used to pay for construction projects that were outside of the TIF district boundaries. However, Winooski could not provide us with documentation that would have allowed us to determine the actual cost of these ineligible activities.
[e]We concluded that Winooski had entered into agreements that pledged the use incremental property tax revenue that was not allowed by statute (e.g., not a bonded debt). However, Winooski had not used incremental property tax revenue to make payments pursuant to these agreements. Nevertheless, if Winooski uses incremental property tax revenue to make these payments in the future, it will be an ineligible use of these funds.

If Milton, Burlington, and Winooski do not correct these errors, they will continue to miscalculate the amount of incremental property tax revenue generated by the TIF district and will likely continue to retain funds that should be sent to the state for purposes of funding public education.

The fourth municipality we audited, Newport, also miscalculated the amount of statewide education increment it could retain by about $37,000. Newport's retention amount was wrong because it tried to use a calculation other than what was provided for in statute. According to the Newport city manager, based on the advice of counsel, Newport has established an account within its general ledger accounting system to record a potential liability to the state for excess incremental property tax revenues.

Performance Measurement

The municipalities' establishment and monitoring of performance measures to indicate the extent to which the TIF districts were meeting state and municipal economic and fiscal goals were limited. Three out of four municipalities established performance measures for less than half of the objectives that the TIF districts were intended to achieve. Moreover, for those objectives in which performance measures were established, the municipalities generally did not establish targets or consistently track actual results.

Without performance measures, targets, and monitoring of actual results for all objectives, the municipalities' ability to determine whether the TIF districts are operating as intended is limited. For example, one of the objectives of the TIF districts set forth by the legislature is to improve employment opportunities. None of the four municipalities had established a performance measure for this objective. Without a performance measure (with associated targets) against which actual results are tracked there is no systematic mechanism in place to evaluate the extent to which the TIF districts have improved employment opportunities and to discern whether the level of improvement is what was intended.

Enhancements to Statute Could Improve Administration and Oversight of TIF Districts

Over time, the legislature has improved the TIF district statutes, but additional amendments could clarify and improve the statutorily required processes for municipal administration and state oversight. Further, state oversight is largely unaddressed in statute. Municipalities establishing TIF districts follow a statutorily required application and approval process administered by VEPC, but the statute does not specify whether VEPC or any other state entity has responsibility for oversight of TIF districts subsequent to the initial application approval. Moreover, in the event of municipal non-compliance with statutory requirements, there is no statutory remedy with which to require corrective action. This means there is no mechanism to recoup the $6 million our audits determined are owed to the education fund.

Our audits also identified areas that the legislature may want to consider related to 1) the required adjustments to statewide education increment and 2) the audit requirement. We are not making recommendations related to these issues, but our observations are located in appendix V.

Legislature Has Made Improvements to the TIF Statute

Some amendments to TIF statute have served to clarify legislative intent or have added limited state oversight role which may help to prevent certain issues we noted during our TIF district audits from occurring in other TIF districts. See table 3 for a description and analysis of some of the statutory amendments that have improved the TIF statutes.

Table 3. Description and Analysis of Select Statutory Amendments

Statute reference	Act (session)	Description of Statutory Amendment	Explanation of Improvements
32 VSA § 5404a(h)	Act 71 (1997) Act 184 (2005)	Required VEPC authorization for municipality to utilize statewide education increment to repay TIF district debt. Approval criteria specified.	During the initial phase of the TIF district, VEPC's oversight might prevent errors in calculating OTV and failing to record an official list of TIF district properties.
24 VSA § 1901	Act 190 (2008)	Required all TIF districts to report certain data to VEPC and DOT annually. VEPC and DOT to compile data and report to legislature.	Added a state role in providing data on TIF district status to the legislature.
24 VSA §1897(a)	Act 184 (2005)	Added requirement to Title 24 to use proportionate amounts of municipal and statewide education increment to repay TIF district debt.	Might prevent errors in calculation of how much statewide education increment may be retained and prevent municipalities from using a disproportionate share of municipal increment. Prior to this amendment, the provisions of Title 24 did not distinguish between the components comprising tax increment and did not expressly address the issue of whether there could be unequal use of the tax increment components for debt repayment. Title 32 already required that all of the tax increment be used to repay TIF district debt.
24 VSA § 1891(7)	Act 190 (2008)	Expanded the types of debt instruments that municipalities could use to finance TIF district improvements.	Allows municipalities to use a greater variety of debt instruments to finance TIF district improvements than originally was available to the districts we audited.

Some Statutory Provisions for Municipal Administration of TIF Districts are Ambiguous or Inconsistent

Some of the statutory provisions that direct municipalities in administering TIF districts contain ambiguities or inconsistencies that could result in municipal interpretations that diverge from legislative intent (see table 4). These provisions have potential to complicate TIF management and put the state education fund at risk of receiving less funds from municipalities with

TIF districts than was intended. Amending these statutory requirements could improve compliance with the legislature's intended operation of the TIF districts and reduce the risk that municipalities will retain statewide education increment that should be remitted to the state's education fund. The AG's office agrees that the provisions identified in table 4 are ambiguous or inconsistent.

