Study of the Metropolitan Area Fiscal Disparities Program

EXECUTIVE SUMMARY

Prepared for:

MINNESOTA DEPARTMENT OF REVENUE

February 13, 2012 ***(revised)***

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This study was prepared by TischlerBise for the Minnesota Department of Revenue.

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Disclaimer
The analysis and findings conveyed in this report are that of TischlerBise, the authors of the study, unless otherwise noted. Any errors are the responsibility of the authors.

Per Minnesota Statutes, section 3.197, any report to the legislature must contain, at the beginning of the report, the cost of preparing the report, including any costs incurred by another agency of another level of government.

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Note: A previous version of this report contained data errors (in tax rates and taxes paid) that have been corrected.

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** The chapter on property tax, aid, and local development programs that interact with Fiscal Disparities program was written by Minnesota Department of Revenue.*

Executive Summary: Study of the Metropolitan Area Fiscal Disparities Program

For the Minnesota Department of Revenue

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I. EXECUTIVE SUMMARY

OVERVIEW OF THE STUDY

TischlerBise has been retained by the Minnesota Department of Revenue to analyze the Twin Cities Metropolitan Area Fiscal Disparities Program. The "Charles R. Weaver Metropolitan Revenue Distribution Act" enacted in 1971, commonly referred to as the Metropolitan Fiscal Disparities program, was an attempt to address growing fiscal concerns within the seven-county Minneapolis-St. Paul region, home to over 180 cities and townships, over 60 school districts, and dozens of other taxing authorities. The law requires all communities in the seven-county area to contribute 40 percent of the growth in their commercial/industrial tax base (from 1971) to a regional pool.

The objectives of the Program as stated in the original Act were as follows:

- To provide a way for local governments to share in the resources generated by the growth of the area, without removing any resources that local governments already have.
- To increase the likelihood of orderly urban development by reducing the impact of fiscal considerations on the location of business and residential growth and of highways, transit facilities, and airports.
- To establish incentives for all parts of the area to work for the growth of the area as a whole.
- To provide a way whereby the area's resources can be made available within and through the existing system of local governments and local decision making.
- To help communities in different stages of development by making resources increasingly available to communities at those early stages of development and redevelopment when financial pressures on them are the greatest.
- To encourage protection of the environment by reducing the impact of fiscal considerations so that flood plains can be protected and land for parks and open space can be preserved.

These objectives have been commonly reduced to two main goals:[1]

- *Promoting more orderly regional development.*
- *Improving equity in the distribution of fiscal resources.*

This report seeks to provide information and analysis on:

- Growth trends in the Twin Cities metro region;
- Fiscal and economic conditions in the region;
- The basics of the Fiscal Disparities program including what has been said about it in the past and today, what the trends have been regarding tax capacity, tax rates, and residential homestead burden, and what the changes would be if the program were eliminated particularly on tax rates, taxes paid, and residential homestead burden;
- The potential "overburden" on jurisdictions—including the major local taxing jurisdictions (city, county, school)—from different types of land uses both under the current taxation system (with Fiscal Disparities) and a hypothetical scenario if the program were eliminated; and
- Major policy considerations addressing criticisms, issues, and praise for the program.

THE REGION

The Fiscal Disparities Program in the Minneapolis-St. Paul region includes seven counties and is home to over 180 cities and townships; over 60 school districts; and dozens of other taxing authorities. While the region has expanded in recent years in terms of economic reach, market area, and commuting patterns—as evident by the U.S. Census metropolitan statistical area (MSA) expansion from 5 to 13 counties from 1971 to 2009—the Fiscal Disparities Program by law includes only the jurisdictions within the seven-county region.

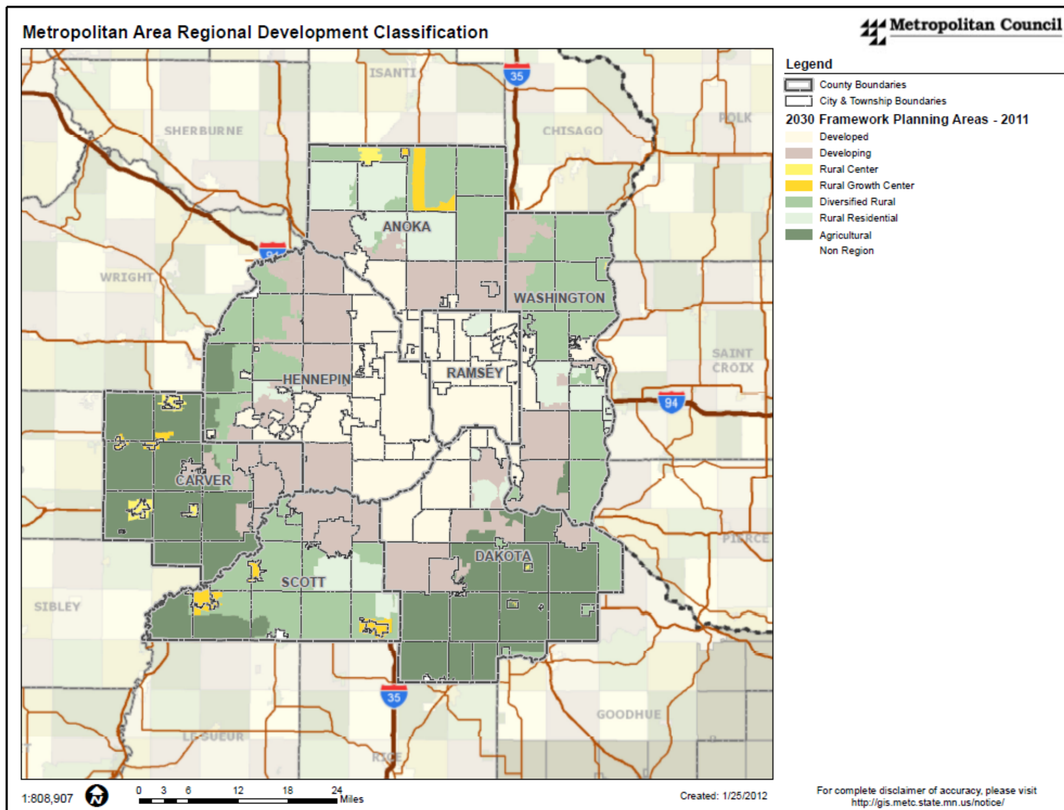
This study primarily uses three groupings to describe and discuss the jurisdictions included in the Fiscal Disparities Program.

- First, we group by County for the seven-county region: Anoka, Carver, Dakota, Hennepin, Ramsey, Scott, and Washington.

[1] Hinze and Baker, 2005.

- The second grouping is the Metropolitan Council's regional development classifications or planning areas,[2] which provide a way to group localities by development characteristics in a way that geographic classifications do not. (See map below.) The groups are:
  - Central City
  - Developed Area
  - Developing Area
  - Rural Area
  - Rural Growth Center

Figure 1. Metropolitan Council Regional Development Classification



- The third and final grouping is by Fiscal Disparities status as a *net contributor* or *net recipient*.

[2] Regional development framework classifications or planning areas used in this study are the Metropolitan Council designations as of 2011. The designations were originally established in 2004.

GROWTH TRENDS

The seven-county metropolitan region has grown significantly from 1970 to today. The current estimate of total population is approximately 2.85 million. This reflects an increase of almost 1 million people since 1970. Hennepin and Ramsey counties—while still the most populous counties in the region—comprise a smaller share of the regional population in 2010 when compared to 1970.

Additional detail is provided below in Figure 2, depicting the absolute growth and percentage increase in population from 1970 to 2010. As shown, the highest percentage growth occurred in Scott County followed by Carver and Washington counties. The lowest percentage growth occurred in Ramsey and Hennepin counties.

Figure 2. Population Growth by County: 1970 to 2010

	Population		Population Growth or Decline From 1970 to 2010		
	1970	2010	Increase/Decrease	% Total Growth	% Avg Ann Growth
Anoka	154,815	331,022	176,207	113.8%	2.8%
Carver	27,652	91,042	63,390	229.2%	5.7%
Dakota	139,824	397,405	257,581	184.2%	4.6%
Hennepin	962,393	1,155,495	193,102	20.1%	0.5%
Ramsey	473,822	505,795	31,973	6.7%	0.2%
Scott	32,423	129,928	97,505	300.7%	7.5%
Washington	79,980	237,733	157,753	197.2%	4.9%
Grand Total	***1,870,909***	***2,848,420***	***977,511***	***52.2%***	***1.3%***

Source: Census data via Metropolitan Council; analysis by TischlerBise

Grouping metropolitan area communities into regional development classifications reveals that population in the Central Cities has decreased from 1970 to 2010 by a little over 10 percent, which is a decrease of approximately .3 percent per year when averaged over the 40-year time period. At the other end of the continuum are Developing Areas, which saw an increase in population of over 350 percent from 1970 to 2010. This reflects a 9 percent average annual growth rate over the 40-year time period.

Figure 3. Population Growth by Regional Development Classification: 1970 to 2010

	Population		Population Growth or Decline From 1970 to 2010		
	1970	2010	Increase/Decrease	% Total Growth	% Avg Ann Growth
Central Cities	744,266	667,646	-76,620	-10.3%	-0.3%
Developed Area	873,808	1,184,186	310,378	35.5%	0.9%
Developing Area	180,660	823,895	643,235	356.0%	8.9%
Rural Areas	53,981	116,813	62,832	116.4%	2.9%
Rural Growth Centers	13,641	49,255	35,614	261.1%	6.5%
Excluded from FD	4,553	6,625	2,072	45.5%	1.1%
Grand Total	***1,870,909***	***2,848,420***	***977,511***	***52.2%***	***1.3%***

Source: Census data via Metropolitan Council; analysis by TischlerBise

Employment in the region has also grown significantly, essentially doubling from 1970 to today. The current estimate of total number of jobs in the seven-county study region is approximately 1.5 million. Hennepin and Ramsey counties contain the largest number of jobs in the region, but have declined in regional share relative to the other counties (combined comprising 73 percent of jobs in the region down from 89 percent in 1970).

As shown below, the highest percent of growth occurred in Carver County followed by Scott, Dakota, and Washington counties. The largest absolute gain in employment occurred in Hennepin County following by Dakota County. The lowest percentage increase occurred in Ramsey County.

Figure 4. Employment Growth by County: 1970 to 2010

	Jobs		Job Growth From 1970 to 2010		
	1970	**2010**	*Increase/Decrease*	*% Total Growth*	*% Avg Ann Growth*
Anoka	29,170	107,074	*77,904*	*267.1%*	6.7%
Carver	4,120	32,955	*28,835*	*699.9%*	17.5%
Dakota	31,100	169,360	*138,260*	*444.6%*	11.1%
Hennepin	463,090	804,056	*340,966*	*73.6%*	1.8%
Ramsey	230,240	314,347	*84,107*	*36.5%*	0.9%
Scott	6,820	41,557	*34,737*	*509.3%*	12.7%
Washington	14,370	71,454	*57,084*	*397.2%*	9.9%
Grand Total	***778,910***	***1,540,803***	***761,893***	***97.8%***	***2.4%***

Grouping employment data into regional development classifications shows that all areas added jobs since 1970 with Developing Areas adding the second largest number of jobs (behind Developed Areas) with the highest growth rate. Rural Areas also added jobs at a high growth rate, mainly because the initial number of jobs is so low. Central Cities added jobs, but at a much lower growth rate than all other areas.

Figure 5. Employment Growth by Regional Development Classification: 1970 to 2010

	Jobs		Job Growth From 1970 to 2010		
	1970	**2010**	*Increase/Decrease*	*% Total Growth*	*% Avg Ann Growth*
Central Cities	435,580	456,798	*21,218*	*4.9%*	0.1%
Developed Area	288,550	712,372	*423,822*	*146.9%*	3.7%
Developing Area	36,440	320,367	*283,927*	*779.2%*	19.5%
Rural Areas	2,060	16,272	*14,212*	*689.9%*	17.2%
Rural Growth Centers	2,020	9,237	*7,217*	*357.3%*	8.9%
Excluded from FD	14,140	25,757	*11,617*	*82.2%*	2.1%
Grand Total	***778,790***	***1,540,803***	***762,013***	***97.8%***	***2.4%***

Source: Data from Metropolitan Council and MN Dept. of Employment and Economic Development; analysis by TischlerBise

More recent job growth data is shown below from 2000 to 2009. During the recent recession with overall job losses experienced in the region as a whole, it is interesting to note that both the Developing Areas and Rural Areas have added jobs while Central Cities and Developed Areas have lost jobs. See Figure 6.