Table 4: Summary of Ambiguous or Inconsistent Statutory Provisions Related to TIF District Administration

Reference	Description	Comment
Original Taxable Value		
24 VSA §1895 24 VSA §1898 (b)	On or about 12:01 a.m., April 1 of the first year, the assessor shall certify the assessed valuation of all taxable real property within the district as then most recently determined. OTV is established on "the date the district was approved."	§1895 appears to indicate OTV is established on April 1 of the calendar year the district was created, but this provision also refers to the "most recently determined" value which could indicate the value at the precise moment of the creation of the district. §1898 (b) also supports the interpretation that OTV is established on the date the district was created. The selection of the date of OTV establishment might result in significantly different TIF district property values, affecting calculation of the tax increment.
Financing period		
24 VSA §1894(a)–(b)	Subsection (a) (1) provides that municipalities may incur debt at any time within 20 years of the creation of the district. Subsection (b) provides the statewide education increment may only be used to repay debt incurred within the first five years of the district creation.	It is not clear what portion of tax increment may be used to repay debt incurred in the 20-year period specified in subsection (a)(1) since the use of the statewide education increment is restricted to repayment of debt incurred within the first five years of district creation. This inconsistency might lead municipalities to conclude that statewide education increment may be used for debt incurred outside the five-year period.
24 VSA §1894(a)(2)	A borrowing period might be automatically extended if a municipality reapplying to VEPC can demonstrate that the inability to incur indebtedness in the first five years was the result of macro-economic conditions.	Statute does not define specific circumstances that would qualify as macro-economic conditions. Without greater specificity there is a risk of different interpretations by VEPC and municipalities, which could lead to extension of the borrowing period for circumstances not intended by the legislature.
Financing authorization		
24 VSA §1897 (a)	The legal voters of a municipality, by a single vote, shall authorize the legislative body to pledge the credit of the municipality up to a specified maximum dollar amount for all debt obligations to be financed with state property tax increment.	It is unclear whether a single vote means that municipalities are limited to presenting total TIF district debt obligations to voters one time or are able to increase the total debt by seeking voters' approval multiple times. In addition, it is not apparent whether a "single vote" precludes municipalities from seeking voters' approval after an initial defeat.
Financing types		
24 VSA §1894(3)(c) 24 VSA §1891(7)	VEPC shall assure the viability and reasonableness of any proposed financing other than bonding and least-cost financing. Defines financing types municipality can incur, such as bonds, interfund loans, Vermont revolving loan funds.	Least-cost financing is not defined as one or more of the financing types listed in 24 VSA §1891(7). As a result, the reference to least-cost financing in §1894(3)(c) might be interpreted as allowing additional types of financing beyond what is specified in 24 VSA §1891(7). This could result in a municipality using borrowing instruments that the legislature did not intend to allow.

Reference	Description	Comment
24 VSA §1891(7)(c)	Interfund loans are allowed as one of the TIF financing types.	Statute does not specify whether documentation of terms and conditions of interfund loan financing is required, including limitations on interest that can be charged to the TIF district. Given that loans between municipal funds are within the control of the municipality, there is potential for overcharging interest to the TIF district to the benefit of the municipality and detriment of the statewide education fund.
Calculation of increment		
24 VSA §1896(a) 24 VSA §1896(b)	§1896 (a) refers to the calculation of the increment "in each year for which the assessed valuation exceeds the original taxable value." §1896 (b) provides that the state education property tax revenues for the district in the first year following a town-wide reappraisal shall not be less than in the prior year.	Generally, the amount of statewide education property taxes owed to the state education fund is based on the OTV. Subsection (b) requires the payment of education property tax to the state education fund in the year following a town-wide reappraisal to be a minimum of the prior year payment. However, it is not clear how the payment to the state education fund should be calculated when TIF district property values decline below the OTV value and a town-wide reappraisal did not occur.[a]
24 VSA §1898(b)	Increment is defined as the increase in the aggregate taxable valuation of land and improvements in the district.	Statute seems to indicate that tax increment is calculated in the aggregate (netting gains and losses between homestead and non-residential property categories), but some municipalities calculate the tax increment on each property individually. These different methods resulted in fairly inconsequential differences on an annual basis in one of the audited districts, but could have a significant impact over the life of a TIF district.
Exclusion of portion of municipal tax rate		
24 VSA §§1896, 1897	§1896 – Municipal treasurer shall hold apart all taxes paid on the excess valuation of real property in the TIF district, which amount is the "tax increment." §1897 – Municipality may use any part or all of the state and municipal tax increments in equal proportions; no more than 75% of the state property tax increment and no less than an equal percent of the municipal tax increment may be used.	An apparent conflict exists between these statutory provisions, which require use of all tax rates to calculate tax increment, and some municipal charters (approved by legislature), which designate portions of municipal tax rates to be used for specific purposes. It is not clear whether municipalities must comply with state statute requiring use of all tax rates or whether charter provisions apply. If charter provisions supersede state statute, disproportionate amounts of municipal and statewide education increment would be contributed toward payment of TIF district obligations.
Retention		
24 VSA §1894(b)	The statewide education increment may be retained for up to 20 years. Retention commences with the first debt incurred.	Because statute does not expressly indicate what constitutes "first debt," it is not clear whether this is intended to be the debt that will be repaid with statewide education increment. As a result, it could be interpreted to mean the first debt incurred even if that debt will not be repaid with statewide education increment.

Reference	Description	Comment
Utilization		
24 VSA §1891 (6) 24 VSA §1891 (4)	Defines TIF district related costs, including "[sums] attaining the purposes and goals for which the tax increment financing district was created." Defines allowed TIF district improvements, but also provides a provision for other public improvements necessary for carrying out the objectives of [the] chapter, which are contained in 24 VSA §1893.	Expansive statutory provisions without express limitations could cause a great variety of interpretations of related costs and/or necessary improvements. For example, municipalities may presume that municipal general operating costs, such as police services, are related costs and the construction of municipal buildings (e.g. a town hall) is a necessary public improvement. As a result, tax increment may be used for purposes that were not intended by the legislature.
24 VSA §1891(7) 24 VSA §1897 32 VSA §5401(10) E)	Lists allowed financing instruments, such as bonds, HUD §108 loans, USDA loans, state revolving fund loans. Provides for the use of the education tax increment to repay bonds and other types of debt. Exempts payment of education increment to state if total incremental property tax revenue is used to pay bonded debt.	It is unclear whether statewide education increment is exempt from payment to the state if it is used to pay any of the financing types allowed in 24 VSA §1891(7) or is only exempt if the use is limited to repayment of bonded debt.

[a]When property values are increasing, OTV is used to calculate the payment due to the state. However, if OTV was $10,000,000, but assessments demonstrated that TIF district property values had declined to $9,000,000, it is not clear which amount would be used to calculate the payment due to the state in a year without a town-wide reappraisal.

Certain of the ambiguities and inconsistencies highlighted in table 4 came to our attention during our TIF district audits. For example:

- *Original Taxable Value.* The significance of the date selected for OTV establishment and the ambiguity surrounding this is exemplified by Milton's interpretation of the relevant statutory provisions. OTV is the baseline for the assessed valuation of all taxable real property within the TIF district and is significant because it 1) impacts the value of taxable property that is exempt from statewide education property taxes and 2) affects the amount of property tax revenue that a municipality may retain to pay debt incurred to finance development in a TIF district. Milton's districts were created by the selectboard on March 30, 1998 at which time improvements had already been made in one of the areas designated as a TIF district. Milton interpreted 24 VSA §1895 as setting OTV at the "most recently determined" property values. This meant using the existing property values that were established at April 1, 1997 and resulted in an OTV of $20.9 million. Alternatively, if OTV had been established as April 1 of the calendar year the district was created, this would have meant property values as of April 1, 1998 and would have resulted in an OTV of $40.6 million. During the course of our audit of Milton's TIF district, we sought the advice of the AG's office about Milton's interpretation.

The AG advised that the statute was ambiguous and that Milton's interpretation was reasonable in light of this ambiguity. To the extent this ambiguity is not addressed, it is possible that very divergent results will occur relative to the determination of the OTV.

- *Interfund loans.* During our audits, we found that Milton[7] and Winooski were using municipal funds to pay for TIF district improvements and subsequently reimbursing these funds with tax increment. However, these municipalities did not have formal documentation of the interfund loan transactions and there is no statutory requirement for documentation of the terms and conditions of interfund loans. Without a requirement for formal loan documentation and no statutory criteria for allowable terms of these types of loans, the state has no way to judge whether the terms of the loans are reasonable. In addition, without statutory criteria for allowable terms, there may be increased risk of conflicts of interest between the related parties (i.e., the municipality and the TIF district are both managed by the same personnel).

- *Calculation of tax increment.* Winooski's TIF district property values declined below OTV in the first two years following establishment of the OTV which reduced the amount of property tax revenue generated by the district to levels less than the amount produced prior to district creation. DOT believed the intent of the TIF statute was to "make the education fund whole," due in part, to the provision that requires the payment of education property tax to the state education fund in the year following a town-wide reappraisal to be a minimum of the prior year payment. Accordingly, DOT concluded that municipalities with TIF districts are required to continue to remit payments to the education fund based on OTV, regardless of whether property values have declined. As a result, DOT billed the city for the difference between the reduced amount and the amount generated prior to the decline in property values even though the decline in property tax revenue was not related to a town-wide reappraisal.

- *Exclusion of portion of municipal tax rate.* Several of Burlington's municipal taxes are authorized by Burlington's city charter (approved by the legislature) for a specific purpose, such as its annual

[7]Milton used this type of financing for its TIF district prior to statute being amended to allow for inter-fund loans and we concluded that it was an ineligible use since the statutory amendment did not provide for retroactive application.

assessments for police and fire, streets, library and park use. Given that state statute requires all tax rates be used to calculate tax increment, our office sought the advice of the AG's office. The AG pointed out that legislative intent with regard to TIF calculations is ambiguous in treating certain assessments as special and at the same time having an "all taxes" mandate. Accordingly, Burlington could exclude a portion of its municipal tax revenues from its TIF revenue calculation if the legislature designated these revenues for a specific purpose. Excluding some municipal tax rates from the calculation of incremental property tax revenue increases the amount of statewide education increment that will be needed to pay TIF district obligations. Burlington excluded certain municipal tax rates which has had the effect of reducing municipal increment by $1 million since the TIF's inception and therefore, increasing the amount of statewide education increment used to repay the TIF district debt.