Figure 6. Employment Growth by Regional Development Classification: 2000 to 2009

	2000 (2nd Qtr)	2009 (2nd Qtr)	Gain (Loss)	% Gain/Loss
Central Cities	496,251	458,026	(38,225)	-7.7%
Developed Areas	709,258	652,577	(56,681)	-8.0%
Developing Areas	374,295	410,827	36,532	**9.8%**
Rural Areas	23,628	25,726	2,098	**8.9%**
Rural Centers	*9,451*	*9,762*	*311*	*3.3%*
Other Rural	*14,177*	*15,964*	*1,787*	*12.6%*
Metro Council Regional Total	1,603,432	1,547,156	(56,276)	-3.5%

Note: All Metro localities are included in one of the categories (unlike above tables with an "Excluded from FD" group).
Source: Metro Council Data; analysis by TischlerBise.

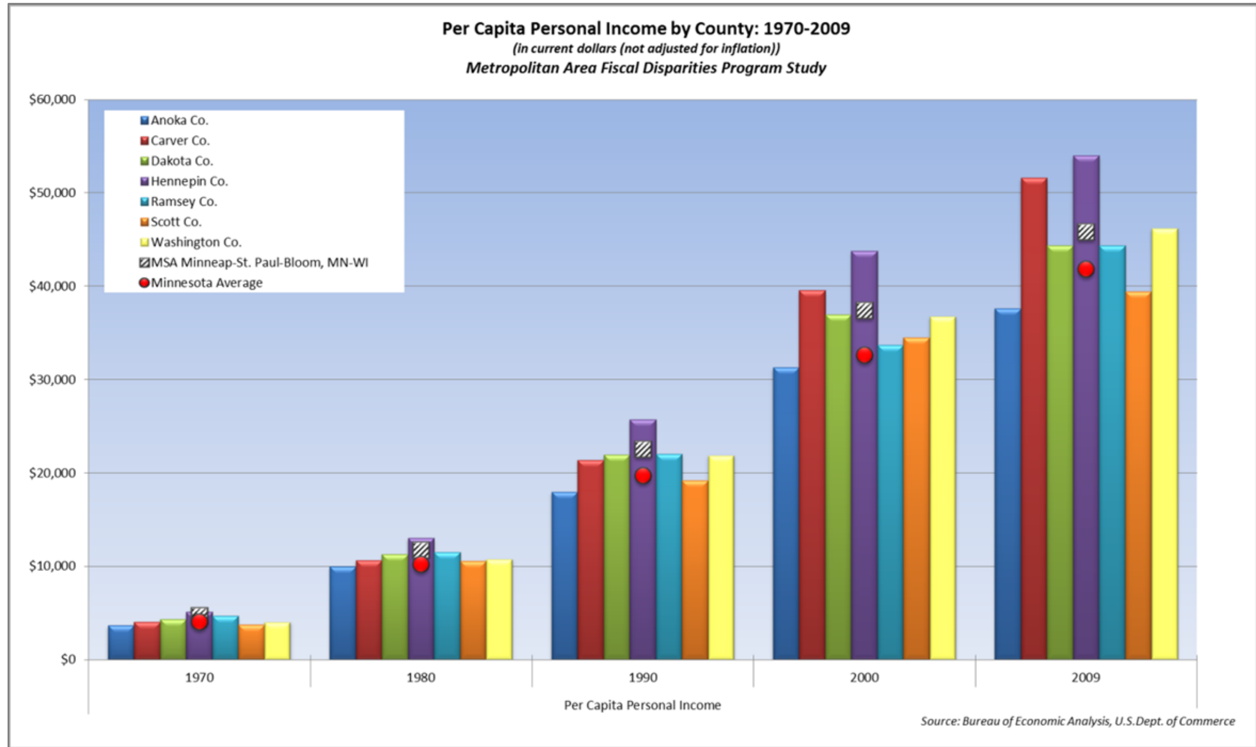
ECONOMIC AND TAX BASE TRENDS

To provide further context of economic and tax base trends in the region, we examine other economic and fiscal factors in this study such as personal income, wages, gross domestic product (GDP) by MSA, and tax base composition.

Economic Trends

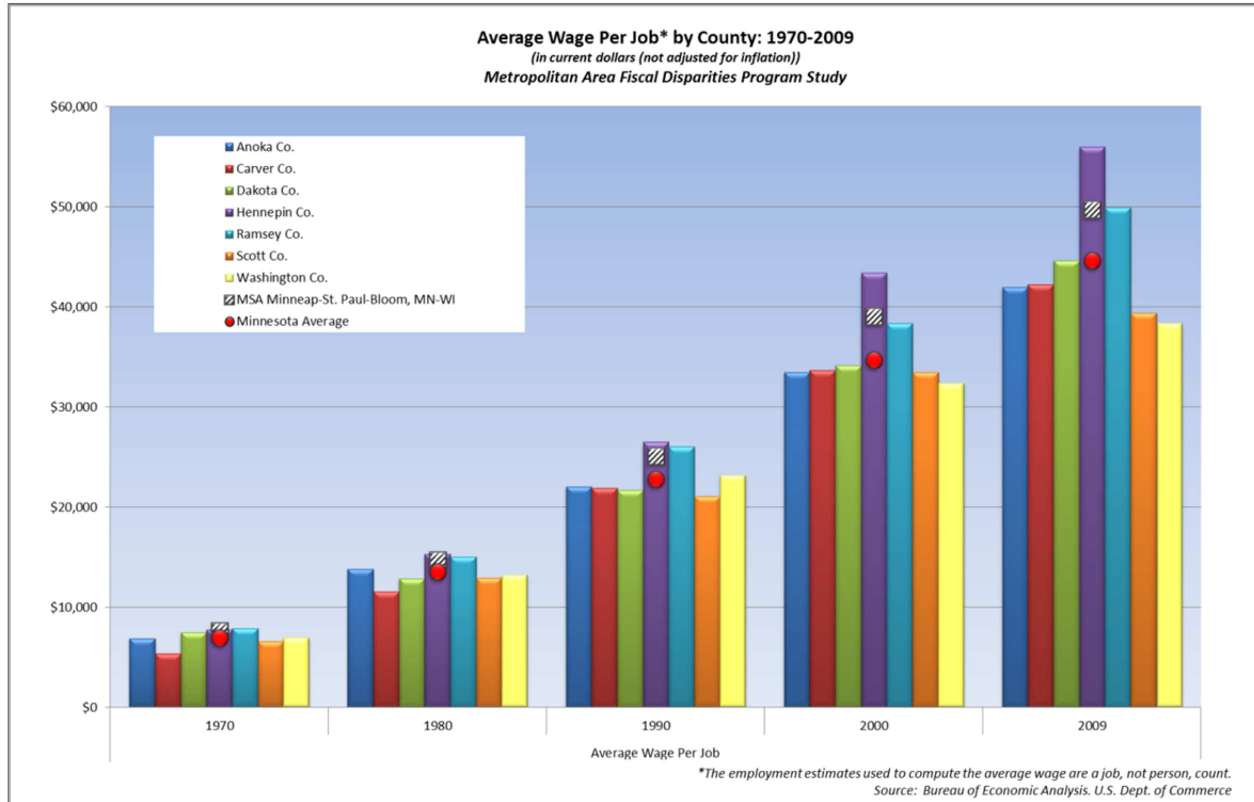
Personal income by *place of residence* is shown below in Figure 7. (Data shown are in current dollars; that is, not adjusted for inflation.) Over the past 40 years, personal income levels have varied when comparing counties in the region. Hennepin County has consistently had the highest per capita income in the region with Anoka County having the lowest. Most of the counties are higher than the Minnesota average with Anoka and Scott counties hovering at or below the state average.

Figure 7. Per Capita Personal Income by County: 1970 to 2009



Another factor to examine is wage and salary data by *place of employment*. Figure 8shows average wages per job by County location, reflecting where the job is located as opposed to where workers live. (Data shown are in current dollars; that is, not adjusted for inflation.) Aside from 1970, Hennepin County has had the highest average wages per job in the region. Ramsey County has ranked second in all years except 1970 when it was ranked first. The county with the lowest average wages per job has changed over time with Carver County ranking at the bottom in 1970 and Washington County in 2009.

Figure 8. Average Wage Per Job by County: 1970 to 2009



Tax Base Composition

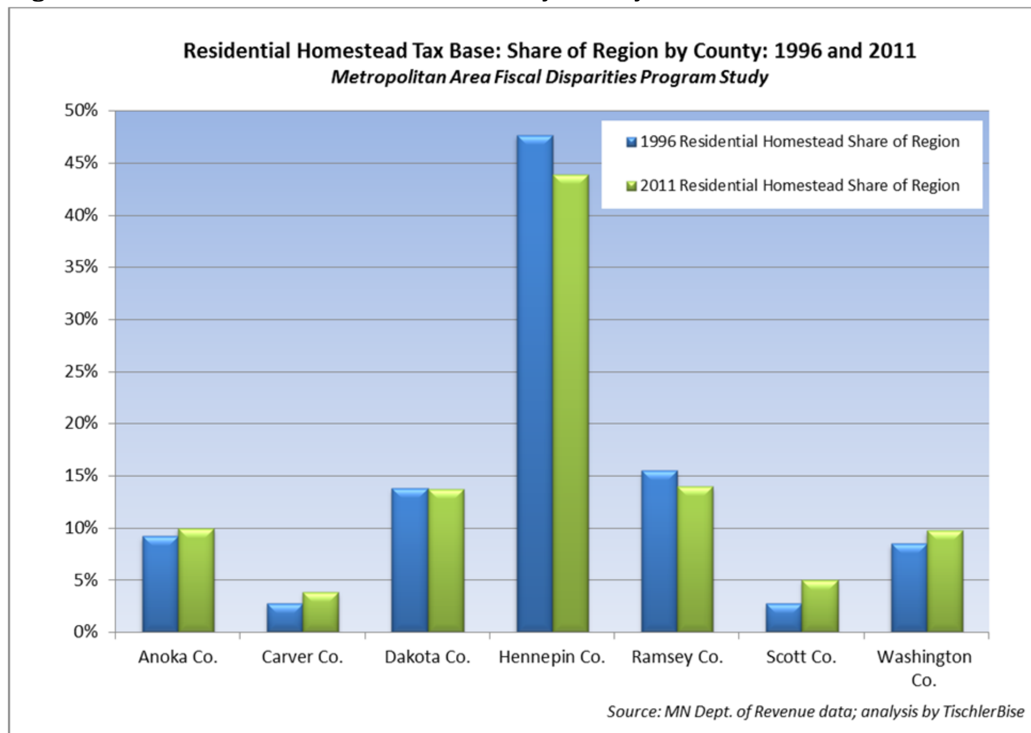
Tax base composition was also evaluated to understand fiscal conditions in the region and changes over time. Results are presented in the body of the report by county for 1996 and 2011 showing the dollar amounts and share by type of tax capacity[3] (residential homestead, commercial/industrial, and other). In 1996, tax base in the region was generally evenly split between residential homestead and commercial/industrial properties. Hennepin and Ramsey counties were the only counties with a higher percentage of the tax base in commercial/industrial property, however counties had a range of 40 to 60 percent of its tax capacity from residential homestead property. The characteristics of the tax base has shifted by2011, partly due to state policy changes, especially from 1997 to 2002, that significantly changed class rates to reduce C/I tax base relative to residential homestead tax base. In 2011, all counties have a majority of its tax capacity from residential homestead properties with most counties

[3] Tax capacity is based on a property's market value and the state-mandated classification system by land use type (e.g., residential homestead property under $500,000 has a class rate of 1.0 percent compared to a commercial/industrial property with a class rate of 1.5 percent for the first $150,000 in value and 2 percent over $150,000.).

now having anywhere from 50 to 64 percent of their tax capacity from residential homestead properties.

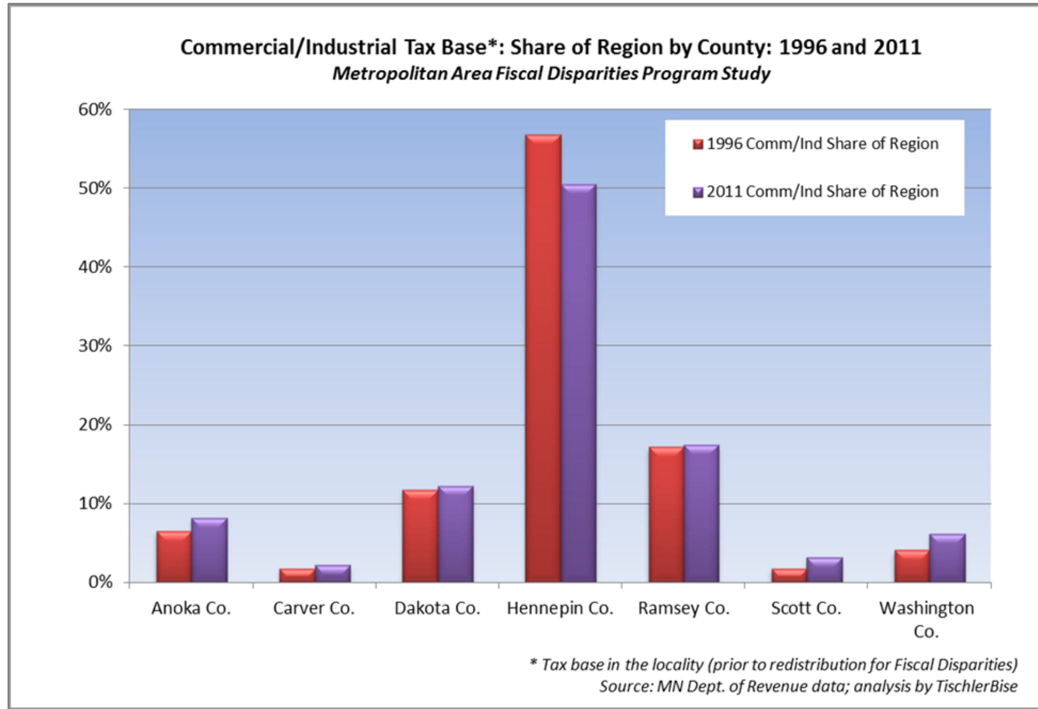
County data was analyzed for 1996 and 2011 looking at each county's share of the regional total and how that may have changed over time. For residential homestead tax capacity, most counties have maintained the same approximate share of the regional total from 1996 to 2011 with the exception of Hennepin County (with a 3.8 percent *decrease* in regional share) and Scott County (with a 2.2 percent *increase* in regional share). See Figure 9.

Figure 9. Residential Homestead Tax Base by County: 1996 and 2011



For commercial/industrial tax capacity (before Fiscal Disparities distributions), Hennepin County has lost 6.3 percent of its regional share from 1996. All other counties have either retained or increased their share since 1996. Counties that have increased their regional share of commercial/industrial tax capacity by over 1 percent are Anoka, Scott, and Washington counties. See Figure 10.

Figure 10. Commercial/Industrial Tax Base by County: 1996 and 2011

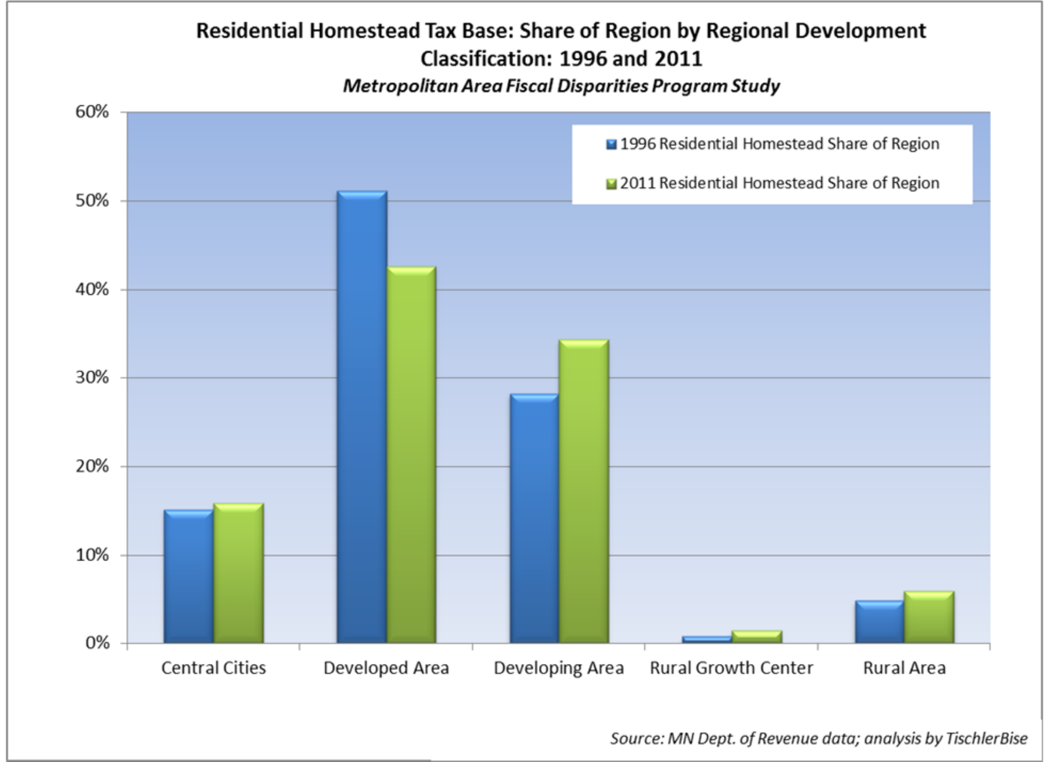


The above analysis was replicated using the regional development classifications. In 1996, Central Cities and Developed Areas had the majority of their tax capacity from commercial/industrial property. As one moves down the development classification continuum from more developed (Central Cities) to less (Rural Areas), the share in commercial/industrial properties decreases, as one would expect.

In 2011, characteristics of the tax base have shifted by2011, partly due to state policy changes, especially from 1997 to 2002, that significantly changed class rates to reduce C/I tax base relative to residential homestead tax base. However, the general relationship holds that as one moves down the development classification continuum from more to less developed, the share in commercial/industrial properties decreases, as one would expect.

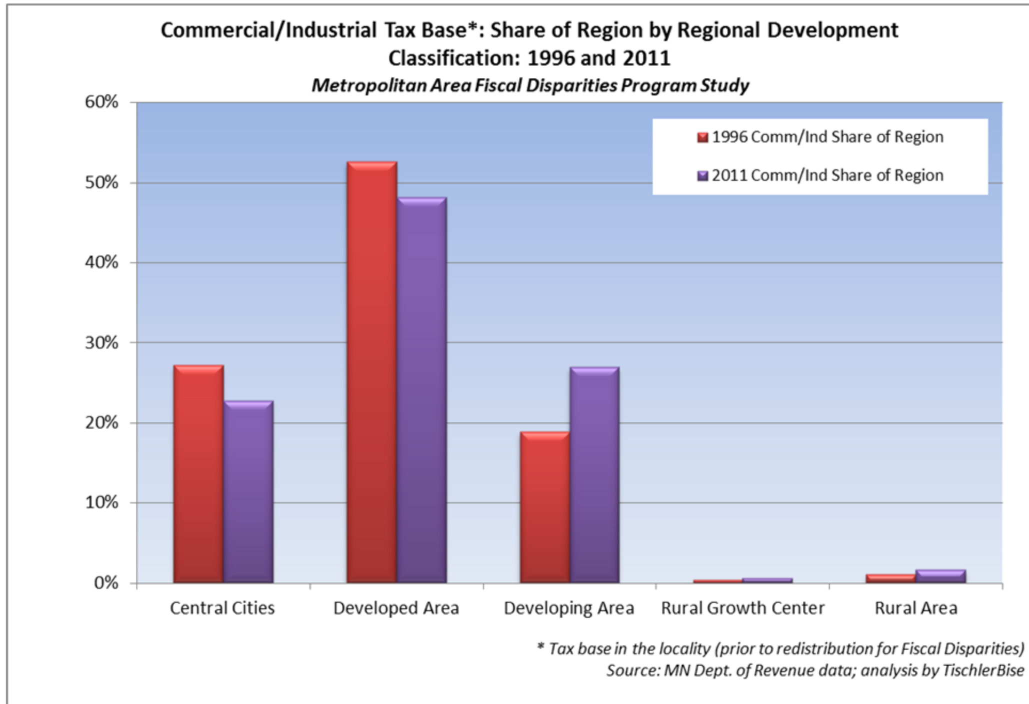
As was done by county, regional development classification groupings were analyzed for 1996 and 2011 to evaluate the share of tax capacity out of the regional total and how that may have changed over time. For residential homestead tax capacity, most areas have maintained the same approximate share of the regional total from 1996 to 2011 with the exception of Developed Areas (with a 9 percent *decrease* in regional share) and Developing Areas (with a 6 percent *increase* in regional share). See below.

Figure 11. Residential Homestead Tax Base by Regional Development Classification: 1996 and 2011



For commercial/industrial tax base (before Fiscal Disparities distributions), Central Cities and Developed Areas have each lost 4 percent of their regional share with Developing Areas gaining 8 percent. This reflects the development trends discussed above (and in further detail in the body of the report) regarding the outward growth of employment. See Figure.

Figure 12. Commercial/Industrial Tax Base by Regional Development Classification: 1996 and 2011



PROPERTY TAX, AID, AND LOCAL DEVELOPMENT PROGRAMS THAT INTERACT WITH FISCAL DISPARITIES

The report provides a description of a range of property tax, aid, and local development programs that are in existence in Minnesota and available to local governments. The following are discussed in the body of the report:

- Category I: Classification and Other Tax Base Features
  - Classification
  - Homestead Market Value Exclusion

- Category II: Aids and Refunds
  - Local Government Aid
  - County Program Aid
  - Property Tax Refund
  - Disparity Reduction Aid

- Category III: TIF and Economic Development
  - Tax Increment Financing
  - Economic Development Abatements
  - Metro Vacant Land Plat Law

- Category IV: Open Space Preservation and Conservation
  - Green Acres Program
  - Rural Preserve Program
  - Ag Preserves Credit
  - Open Space Property
  - Agricultural Homestead Market Value Credit
  - Payments in Lieu of Taxes (PILT)
  - Sustainable Forest Incentive Act

FISCAL DISPARITIES PROGRAM OVERVIEW

The Minnesota Fiscal Disparities Act of 1971 was an attempt to address growing fiscal concerns within the seven-county Minneapolis-St. Paul region. The law, which took effect 35 years ago after surviving two court challenges, required all communities in the seven-county area to contribute 40 percent of the growth after 1971 in their commercial-industrial tax base to a regional pool. By 2011, the Fiscal Disparities program included $420.7 million of shared tax base resulting in $544.1 million in tax revenue generated across all taxing jurisdictions.[4]

The distribution of the pool is based on fiscal capacity, defined as equalized market value per capita. This means that:

- If the municipality's fiscal capacity is the same as the metropolitan average, its percentage share of the pool will be the same as its share of the area's population;
- If its fiscal capacity is above the metro average, its share will be smaller; and
- If its fiscal capacity is below the metro average, its share will be larger.[5]

All units of local government in the Fiscal Disparities program are participants, including cities, counties, school districts, and special districts. Each jurisdiction determines its levy needs (i.e., the amount of property taxes needed to provide its desired level of services) and then determines the property tax rate based on the levy and net tax capacity in the taxing unit. Without the Fiscal Disparities program, the rate would be determined based on the tax base of the jurisdiction, with no contribution or distribution of tax base. With the Fiscal Disparities program, the tax rate—and burden—is determined based on an adjusted net tax capacity. Taxpayers in jurisdictions contributing more than they receive (net contributors), pay more than their jurisdiction's levy, and those receiving more than they contribute (net recipients) pay less.[6]

[4] Metropolitan Council.
[5] Hinze and Baker, 2005.
[6] From Hinze and Baker, 2005; this report also provides a detailed description of the Fiscal Disparities formula.