State's Oversight Provisions of TIF Statute Warrant Further Improvement

Current TIF statute contains a limited state oversight role, that if strengthened, could help prevent the types of errors and statutory misinterpretations we found in our audits. Moreover, current statute does not have a mechanism to remediate municipal errors that result in underpayments to the education fund. Lastly, the TIF statute does not explicitly require municipalities to establish performance measures and targets and to track and report actuals to the state. Without this type of data, the legislature has limited information to determine whether TIF districts are achieving desired results and whether the state is achieving the expected benefit from the use of the education fund to finance economic development.

State oversight of TIF district operations and authority to interpret and apply statutory requirements

Combining the results our four TIF district audits, we determined that municipalities have retained $13 million of statewide education increment[8] and that almost $6 million[9] of this amount should have been remitted to the state's education fund. Given these results, stronger state oversight is

[8]We audited the Newport, Milton and Burlington TIF districts through June 30, 2010 and Winooski's TIF district through June 30, 2011.

[9]This amount could be higher because Winooski mischaracterized some TIF district properties as tax exempt when the properties should have been treated as taxable.

justified. Without stronger state oversight, the errors we identified are likely to continue in the districts we audited and may be perpetuated in other districts not yet subject to audit.

Under current statute, VEPC oversees the application and approval process for TIF districts and collects some TIF district data from municipalities for reporting to the legislature. In addition, DOT manages the processes utilized by municipalities to report TIF district incremental property values to the state so that the state has data to calculate the amount of statewide education taxes due to the education fund. However, state statute does not designate either entity with responsibility for oversight of TIF district operations. As a result, there is no state entity with systematic processes in place to review critical aspects of municipal administration of TIF districts such as how tax increment is utilized or to verify whether a municipality has retained the appropriate amount of statewide education increment and directed an appropriate amount to the education fund. In addition, VEPC approves TIF district applications, but the statute does not address whether VEPC has authority to enforce a municipality's compliance with the parameters of the TIF district plan as approved by VEPC.

Further, no state entity is designated with rule-making authority which would encompass interpreting statutory provisions associated with TIF districts. As a result, although VEPC and DOT are involved in aspects of TIF district administration both lack definitive authority to interpret statute and to apply statutory requirements to municipalities. Likewise, there is no entity that municipalities may consult with regarding statutory interpretation and have confidence that they receive advice that is authoritative and enforceable.

Our research of oversight mechanisms utilized in other states and best practice recommendations of some government and development associations indicate various models for state oversight are applied or recommended. For example, of the six states with well-established TIF programs that we reviewed, five have designated state entities with some oversight responsibility. In three of these states, the designated entity is a state agency responsible for taxation and the oversight includes some level of review of the amount of tax increment that a municipality is entitled to receive. Other states utilize departments of education, finance or the state comptroller to provide oversight. Two of the states that designated state entities with some oversight responsibility, also vested these entities with authority to promulgate rules.

The Government Finance Officers Association recommends formation of a committee, comprised of members of the taxing authorities associated with

the TIF district, and that this committee hold periodic meetings to, among other things, assess the project progress, determine if the TIF district is following the project plan and whether the district should continue to operate.

Remedy for municipal non-compliance

State statute is silent with regard to remedies for instances in which municipal noncompliance with statutory provisions results in an underpayment to the education fund. This leaves the state without a mechanism to recoup funds that should have been remitted to the education fund or to require corrective action in the event of statutory non-conformance. This lessens the ability of the state to hold municipalities accountable. Further, the state has not attempted to collect the $6 million that our TIF districts audits concluded should have been remitted to the education fund, in part because there is no mechanism in place to facilitate collection.

Reporting results of TIF district activity

State statute requires municipalities to report some performance results, such as financing repayments, tax increment, and actual investment, in a form prescribed by VEPC. VEPC requests additional information such as the annual amount of tax increments utilized among other information. Commencing in 2012, VEPC requests that municipalities with TIF districts approved subsequent to 2008 report actual results for specific performance measures. As of 2012, this request applies to four municipalities. Two of the four municipalities had actuals to report relative to the specific performance measures and these municipalities provided data to VEPC.[10] One other municipality reported actuals for one of ten performance measures included in the annual VEPC report.

Overall, the results reported for most municipalities are limited and do not provide information needed to assess whether all of the state's goals delineated in 24 VSA §1893, to broaden the tax base, encourage development and improve employment opportunities, have been achieved.

Establishing performance measures with targets for each measure, monitoring actual results and reporting to a state oversight entity and the legislature is critical in order to assess if the state goals are being met. However, since there is no statutory requirement to implement performance measures, it is

[10]The other two municipalities did not incur TIF district debt to finance improvements in the TIF districts.

not certain whether municipalities will follow VEPC's direction. In fact, in response to our recommendation to implement performance measures, Burlington noted that this was not a statutory requirement, but that it had no objection to implementing performance measures for new projects in its waterfront TIF district.