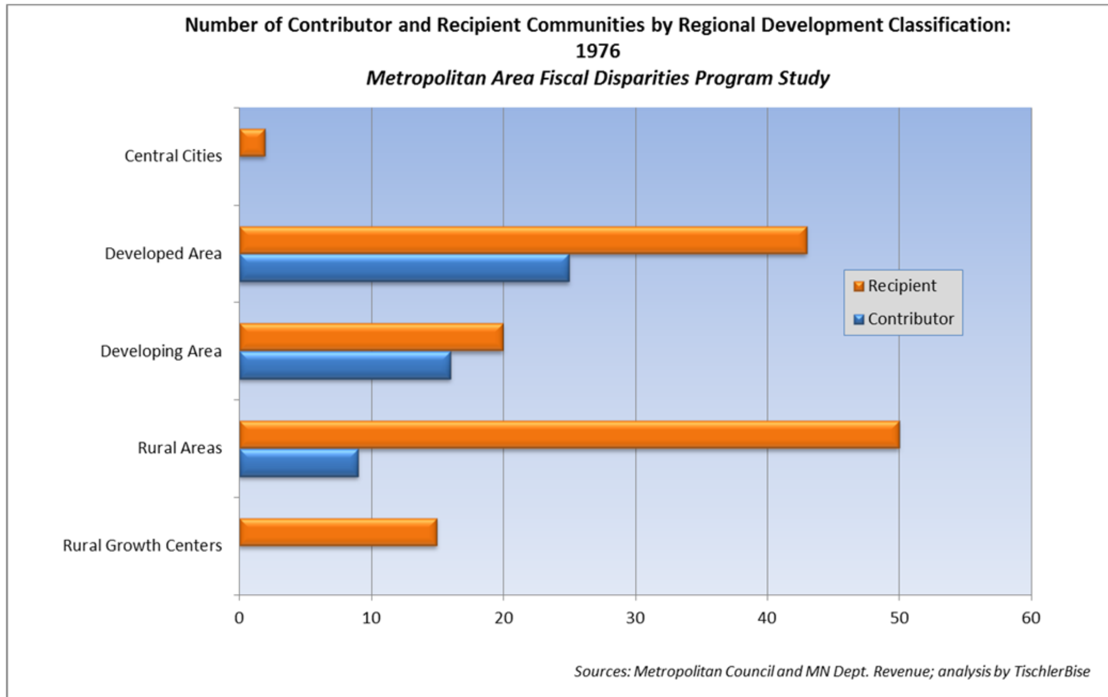
FISCAL DISPARITIES PROGRAM TRENDS

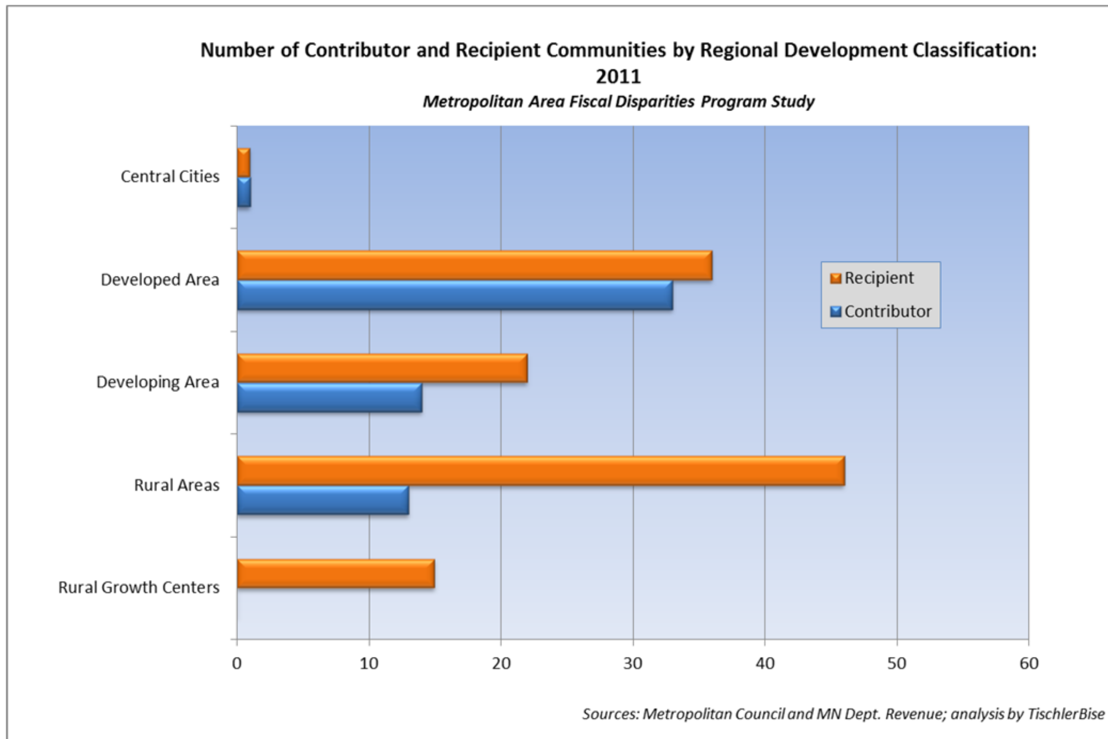
Jurisdictions that contribute more in tax base than they receive are known as “net contributors” and those that contribute less tax base than they receive are known as “net recipients.” Figure 13provides further detail on the types of communities that are net contributors or net recipients comparing the start of the program, 1976to 2011.[7] The comparison reveals the following:

- Central Cities (for which there are two) have typically been either all recipients or split with Minneapolis as a net contributor and St. Paul as a net recipient.
- Developed Areas in 2011 are almost evenly split between recipients and contributors with recipients outnumbering contributors only slightly, which is a change from 1976 where recipients outnumbered contributors by a factor of 1.7.
- The number of Developing Area communities in either category has remained relatively constant when comparing 1976 to 2011 with net recipients outnumbering contributors in both years.
- For Rural Areas, the relationship of recipients to contributors has changed from 1976, where the ratio of recipients to contributors was 5.5. In 2011, the ratio has decreased to 3.5.
- All Rural Growth Centers are net recipients in 2011, as they were in 1976 as well.

[7] The regional development classifications were designated in 2004 and therefore were not in existence in 1976. However, as is done elsewhere in this study, we group the municipalities in these classifications for comparison purposes.

Figure 13. Number of Recipients and Contributors by Regional Development Classification: 1976 and 2011





Impacts if the Fiscal Disparities Program Were Eliminated

We then examine the impact to tax capacities if the program had not been in existence in 1996 as well as today (2011). We also evaluate the impact to taxes paid and tax rates in 2011 if the program were eliminated.

Impact on Tax Capacity

Per capita commercial/industrial tax capacities are evaluated with and without the Fiscal Disparities Program to enable a comparison among counties. The first set of figures is C/I tax capacity per person by County compared to the regional average.

Figure 14. Commercial/Industrial Tax Capacity Per Capita with and without the Fiscal Disparities Program by County: 1996

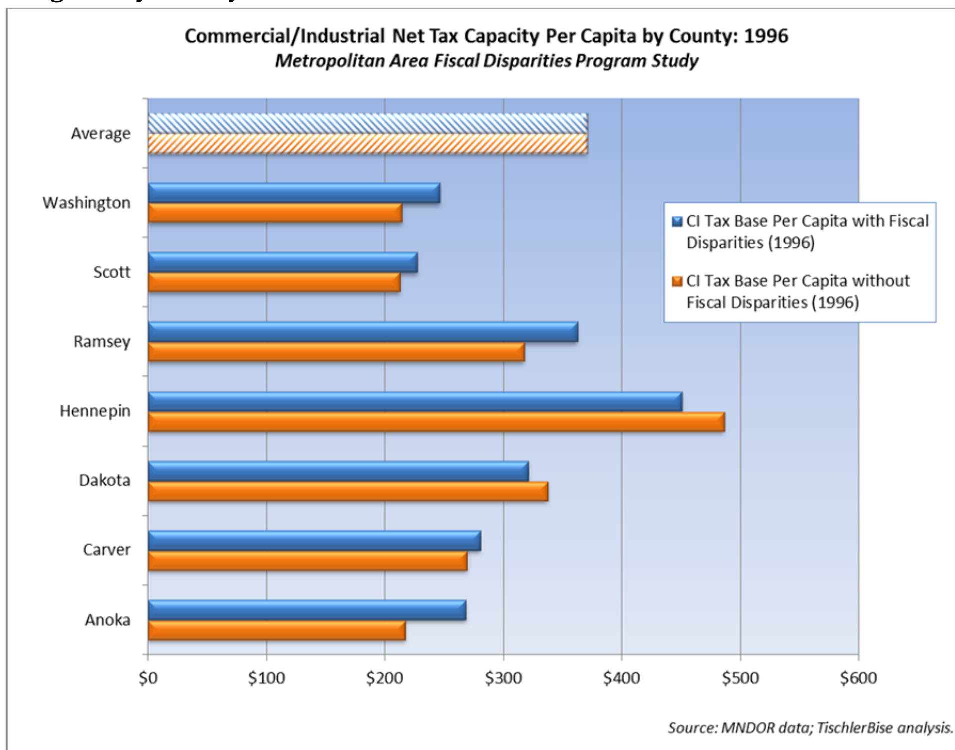
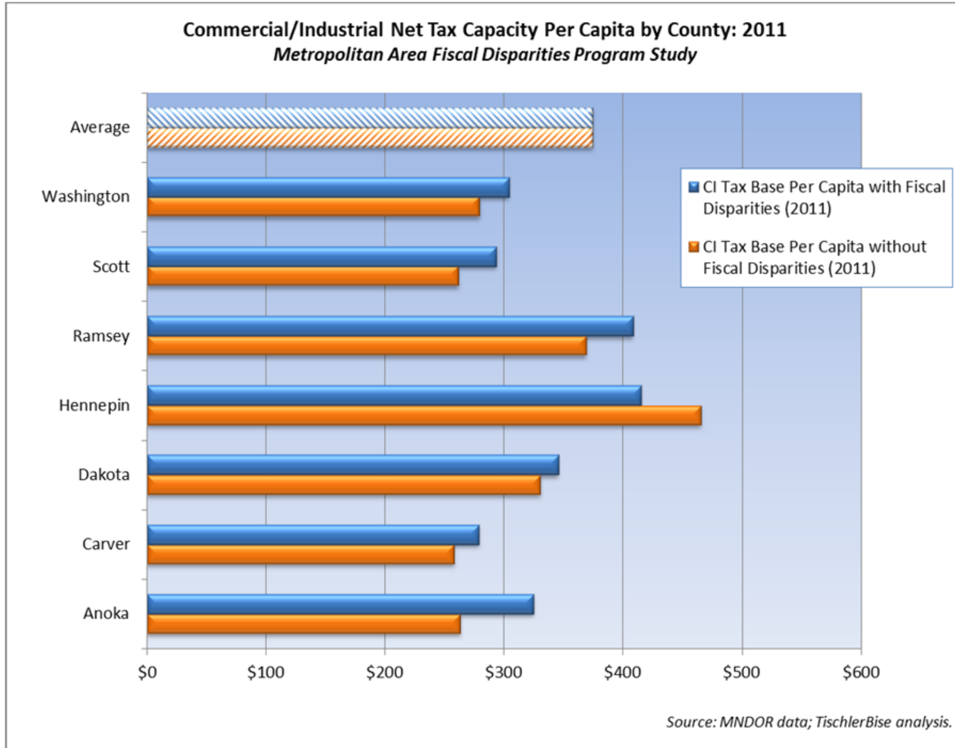


Figure 15. Commercial/Industrial Tax Capacity Per Capita with and without the Fiscal Disparities Program by County: 2011



The average C/I tax capacity per person has remained constant from 1996 to 2011 at around $370 per person.[8] In 1996, Hennepin County was the only county with *above average* per capita figures both with and without the Fiscal Disparities Program. In 1996, Hennepin and Dakota counties were net contributors, therefore with the Fiscal Disparities Program both have a lower per capita amount with the program in effect than each would if the program were eliminated.