Conclusion

Since the inception of the TIF district program, the TIF statutes have undergone numerous changes. However, further revisions are warranted to clarify certain provisions, augment the state oversight role, provide a remedy for municipal non-compliance, and add requirements for municipal performance measurement. To the extent ambiguities and inconsistencies remain in the TIF statutes, municipalities may err in managing TIF districts as we found in our TIF district audits. Furthermore, limited state oversight exacerbates the risk that municipalities will make errors in administering TIF districts. Without a strengthened role for the state in oversight of TIF districts and with no remedy for municipal non-compliance with TIF district statutory provisions, it is likely that municipalities will continue to make errors in administering TIF districts, including retaining funds that should have been remitted to the state education fund. Without a statutory requirement to implement performance measures and report actual results, the state will remain without the information necessary to determine whether TIF districts are operating as intended and whether the state is achieving the expected benefit from the use of the education fund to finance economic development.

Recommendations

We recommend that the legislature consider:

1. Clarifying ambiguous or inconsistent TIF statutory provisions for district administration – as discussed in table 4 – related to:

    a. The date of OTV establishment;

    b. What portion, if any, of tax increment may be used to repay debt incurred in the 20-year period following creation of the TIF district;

    c. What qualifies as a macro-economic condition;

d. The intent of the single vote requirement;

e. The definition of least–cost financing;

f. A requirement that terms and conditions of interfund loan financing be documented;

g. Statutory criteria for allowable terms of interfund loans;

h. The calculation of the education fund payment in years when property values decline below the OTV;

i. The calculation of tax increment when there are gains and losses in the different property categories (i.e., homestead and non-residential);

j. The inclusion/exclusion of municipal charter restricted components of municipal tax rates in calculation of tax increment;

k. The definition of first debt;

l. The definition of related costs and improvements;

m. The type of debt that may be paid by statewide education increment.

2. Designating a state agency, such as VEPC and/or DOT, with TIF oversight responsibilities, including enforcement of compliance with approved TIF district plans, and authority to interpret and enforce statutory requirements.

3. Specifying remedies in the event of non-compliance by municipalities.

4. Requiring municipalities to establish and monitor performance measures with targets where the measures are linked to the statutory TIF goals and actual results for each measure are reported to the state oversight entity and the legislature at least annually.

Management Comments and Our Evaluation

The Chief Assistant Attorney General of the Attorney General's Office provided written comments on a draft of the report on December 19, 2012 which is reprinted in appendix VI. On December 21, 2012, the Secretary of the Agency of Commerce and Community Development, the Director of the Vermont Economic Progress Council and the Commissioner of the Department of Taxes provided a single set of written comments on a draft of the report which is reprinted in appendix VII.

In his response the Chief Assistant Attorney General stated that the AG's Office is in agreement with the report findings, conclusions, and recommendations on the statutory issues.

In particular, the Chief Assistant Attorney General concurred that the statutory provisions highlighted in table 4 are ambiguous or inconsistent with one another, thereby complicating the administration and oversight of TIF districts. Further, he agreed with our finding that the statutes do not provide adequate state oversight of the TIF program. Specifically, he noted the statutes do not 1) designate an executive or legislative agency to oversee the administration of the TIF districts, 2) grant any agency the statutory authority to assure the proper allocation of education property taxes to the education fund and 3) provide specific remedies to address miscalculations of TIF increments. He points out that the laws do not establish a legislative or administrative process for resolving disagreements about sometimes ambiguous statutes and do not authorize any state official to make the education fund whole by applying offsets against state payments to municipalities for education or other purposes.

The Chief Assistant Attorney General stated that some immediate issues could be resolved by the legislature, including determining whether and how the underpayments to the education fund might be remedied, providing guidance to municipal and state officials on the administration and oversight of TIF districts and reconciling and consolidating in one place TIF laws contained in Vermont statutes, session laws and municipal charters.

Finally, the Chief Assistant Attorney General suggested that a legislative review of these laws should also consider the relation between tax increment financing and education funding, emphasizing that "the legal consideration is that tax increment financing must be structured in a way that does not upset

the equality of education funding mandated by the *Brigham* decision[11] and by the education funding laws enacted to comply with that decision."

In their response, the Secretary of the Agency of Commerce and Community Development, Director of VEPC and Commissioner of DOT state that they generally agree with the findings and conclusions of the report. Specifically, they agree with the recommendations for specific statutory clarifications and that the matter of oversight and enforcement needs to be addressed for TIFs. However, they expressed concern that some solutions might require too much state resources and suggested that oversight and enforcement that puts TIF towns and state administrators in a consistently adversarial relationship should be avoided. They recommend that an alternative dispute resolution mechanism be used in conjunction with the current audit procedures.

SAO believes that an alternative dispute resolution mechanism could be an aspect of enforcement, but that on its own, it is not an effective replacement for designating a state agency, such as VEPC and/or DOT, with TIF oversight responsibilities and interpretive authority because dispute resolution could occur well after non-compliance occurs. Further, oversight designed to be systematically recurring could serve as a preventive measure to reduce the likelihood of future disputes. Equally important, consistent and effective state oversight could provide protection for state education funds that are used in the funding of TIF districts.