In 2011, Hennepin County still has a higher than average per capita amount, under both scenarios—with and without the program. Ramsey County also has a higher than average per capita amount with the Fiscal Disparities Program and a lower than average amount if the program were eliminated. If the program were eliminated, Hennepin County's per capita value would increase by 12 percent, and all other counties would decrease in total by approximately 11 percent.

Impact on Taxes Paid and Tax Rates

One of the questions addressed in this study is the impact on taxes paid and tax rates if the program were to be eliminated. The impact on taxes paid is shown below in the following figures. The data

[8] The property tax reforms from 1997 to 2002 contributed to lowered Commercial/Industrial tax capacities, therefore even with population increasing, the average value per person remains at around the 1996 level.

reflects the amount of taxes paid within each group to **all taxing jurisdictions**, including city, county, schools, state, and any applicable special districts.[9] The assumption regarding the taxes paid with "FD Eliminated' is that there is **no change in the levy amount.** In reality, a jurisdiction is likely to adjust the levy, particularly in localities that would see a significant increase in tax rates as a result of elimination of the program.

Results by County

Results are first presented grouped by county for *taxes paid* and then implications to tax rates if the Fiscal Disparities Program were eliminated. All dollars are shown in thousands for Taxes Payable 2011.

In total, Hennepin County would see the largest percentage decrease (at 2.6 percent) and Anoka County would see the largest increase (at 5.6 percent) if the program were eliminated. The body of the report provides detail on the impact to residential homestead and commercial/industrial properties separately.

Figure 16. Total Taxes Paid with and without the Fiscal Disparities Program by County: 2011

	TOTAL *Taxes Payable 2011 (in $1,000s)*		***TOTAL Increase/Decrease***
County Name	Current Taxes	Taxes with FD Eliminated	Without FD
Anoka	$443,720	$468,665	*5.6%*
Carver	$159,383	$160,606	0.8%
Dakota	$597,704	$598,630	0.2%
Hennepin	$2,535,884	$2,470,867	*-2.6%*
Ramsey	$802,964	$834,111	3.9%
Scott	$204,666	$208,669	2.0%
Washington	$357,293	$358,993	0.5%
Grand Total	***$5,101,614***	***$5,100,541***	***0.0%***

Source: MN Dept. of Revenue data.

Implications to *tax rates* if the Fiscal Disparities Program were eliminated are evaluated as well and grouped by county. All rates are weighted averages for each County for Taxes Payable 2011. The rates shown under the "No FD" scenario assumes the same amount of local levy as under the "Current Law" scenario. Also shown for comparison purposes is the 2011 Fiscal Disparities areawide rate, the tax rate applied to the pooled commercial/industrial property tax capacity.

[9] A computer model was used to estimate 2011 property taxes with and without the fiscal disparities program for each municipality. For this simulation, special taxing district taxes were spread countywide, so special district rates do not match actual rates for each municipality.

Figure 17. Tax Rates with and without the Fiscal Disparities Program by County: 2011

County	Average of Current Law County Rate	Average of Current Law Muni Rate	Average of Current Law School Rate	Average of Current Law Specials Rate	Average of Current Law Total Rate
Anoka	40.19%	38.83%	23.11%	6.00%	108.12%
Carver	41.69%	29.86%	32.69%	5.48%	109.71%
Dakota	29.11%	40.00%	24.36%	5.28%	98.75%
Hennepin	45.54%	43.88%	22.19%	10.26%	121.88%
Ramsey	52.76%	33.05%	25.01%	9.07%	119.89%
Scott	35.47%	34.07%	28.79%	5.39%	103.71%
Washington	29.63%	32.81%	24.91%	5.82%	93.17%

County	Average of No FD County Rate	Average of No FD Muni Rate	Average of No FD School Rate	Average of No FD Specials Rate	Average of No FD Total Rate	Inc/Dec in Rate without FD
Anoka	42.01%	41.12%	29.01%	6.23%	118.38%	**10.26%**
Carver	42.18%	30.41%	34.41%	5.60%	112.60%	**2.89%**
Dakota	29.24%	40.48%	27.49%	5.26%	102.47%	**3.72%**
Hennepin	43.50%	42.41%	23.19%	9.76%	118.85%	**-3.03%**
Ramsey	54.04%	34.51%	29.03%	9.32%	126.90%	**7.01%**
Scott	36.17%	35.35%	31.31%	5.53%	108.36%	**4.65%**
Washington	30.00%	33.54%	27.40%	5.91%	96.85%	**3.68%**
2011 Fiscal Disparities Areawide Rate					129.327%	

Source: MN Dept. of Revenue. (Weighted averages by County.)

As shown above, all counties would see an increase in tax rates with elimination of the program except Hennepin County. The largest percentage increases would be in Anoka and Ramsey counties.[10]

Results by Regional Development Classification

Results are also grouped by regional development classification for taxes paid and then implications to tax rates if the Fiscal Disparities Program were eliminated. All dollars are shown in thousands for Taxes Payable 2011.

In total, Developed Areas would see the largest percentage decrease (at 1.4 percent) and Rural Growth Centers would see the largest percentage increase (at 10.5 percent) in taxes paid. What is noticeable here is the magnitudes of the increases and decreases—with decreases in taxes at a much lower percent than the increases. This can be somewhat explained by the size of the property tax pool in the

[10] An earlier version of this report included averages of the jurisdiction rates within each County for this summary (instead of weighted averages as shown in this revision). Looking at averages of the jurisdiction averages results in Hennepin tax rates decreasing by 1.9 percent and increases in the remainder of the counties with Anoka at 15.6 percent and Washington at 12.9 percent.

respective categories. In this case, a $30 million decrease in taxes out of a larger base results in a smaller percentage (decrease) than a $5.6 million increase in taxes out of a smaller base.

Figure 18. Total Taxes Paid with and without the Fiscal Disparities Program by Regional Development Classification: 2011

	TOTAL Taxes Payable 2011 (in $1,000s)		TOTAL Increase/Decrease
Regional Classification	*Current Taxes*	*Taxes with FD Eliminated*	*Without FD*
Central Cities	$1,163,640	$1,193,460	2.6%
Developed Area	$2,203,657	$2,173,406	*-1.4%*
Developing Area	$1,479,840	$1,469,014	-0.7%
Rural Areas	$181,927	$186,611	2.6%
Rural Growth Centers	$53,680	$59,308	*10.5%*
Excluded from FD	$18,870	$18,742	-0.7%
Grand Total	***$5,101,614***	***$5,100,541***	***0.0%***

Source: MN Dept. of Revenue.

Implications to tax rates if the Fiscal Disparities Program were eliminated are evaluated and grouped by regional development classifications. All rates are for Taxes Payable 2011. The rates shown under the “No FD” scenario assumes the same amount of local levy as under the “Current Law” scenario. Also shown for comparison purposes is the 2011 Fiscal Disparities areawide rate, the tax rate applied to the pooled commercial/industrial property tax capacity.

Figure 19. Tax Rates with and without the Fiscal Disparities Program by Regional Development Classification: 2011

	Average of Current Law County Rate	*Average of Current Law Muni Rate*	*Average of Current Law School Rate*	*Average of Current Law Specials Rate*	*Average of Current Law Total Rate*
Central Cities	47.09%	57.81%	24.15%	9.83%	138.87%
Developed Areas	43.10%	37.66%	21.90%	8.57%	111.23%
Developing Areas	38.89%	34.29%	26.32%	7.42%	106.92%
Rural Areas	34.48%	22.29%	25.26%	5.94%	87.97%
Rural Growth Centers	38.29%	51.17%	26.49%	5.65%	121.60%
Excluded	40.42%	22.87%	15.01%	7.39%	85.70%

	Average of No FD County Rate	*Average of No FD Muni Rate*	*Average of No FD School Rate*	*Average of No FD Specials Rate*	*Average of No FD Total Rate*	*Inc/Dec in Rate without FD*
Central Cities	46.20%	58.32%	27.88%	9.60%	142.00%	**3.14%**
Developed Areas	42.54%	36.98%	23.73%	8.39%	111.63%	**0.40%**
Developing Areas	38.58%	33.82%	28.43%	7.32%	108.15%	**1.23%**
Rural Areas	35.06%	23.63%	28.51%	6.03%	93.24%	**5.27%**
Rural Growth Centers	39.37%	60.03%	31.12%	5.82%	136.35%	**14.74%**
Excluded	39.56%	22.87%	15.64%	7.17%	85.24%	**-0.46%**

2011 Fiscal Disparities Areawide Rate	129.327%

Source: MN Dept. of Revenue. (Weighted averages by group.)

All groupings, other than those excluded from the program, would experience an increase in tax rates if the Fiscal Disparities program were eliminated. As shown above, the largest tax rate increase would be experienced in Rural Growth Centers (with an increase of 14.74 percent). The lowest rate increase would be experienced in Developed Areas, with an increase of 0.40 percent. Note that under this simulation there is an overall increase in local tax rates from the elimination of the program of 2 percentage points. The fiscal disparities areawide rate is based on previous year local tax rates. Local tax rates increased about 10 percentage points across the metro area between 2010 and 2011 due to significant reductions in property values. Replicating this simulation at a time of steady tax rates would result in most net-contributor areas having tax rate reductions.

To further investigate the effect of the Fiscal Disparities Program on tax rates, we used the net contributor/net recipient groupings to determine the magnitude of the rate increase and decrease. Findings are shown below.

Figure 20. Tax Rates with and without the Fiscal Disparities Program for Contributors and Recipients: 2011

	Average of Current Law County Rate	Average of Current Law Muni Rate	Average of Current Law School Rate	Average of Current Law Specials Rate	Average of Current Law Total Rate	
Contributor	43.26%	39.99%	22.75%	8.95%	114.94%	
Recipient	39.96%	38.81%	25.70%	7.23%	111.69%	
	Average of No FD County Rate	**Average of No FD Muni Rate**	**Average of No FD School Rate**	**Average of No FD Specials Rate**	**Average of No FD Total Rate**	**Inc/Dec in Rate without FD**
Contributor	42.24%	37.82%	23.85%	8.67%	112.58%	**-2.36%**
Recipient	40.45%	41.98%	30.02%	7.29%	119.74%	**8.04%**
2011 Fiscal Disparities Areawide Rate					129.327%	

Source: MN Dept. of Revenue (Weighted averages by group.)

As shown, net contributors would see a decrease of 2.36 percent in the overall tax rate. Net recipients would see an increase of 8.04 percent to the overall rate. Further detail is provided in the body of the report and Appendix provides a ranking of the top twenty jurisdictions experiencing a decrease or increase in the total rate without the program.

Residential Homestead Burden

The Minnesota Department of Revenue maintains a database of property-tax and income for each homestead in the state (“Voss database”). For the Fiscal Disparities analysis, the Voss database is used to provide information on the *property tax burden as a percent of income* both under the current Fiscal Disparities law as well as if the program were eliminated. Data are from taxes payable year 2008.

Figure 21. Residential Homestead Property Tax Burden by County (2008)

	Residential Homestead Taxes				
County	Median Total Net Tax* Current Law	Median Total Net Tax* No FD	Inc/(Dec) No FD	Homestead Burden Current Law	Homestead Burden No FD
Anoka	$2,252	$2,403	$151	3.27%	3.49%
Carver	$3,013	$3,107	$94	3.38%	3.48%
Dakota	$2,530	$2,604	$74	3.13%	3.23%
Hennepin	$2,785	$2,784	($1)	3.67%	3.65%
Ramsey	$2,320	$2,426	$106	3.45%	3.63%
Scott	$2,886	$2,990	$104	3.51%	3.62%
Washington	$2,469	$2,559	$90	2.98%	3.08%
Overall Median	**$2,577**	**$2,640**	**$63**	**3.41%**	**3.49%**

** Taxes Payable 2008 (latest data available for Homestead Burden analysis).*
Source: MN Dept. of Revenue

Assuming elimination of Fiscal Disparities with no adjustment in levy amounts, median taxes paid would increase in all counties, except Hennepin where the decrease would be negligible. As a percent of income, the homestead burden would increase for all property from 3.41 percent to 3.49 percent. The largest increase would be in in Anoka County increasing from 3.27 percent to 3.49 percent (*a .22 percent increase*). Hennepin County’s burden would decrease from 3.67 percent to 3.65 percent, *a .02 percent decrease*.