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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.

[11]The Vermont Supreme Court decision that found Vermont's existing educational funding system was unconstitutional and concluded that the state must provide "substantially equal access" to education for all Vermont students.

Appendix I
Scope and Methodology

In performing work in support of our two objectives, we compiled the results of four audits conducted by SAO at the behest of the legislature on the active TIF districts in Vermont, namely the City of Newport's district, the Town of Milton's Husky and Catamount districts, the City of Burlington's waterfront district and the City of Winooski's downtown district (TIF portion only). The audit reports were issued June 2011, January 2012, June 2012, and October 2012, respectively, and are available at www.auditor.vermont.gov.

In planning our work with respect to our second objective, we reviewed the level of oversight provided by state agencies relative to municipal administration of TIF districts, based on the documents and records from the TIF audits conducted to date.

To identify possible changes to statute that could improve municipal administration and state oversight, we performed the following procedures:

- Analyzed current Vermont TIF legislation – applicable sections of Title 24 and Title 32 of the Vermont Statutes Annotated and applicable session laws;
- Compiled a list of ambiguities noted in AG's opinions/advice obtained during TIF district audits; and
- Interviewed state officials from VEPC and DOT to elicit their perspective on whether changes to statutes could improve administration and oversight of TIF district.

In addition, we developed a list of ambiguities and inconsistencies based on these procedures and obtained comment from the AG's office regarding the list.

We provided municipalities with active TIF districts and those with approved or pending TIF district applications the opportunity to contribute their perspective regarding whether 1) statutory changes could be made to improve municipal administrative and state oversight of TIF districts and 2) TIF statute contains ambiguities, inconsistencies or elements that are unclear. None of the municipalities supplied comments.

We reviewed TIF statutes of other states, such as Minnesota, Utah, Michigan, and Illinois, concentrating our review on the statutory requirements providing for TIF districts' oversight.

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 and the

Council of Development Finance Agencies, audit reports of TIFs in other states, and studies conducted related to TIF reform initiatives in other states.

We interviewed the director of VEPC and personnel from DOT's Division of Property, Valuation and Review regarding their processes, policies, and procedures related to overseeing the TIF districts.

Our audit fieldwork was performed between October 2012 and December 2012. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards 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. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

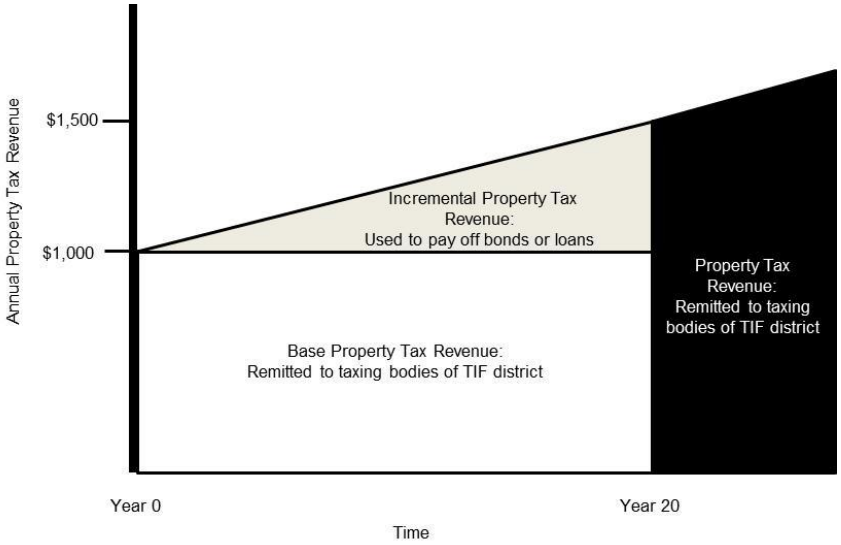
Appendix II
Abbreviations

AG	Office of the Attorney General
DOT	Department of Taxes
OTV	Original Taxable Value
TIF	Tax Increment Financing
VEPC	Vermont Economic Progress Council
VSA	Vermont Statutes Annotated

Appendix III
How a TIF works

In theory, improvements made to TIF districts 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 twenty-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.[12] Once the bonds are paid off, the taxing authorities (municipality and state) receive all property tax revenues (in this example, $1,500 per year). Figure 1 illustrates this example graphically.

Figure 1: Simplified Illustration of How a TIF District Can Generate Incremental Revenue (example assumes a stable tax rate)



[12]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)).

Appendix IV
On-going or Planned TIF Districts

As shown in table 5, 10 municipalities have 13 on-going or planned TIF Districts.

Table 5: Listing of On-going or Planned TIF Districts

Municipality	TIF District	Status as of November, 2012
Burlington	Waterfront	Active – Created in 1996. Borrowing period extended until 2015. Increment may be retained until 2025.
	Downtown	Approved by VEPC 2011.
Milton	Husky	Active – Created in 1998. Borrowing period ended 2008. Increment may be retained until 2019.
	Catamount	Active - Created in 1998. Borrowing period ended 2008. Increment may be retained until 2019.
	Town Core	Approved by VEPC 2011.
Newport	City Center Industrial Park	Active – Created in 1997. Bonding expected to retire in 2014.
Winooski	Downtown	Active – Created in 2000. Borrowing period ended 2005. Increment may be retained until 2024.
Colchester	Severance Corners	Approved by VEPC 2010, awaiting approval of financing plan
Hartford	White River Junction Downtown	Approved by VEPC 2011.
St. Albans	Downtown	Approved by VEPC 2012.
South Burlington	City Center	Application being reviewed by VEPC.
Barre City	Downtown	Application being reviewed by VEPC.
Williston	Taft Corners	Submitted letter of intent to VEPC in 2008.

Appendix V
Observations Pertaining to Required Adjustments to the Statewide Education Increment and Audits of TIF Districts

Required Adjustments to Statewide Education Increment

Current TIF statute contains two mechanisms that adjust the amount of statewide education increment that may be retained by municipalities.

24 VSA §1896(b) requires OTV to be adjusted by a multiplier[13] in the event of a town-wide reappraisal. In addition, 24 VSA §1897(a) stipulates that no more than 75 percent of the statewide education increment may be retained by a municipality which means that at least 25 percent of statewide education increment is remitted to the state education fund.

According to the AG's office, these provisions were imposed to provide protection to the education fund revenues from the impact of tax increment financing. Further, DOT indicated that the legislature's intent in applying the multiplier adjustment may have been to incorporate the growth in TIF district property values that would have resulted absent any TIF district improvements. Theoretically, this adjusted OTV results in less statewide education increment retained by the municipality and more revenue being remitted to the state education fund.

Taken together, the impact of these two statutory provisions could be significant for a municipality.

Table 6 provides an illustrative example of the combined effect of applying the OTV multiplier adjustment and the 75 percent adjustment to the statewide education increment to determine how much statewide education increment may be retained by a municipality.

[13]TIF district properties' reappraised value divided by TIF district properties' values in year prior to reappraisal.

Appendix V
Observations Pertaining to Required Adjustments to the Statewide Education Increment and Audits of TIF Districts

Table 6: Illustration of Effect of OTV Multiplier Adjustment and 75 Percent Adjustment on Municipal Retention of Statewide Education Increment

Facts of Illustration	
OTV	$ 21,000,000
Most recent TIF district property values prior to reappraisal	$ 51,000,000
TIF district property values based on reappraisal	$ 65,000,000
OTV multiplier adjustment (24 VSA §1896(b)) (65,000,000/51,000,000)	1.27
Education tax rate	$1.00
Incremental Property Value Growth	
With no OTV multiplier adjustment (65,000,000-21,000,000)	$ 44,000,000
With OTV multiplier adjustment (65,000,000-(21,000,000*1.27))	$ 38,330,000
Statewide Education Increment Retained by Municipality	
With no adjustments (44,000,000/100 X $1)	$ 440,000
With OTV multiplier adjustment only (24 VSA §1896(b)) (38,330,000/100 X $1)	$ 383,300
With 75% limit on statewide education increment (24 VSA §1897(a)) ((44,000,000/100)*.75 X $1)	$ 330,000
With OTV multiplier adjustment and 75% limit on statewide education increment ((38,330,000/100)*.75)	$ 287,475

Audits of TIF districts

Existing statute[14] requires that SAO perform audits of all active TIF districts every four years. Based on knowledge gained during the course of the TIF district audits, we believe that modification of certain aspects of the audit requirement may reduce the cost of the audits and provide information to the legislature at key points in a TIF district's operations.

[14] 32 VSA §5404a (l), Act 190 (2008).

Designation of a dollar threshold that could be used to trigger a TIF district audit

Some of the TIF districts may not be significant in terms of the statewide education increment estimated to be used to finance public infrastructure improvements. Since the life of TIF districts may be fairly long, $1,000,000 of projected statewide education increment seems a reasonable threshold to establish. On average, this would represent $50,000 per year that would be redirected from the state education fund. Exempting certain districts from the TIF audit requirement would reduce overall audit costs of the TIF program.

The discretion to conduct an audit of any district, regardless of the projected statewide education increment, could be preserved in the event that the DOT, VEPC or the legislature has concerns about a TIF district that falls below the threshold.

Modification of the frequency and scope of the audits

The requirement to audit TIF districts every four years may result in an overly large number of audits, rather than ensuring that the audits occur at key phases of a TIF district's operation. We suggest that the timing of required audits be linked to specific phases (see table 7), which would have the added benefit of reducing the scope of any single audit and thus reduce the cost.

Table 7: Key Phases of TIF Districts and Suggested Audit Timing

Phase	Timing	Likely Audit Scope
Phase I	At completion of construction of public infrastructure improvements	Validate that expenditures were for public infrastructure improvements approved by VEPC, that the debt utilized to finance the construction was a form of financing allowed per the TIF statutes and that the municipality has implemented a process to correctly derive the statewide education increment.
Phase II	Midway through debt repayment	Confirm that appropriate amount of statewide education increment was retained by municipality and that it was utilized to pay for authorized debt.
Phase III	Termination of TIF district	Update to Phase II and confirm that any statewide education increment retained by municipality that was not used to repay debt or pay for improvements in the TIF district was returned to the requisite taxing authority (i.e., municipality or state).