Looking at the data grouped by regional development classification yields the following results.

Figure 22. Residential Homestead Property Tax Burden by Regional Development Classification (2008)

	Number of Homesteads (2008)	Homestead Burden* Current Law	Homestead Burden* No FD
Central Cities	130,110	3.95%	4.11%
Developed Area	329,039	3.34%	3.40%
Developing Area	218,933	3.27%	3.33%
Rural Areas	40,726	3.28%	3.44%
Rural Growth Centers	13,395	3.43%	3.72%
Excluded from FD	1,904	3.53%	3.57%

** Taxes Payable 2008 (latest data available for Homestead Burden analysis).*

Source: MN Dept. of Revenue

Median taxes paid by residential homestead properties grouped by regional development classifications as a percent of income would increase for all groups if the Fiscal Disparities program were eliminated. Rural Growth Centers, Rural Areas, and Central Cities would see the largest increases in homestead burden.

Finally, the data is grouped by Fiscal Disparities status (net contributor or net recipient in 2011). Results are shown below.

Figure 23. Residential Homestead Property Tax Burden by Fiscal Disparities Status (2008)

	Number of Homesteads (2008)	Homestead Burden* Current Law	Homestead Burden* No FD
Contributor**	364,194	3.37%	3.37%
Recipient**	368,009	3.44%	3.62%
n/a	1,904	3.53%	3.57%

** Taxes Payable 2008 (latest data available for Homestead Burden analysis).*

*** Status for taxes payable 2011*

Source: MN Dept. of Revenue

Homestead burden would stay the same in contributor communities at 3.37 percent of income. Residential homestead property taxes in recipient communities would increase the percentage of income spent on taxes from 3.44 percent to 3.62 percent. What is also interesting to note is the number of homestead properties in each category, which is almost evenly split between contributors and recipients (in 2011).

EVALUATION OF OVERBURDEN: FISCAL IMPACTS OF LAND USES

The legislation authorizing this study identified a need to analyze a locality's "overburden," particularly related to Commercial/Industrial property under the Fiscal Disparities program. That is, is the revenue generated to a locality from C/I property sufficient to cover the direct expenditures incurred.

To attempt to address the issues identified in the legislation authorizing the study as well as in stakeholder discussions, we conducted a *Cost of Land Use* fiscal impact analysis of a select group of jurisdictions in the region. The selected jurisdictions reflect one from the regional development classification groupings used in this analysis:

- Central Cities
- Developed Cities
- Developing Cities
- Rural (Rural Area and Rural Growth Center)

Fiscal impact analysis is one tool to understand the direct fiscal implications of tax structures, cost burdens, and development patterns on local governments. Most states require local governments to prepare a balanced budget on an annual basis. However, most states do not require that jurisdictions conduct fiscal impact evaluations to help ensure that local officials understand the short- and long-term fiscal effects of land-use and development policies and of potential new development. A fiscal impact analysis clarifies the financial effects of such policies and practices by projecting net cash flow to the public sector due to residential and nonresidential development.

A Cost of Land Use fiscal impact study is one type of fiscal analysis. It analyzes the fiscal impact of prototypical land uses that are currently developed in the jurisdiction. In this type of analysis, a "snapshot" approach is used that determines the costs and revenues for various land use prototypes in order to understand the fiscal effect each land use has independently on the jurisdiction. In other words, it seeks to answer the question, ***"What type of development pays for itself?"***

This type of analysis is used to investigate whether there is an "overburden" in providing public services to commercial and industrial land uses that are not sufficiently being covered by revenues generated by that land use—particularly due to the Fiscal Disparities program. Toward that end, we include in this analysis two scenarios for each case study:

1. With Fiscal Disparities (Current System)
2. Without Fiscal Disparities (Hypothetical Scenario)

For each jurisdiction, TischlerBise evaluated nine land use categories—five residential and four nonresidential land uses. The land use categories are listed below. Demographic factors vary by jurisdiction and are discussed in each jurisdiction's section of this report. These prototypes are then used to analyze fiscal impacts to the (a) municipality, (b) county, and (c) primary school district.

Residential Land Use

- Single family detached unit: Higher value
- Single family detached unit: Median value
- Single family detached unit: Lower value
- Multifamily/Condo (Homestead) unit
- Apartment unit

Nonresidential Land Use

- Commercial/Retail
- Office
- Industrial
- Institutional (tax exempt)

This study does not intend to be comprehensive or exhaustive identifying overburdens in Metro area municipalities or fiscal impacts if the Fiscal Disparities program were eliminated. This would be impossible even with unlimited time and funding.[11] Rather, it is intended to identify the fiscal relationship between land uses and service demands/costs at the main levels of government providing services and infrastructure under the current Fiscal Disparities program and potential fiscal impacts if the program were eliminated.

Cost of Land Use Fiscal Analysis: General Approach

For each case example, cost and revenue factors have been determined based on FY 2011budgetsand additional fiscal research. The analysis is based on **current levels of service**. Current levels of service represent the respective level of government's (City, County, or School District) current level of spending for services and facilities. That is, assumptions made in the analysis are based on revenue sources, programs, services, requirements, and policies that are in place today (with the exception of the "without Fiscal Disparities Program" scenario where tax rates are adjusted to reflect hypothetical elimination of the program).

The analysis includes General Funds and major Special Funds, both operating and capital, for each level of government evaluated. Enterprise funds are not included in the analysis as they are assumed to be

[11] However, on a location-specific level, this could be done as is being done in the City of Anoka (see the GISRDC study) as well as was conducted by TischlerBise in 2000-01.

self-sustaining. Only those revenues and costs **directly attributed** to the land use are assumed with the exception of Fiscal Disparities Program revenue. The approach taken for Fiscal Disparities revenue allocates the distribution levy in the jurisdiction using the factors in the Fiscal Disparities distribution formula—namely market values and population. Therefore, the residential prototypes in this analysis get "revenue credit" for distribution levies in the "With Fiscal Disparities" scenario.

Indirect, or spin-off, impacts are not included. An average cost approach is taken and where appropriate, revenues and costs are allocated to residential development, nonresidential development, or both with proportionate share factors.

As noted, there are two scenarios analyzed: (1) Current with Fiscal Disparities (Current System); and (2) Without Fiscal Disparities (Hypothetical Scenario). In the latter scenario, the tax rates are adjusted to assume the same amount of levy in the respective locality; therefore, for net contributors, the tax rates are assumed to decrease and for net recipients, the tax rates are assumed to increase. However, other revenue sources (such as state funding that may be affected by changes to the Fiscal Disparities program) are **not** adjusted. The concept is to test what would happen to revenue generation by type of land use if the Fiscal Disparities program were to be dismantled and levels of service maintained—without clouding the results with changes to other funding programs.

The Cost of Land Use fiscal impact results for all levels of government are discussed in terms of annual net results for each land use prototype. The figures show net fiscal results by type of land use for residential development and nonresidential development. For residential development, results are shown **per residential unit** and for nonresidential development results are shown **per 1,000 square feet of floor area** in all figures. ***Data points above the $0 line represent net surpluses; data points below the $0 line represent net deficits. Where net deficits are shown, one can assume an "overburden" for that particular prototype land use.***

Summary results are provided below for each of the case example jurisdictions for all levels of government.

Summary Results of Cost of Land Use Fiscal Impact Analysis

Results for each case example are presented in total layering each jurisdiction's results in one chart. For each case example, fiscal impact summary results are shown first with the Fiscal Disparities program followed by fiscal impact summary results without the Fiscal Disparities program. While results are presented in total (combined results from the city, county, and school district), it should be acknowledged that local governments provide services and infrastructure separately. Therefore, a "net surplus" per land use at one level of government (e.g., city, county, schools) does not offset a "net deficit" at another level.

Central City Fiscal Impact Results

Figure 24.CENTRAL CITY Annual Net Fiscal Results: TOTAL Results with Fiscal Disparities

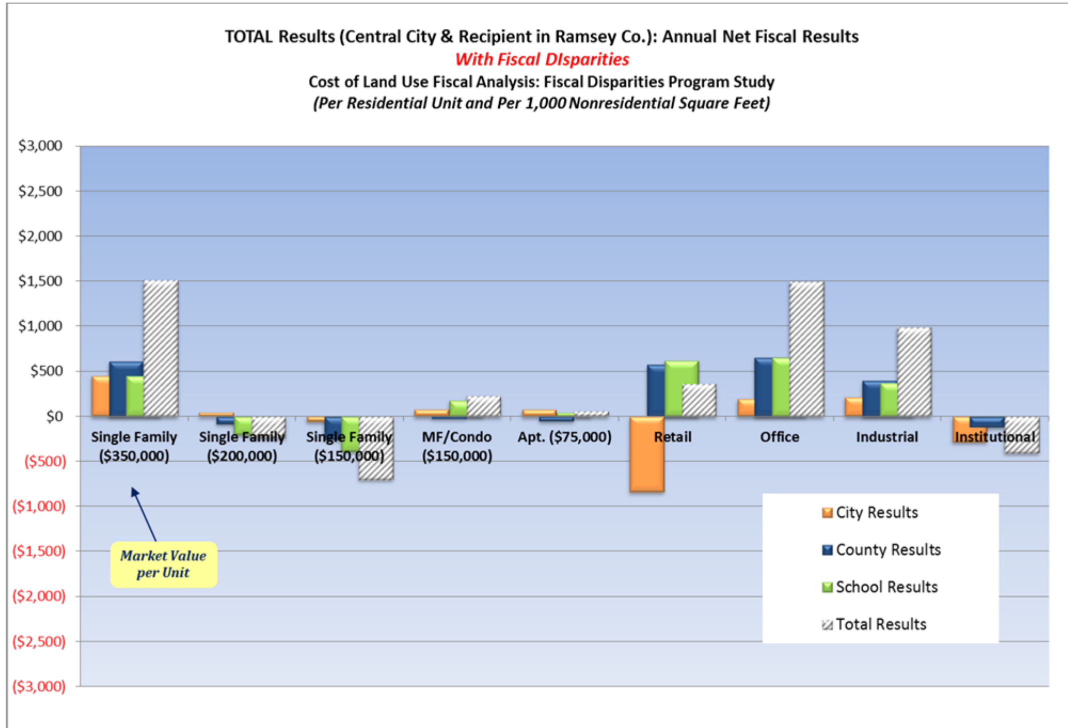
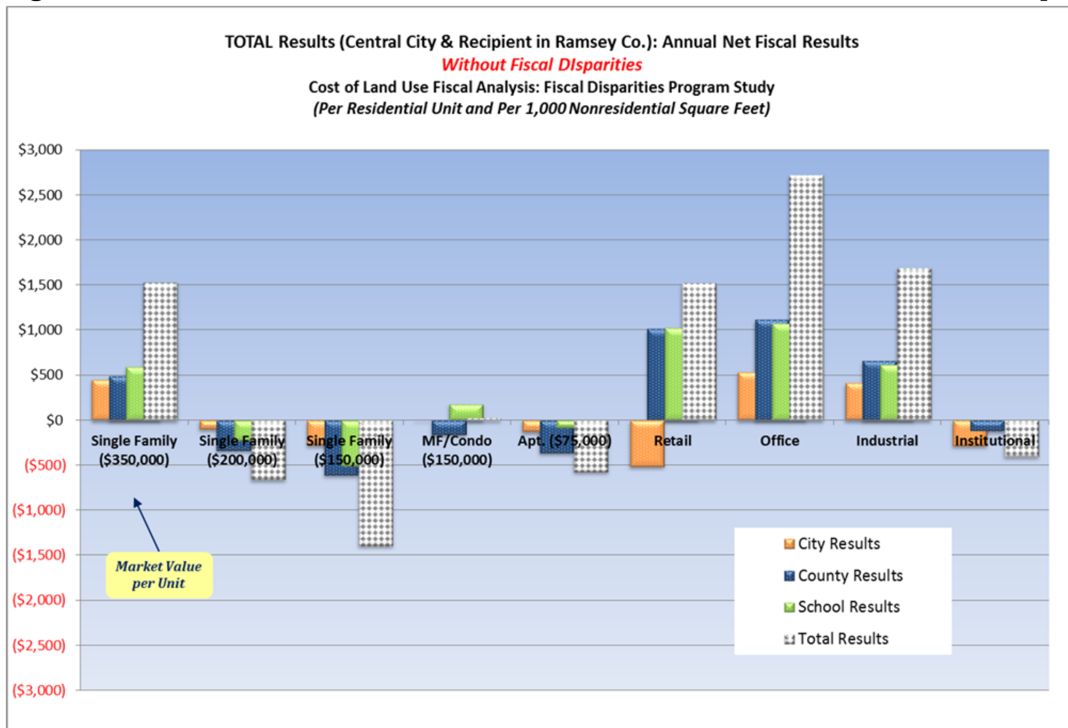


Figure 25.CENTRAL CITY Annual Net Fiscal Results: TOTAL Results without Fiscal Disparities



- With all jurisdictions combined, single family residential prototypes tend to produce net deficits unless the property values are high enough to offset the expenditures. This is true both under the current law—with Fiscal Disparities—and if it were eliminated. At the City government level, however, results for all residential prototypes under the current system are net surpluses or small net deficits, due to non-local revenues.