Systematically aligning the audit requirement with the key phases, rather than requiring an audit every four years, will better capture the time periods when the greatest potential risk of errors or manipulation exists. It is a standard audit practice to focus audit efforts to address risk.

Appendix VI
Response of Chief Assistant Attorney General

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December 19, 2012

Thomas M. Salmon, CPA, CFE
State Auditor
Office of the State Auditor
132 State Street
Montpelier, VT 05633-5101

Re: Draft Report of the Vermont State Auditor on Tax Increment Financing

Dear Mr. Salmon,

Thank you for sending us your Draft Report on Tax Increment Financing ("TIF") and for inviting comments on your findings, conclusions and recommendations. The Draft summarizes the results of several TIF district audits and discusses issues identified in the course of the audits. The Attorney General's Office consulted with your staff on the statutory issues discussed in the Draft, and we are in agreement with your findings, conclusions and recommendations on the statutory issues.

For example, the Office agrees with your finding that several provisions in the TIF statutes are ambiguous or inconsistent with one another. Table 4 on pages 9 - 11 of the Draft Report lists eighteen statutory sections and subsections that are subject to interpretation and debate. As noted in the Draft Report, these ambiguities and inconsistencies complicate the administration and oversight of TIF districts.

We also agree with your finding that the statutes do not provide adequate state oversight of the TIF program. For example, the statutes do not designate an executive or legislative agency to oversee the administration of TIF districts. *See* Draft at p. 7 ("[T]he statute does not specify whether VEPC or any other state entity has responsibility for oversight of TIF districts subsequent to the initial application for approval."). They do not grant any agency the statutory authority to assure the proper allocation of education property taxes to the education fund. *See* Draft at p. 14 ("[T]here is no state entity ... to verify whether a municipality has

Appendix VI
Response of Chief Assistant Attorney General

retained the appropriate amount of statewide education increment and directed an appropriate amount to the education fund.").

We also agree with your finding that the statutes do not provide specific remedies to address miscalculations of TIF increments and resulting shortfalls in municipal payments to the education fund. *See* Draft at p. 15. For example, the laws do not establish a legislative or administrative process for resolving disagreements about sometimes ambiguous statutes. They do not authorize any state official to make the education fund whole by applying offsets against state payments to municipalities for education or other purposes.

Finally, the Office agrees with your suggestion that certain legislative measures might be appropriate. *See* Draft at pp. 16 and 17 (Conclusion and Recommendations). The Legislature could resolve some immediate issues by determining whether and how underpayments to the education fund might be remedied and could provide guidance to municipal and state officials on the administration and oversight of TIF districts going forward. The Legislature could reconcile TIF laws that now appear in the Vermont Statutes, in the Session Laws and in Municipal Charters, and consolidate them in one place.

A legislative review of these laws should also consider the relation between tax increment financing and education funding. This connection was noted in your Draft Report and also in an earlier report prepared by the Tax Department and the Joint Fiscal Office. *See* Tax/JFC Report (2009) at p. 3 (citing "the unusual nature of TIF in the context of a statewide education tax system"). The legal consideration is that tax increment financing must be structured in a way that does not upset the equality of education funding mandated by the *Brigham* decision and by the education funding laws enacted to comply with that decision.

Your staff have obviously done a very thorough job on the district audits and on the overall report. They are to be commended for their work.

Very truly yours,

William E. Griffin
Chief Assistant Attorney General

Appendix VII
Response of Secretary of the Agency of Commerce and Community Development, Director of VEPC and Commissioner of DOT

State of Vermont
Department of Taxes
133 State Street
Montpelier, VT 05633-1401

Agency of Administration

December 21, 2012

Tanya Morehouse, Chief Auditor
State Auditor's Office
132 State Street
Montpelier, Vermont 05633-5101

Re: Comments to TIF Capstone Report

Dear Tanya,

The Agency of Commerce and Community Development, Vermont Economic Progress Council and The Department of Taxes appreciates the diligence of the State Auditor's Office (SAO) in producing this capstone report. The Administration is in general agreement with the findings and conclusions of this report. The Administration agrees with the recommendations for specific statutory clarifying provisions.

The Administration agrees generally that the matter of oversight and enforcement needs to be addressed for TIFs. However, The Administration is concerned that some solutions might require an inordinate amount of state resource. Specifically, the public fisc must be protected, but any type of oversight and enforcement that puts the TIF towns and state administrators in a consistently adversarial, potentially litigious, relationship over the use of tax money should be avoided.

The Administration recommends that the legislature consider leveraging the current audit procedures with modern alternative dispute resolution mechanisms to balance the need for accountability in a resource constrained context.

Sincerely,

Lawrence Miller, Secretary, Agency of Commerce and Community Development

Fred Kenney, Director, Vermont Economic Progress Council

Mary Peterson, Commissioner, Department of Taxes

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