- For multifamily units, the results are worse with Fiscal Disparities eliminated—costs are assumed to remain the same but less revenue is allocated to these units due to loss of Fiscal Disparities revenue allocated to these units with a tax rate increase that does not cover the shortfall.

- For all nonresidential land uses except institutional uses, the overall fiscal impact is positive. The combined result is that there does not appear to be an “overburden” in total to serve these land uses (based on the prototype land use assumptions in this analysis). The results are better per nonresidential prototype without the program because more direct revenue is allocated to these land uses. Results vary by type of jurisdiction where service impacts are experienced, specifically for retail land uses where a net deficit (overburden) is generated at the city level but not at other governmental unit levels under both scenarios. Institutional uses generate a net deficit at all levels.

Developed City Fiscal Impact Results

Figure 26.DEVELOPED CITY Annual Net Fiscal Results: TOTAL Results with Fiscal Disparities

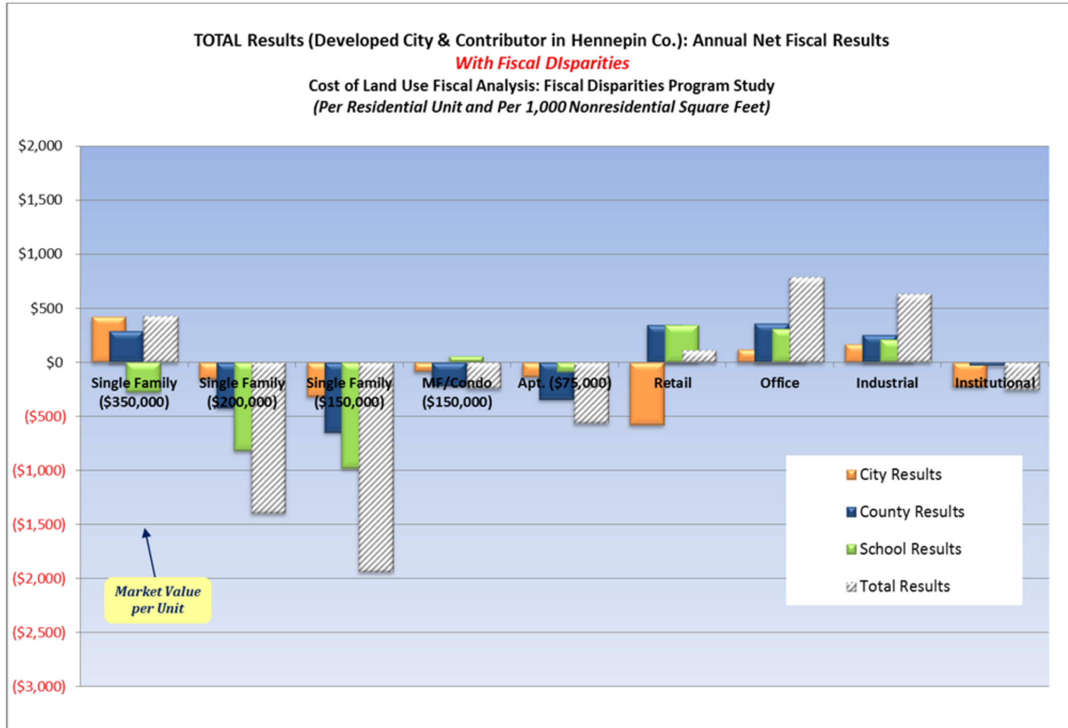
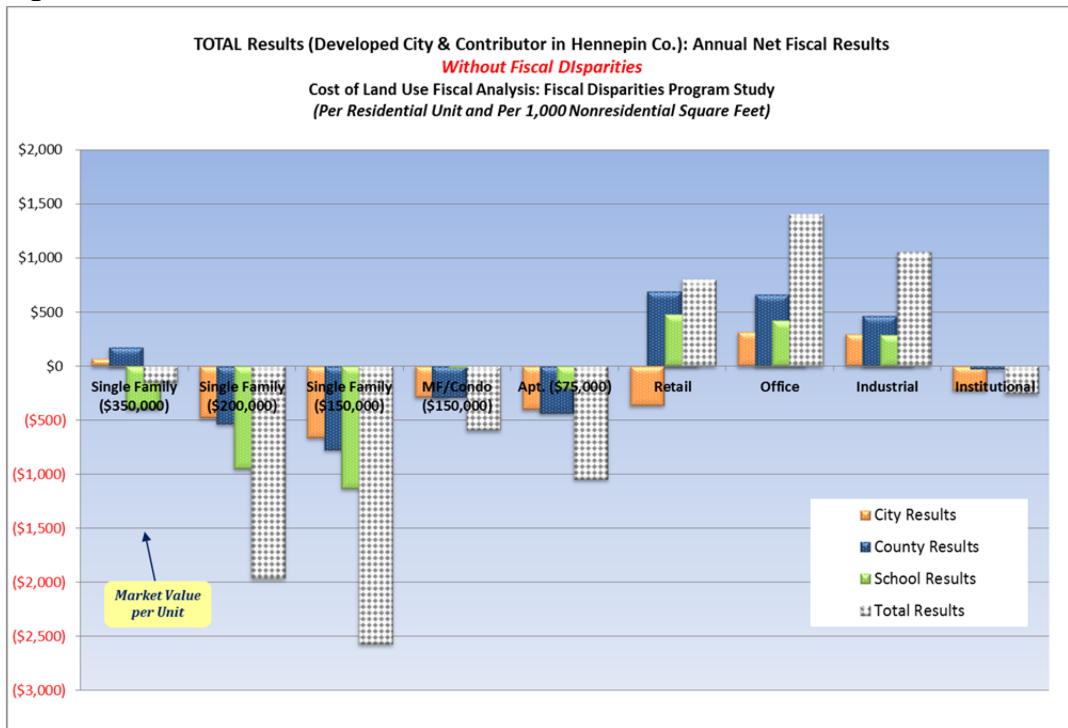


Figure 27.DEVELOPED CITY Annual Net Fiscal Results: TOTAL Results without Fiscal Disparities



- With all jurisdictions combined, all single family residential prototypes produce net deficits, except for single family detached units of higher value under the current taxing system. Multifamily (condo homestead) units generate the smallest overall net deficit due to a smaller relative household size and number of students per unit.

- For residential development, overall fiscal results are essentially the same (i.e., net deficits) under the current law—with Fiscal Disparities—and without it. The magnitude of the net deficits is greater assuming elimination of the program due to a lower property tax rate in this net contributor city. The exception is a single family unit of higher value, which switches from a net surplus to a net deficit under the scenario eliminating the program due to lower property taxes.

- All nonresidential land use prototypes produce net surpluses in total, with the exception of institutional uses. The combined result is that there does not appear to be an "overburden" in total to serve these prototype land uses. Results vary by jurisdiction level with retail as an overburden to the city, but not the other levels of government. All other nonresidential prototype land uses cover their respective costs.

- The results are better per nonresidential prototype without the Fiscal Disparities program because more direct revenue is allocated to these land uses, even with the lowered tax rate. And as discussed above, results vary by jurisdiction level where service impacts are experienced, specifically for retail land uses. At the city level, retail still generates a net deficit (an "overburden") even with elimination of the program.

Developing City Fiscal Impact Results

Figure 28.DEVELOPING CITY Annual Net Fiscal Results: TOTAL Results with Fiscal Disparities

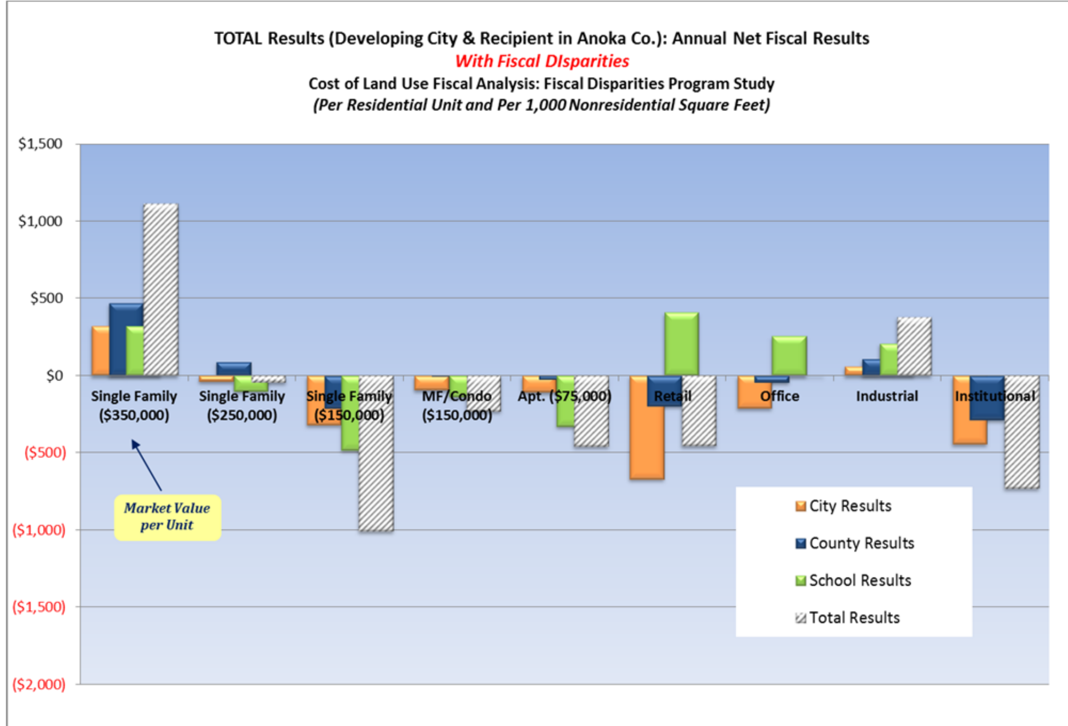
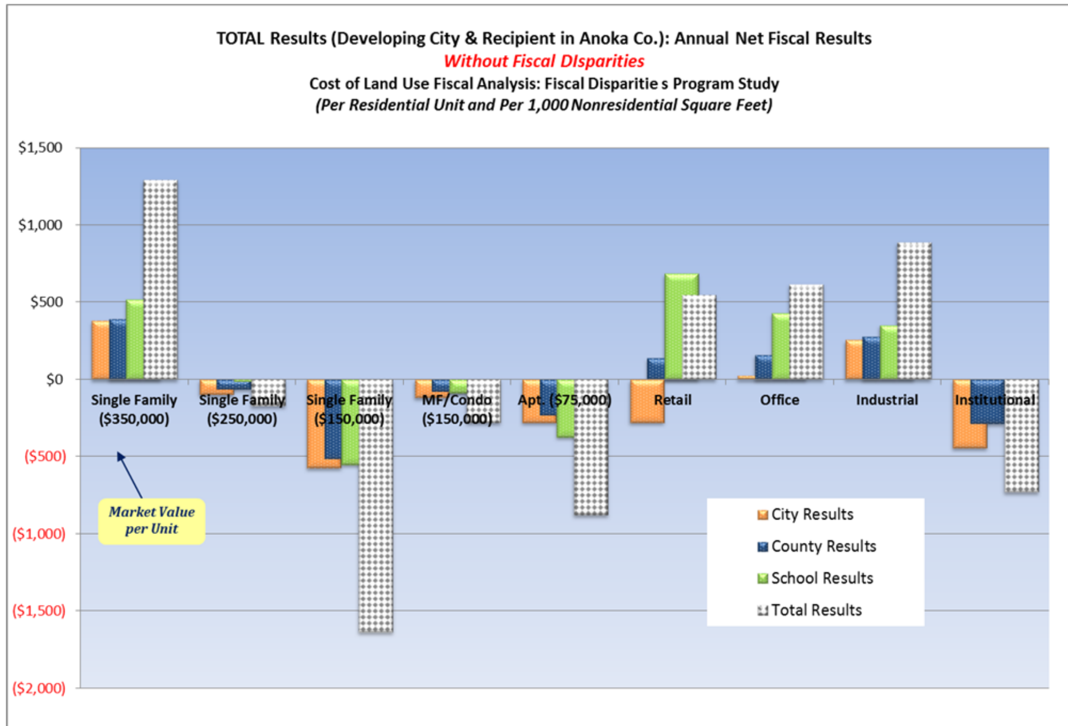


Figure 29.DEVELOPING CITY Annual Net Fiscal Results: TOTAL Results without Fiscal Disparities



- With all jurisdictions combined, all single family residential prototypes produce net deficits, except for single family detached units of higher value under both tax system assumptions. For all residential land uses—single family median and lower value units, multifamily/condo, and apartment—revenues at each level of government are insufficient to cover costs. (The only exception is single family median value units at the county level under the current system.) Even with Fiscal Disparities allocation to residential land uses, net deficits are generated.

- For residential units without the Fiscal Disparities program, net deficits are deepened—and generated at all levels of government (with the exception of higher value single family units). The increase in tax rates is not sufficient to cover the loss in Fiscal Disparities revenue.

- For nonresidential prototype land uses under the current tax system, only industrial land uses generate net surpluses. The remaining nonresidential prototypes generate net deficits (office and institutional)—an overburden, or break even (office). (For school district results, the result for nonresidential land uses are a net surplus due to revenues generated but no direct costs.)

- For nonresidential land uses without the Fiscal Disparities program, combined results produce net surpluses, with the exception of institutional uses. The amount of direct revenue captured by these land uses is sufficient to cover the projected expenditures, due to both the direct capture of tax base and the tax rate increase needed to generate the same levy.

- The combined result is that there appears to be an “overburden” under the current system when looking at individual nonresidential land use prototypes for this community, specifically with retail and office to a certain extent. This is true even though this community is a net recipient. Industrial land uses cover their respective costs. When the program is assumed to be eliminated, tax rates are assumed to increase in this community and more revenue is captured by the nonresidential development. Therefore, fiscal results improve and switch from an overall net deficit to net surplus for nonresidential land uses (except institutional). However, results vary by jurisdiction level where service impacts are experienced (i.e., city results for retail remain an overburden).

Rural Area Fiscal Impact Results

Figure 30. RURAL AREA Annual Net Fiscal Results: TOTAL Results with Fiscal Disparities

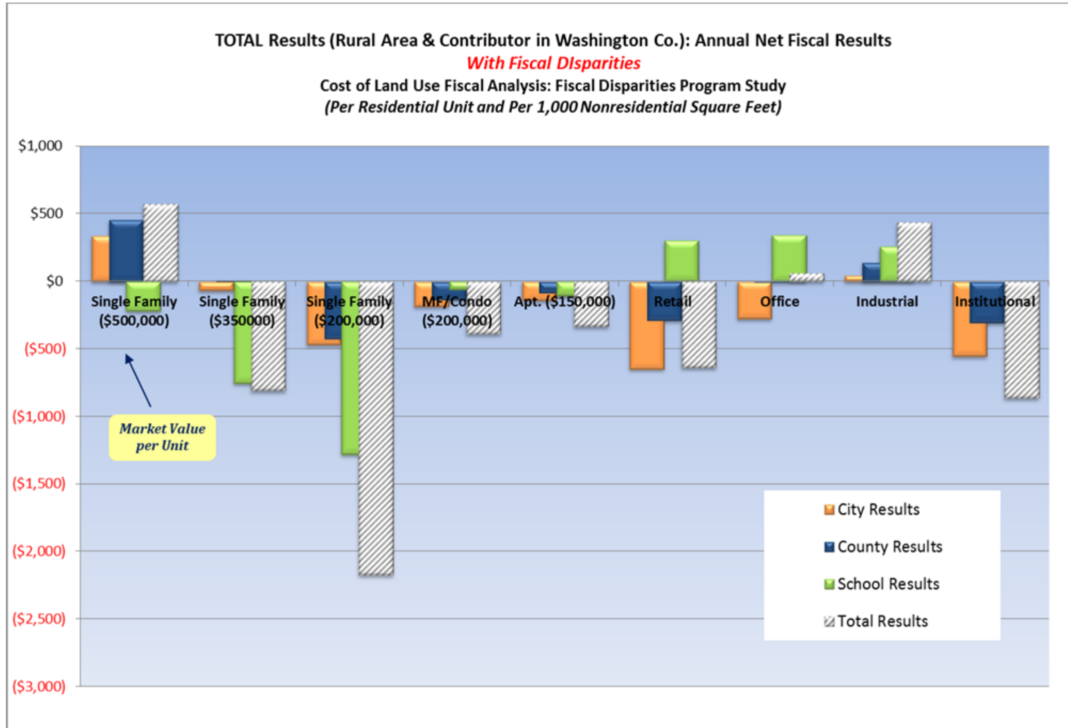
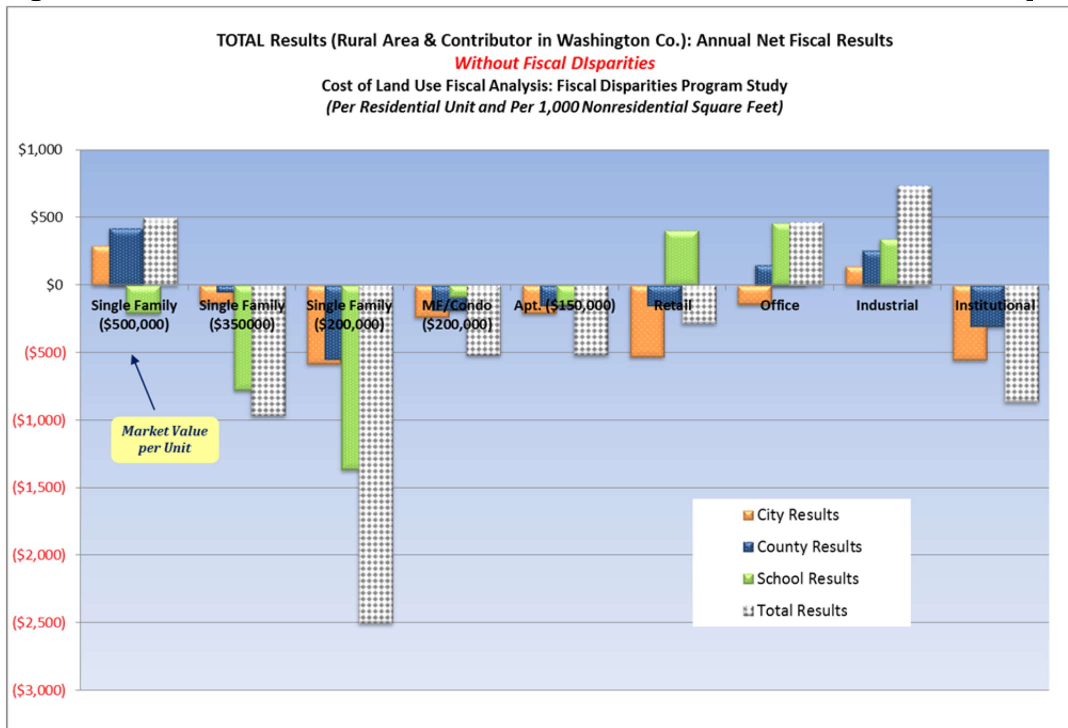


Figure 31. RURAL AREA Annual Net Fiscal Results: TOTAL Results without Fiscal Disparities



- With all jurisdictions combined, most single family residential prototypes produce net deficits with the exception of single family detached units of higher value under both the current taxing system and if Fiscal Disparities were eliminated.

- Under the current system with Fiscal Disparities combined for all jurisdictions, office and industrial generate net surpluses with retail and institutional generating net deficits. Retail generates net deficits at both the city and county level and office generates a net deficit at the city level.

- Overall findings are essentially the same under the current law—with Fiscal Disparities—and if it were eliminated. That is, whether a land use produces a net deficit or net surplus is unaffected by removal of the Fiscal Disparities program. What is affected is the magnitude of the deficit or surplus. Residential net deficits get larger, due to the removal of Fiscal Disparities revenue allocation and a decreased tax rate since this community is a net contributor.

- For nonresidential land use prototypes, the overall result is larger net surpluses for office and industrial, due to more direct revenue captured. The retail land use is still a net deficit—an overburden, even with more direct property tax revenues captured.

- For nonresidential land uses except retail and institutional uses, the overall fiscal impact is a net surplus, indicating that there is not an "overburden" in total to serve these land uses. However, for retail (and institutional) land uses, there appears to be an overburden in total. Results vary by jurisdiction level where service impacts are experienced.

POLICY CONSIDERATIONS

The report concludes with a discussion of policy considerations, including criticisms, issues, and praise for the Fiscal Disparities program.

Key Issues

- *Impact of the current economic downturn on localities.* With the current economic downturn and local government budgetary stress, a prominent issue is that with a portion of a locality's tax capacity going to a shared pool, net contributors are not receiving the full revenue from their property tax base.

- *Expansion of the Program to additional, outlying jurisdictions*. Suggstions have been made to expand the program to outlying Minnesota counties, which are now considered part of the regional labor market.

- *Inclusion of residential tax base in the program*. Some have called for adding "high-end" residential tax base to the Program. Expansion of the program to include residential homestead properties over $200,000 was proposed and passed in the Minnesota Legislature in 1995 but vetoed by the Governor.

- *Adjusting the 40 percent contribution*. It has been noted in the literature that the 40 percent share is arbitrary and it has not been proven if this is the threshold after which a commercial/industrial property "pays for itself" locally in terms of revenues generated and costs incurred.As discussed in this report, this depends on the level of government and the type of commercial/industrial property.

- *Allowing for exclusions of certain "regional benefit" properties that generate high costs and serve as regional economic engines (e.g., the Mall of America).* This was attempted recently in 2007-08 when the Mall of America requested exemption from the tax-base sharing pool for its expansion. The proposal was defeated, but opened discussion and attention on the issue surrounding properties of regional benefit and how they relate to the Fiscal Disparities Program.

- *Adjusting the assessment level*. Each jurisdiction assesses property under its own assessment system allowing for some variation in assessment levels. Therefore, the contribution from each taxing jurisdiction is based on the locally derived assessment, thus creating "an apparent

inequity and discourages assessors from raising assessment levels in their jurisdictions."[12] However,a number of administrative challenges to addresss this issue have been identified.

- *Eliminating the exemptions.* Property at the Minneapolis-St. Paul Airport is exempt from fiscal disparities contributions.While the Airport may seem a likely candidate for inclusion in the program, eliminating the exemption would be problematic since it would contribute to the pool but would not receive any distribution under the current population-based formula.[13]

- *Eliminating the 1971 base value subtraction*. The argument here is that the 1971 starting point "discriminates against those areas that have experienced most of their development since 1971."[14] Related to this is the concept that the areawide pool reflects 40 percent of total C/I valuation from 1971 including increases due to growth and inflation. It has been argued that only net new growth should be included based on the logic that development is able to occur because of regional investment (e.g., roads, sewers) and therefore the formula would be more reflective of the program's goals. The counterargument to this is that the law allows for a regional balance among properties that increase in value and those that decline.

- *Including a spending need component to the formula, rather than purely tax-base driven.* As discussed in this report, this aspect of the Program is widely discussed. The argument being that spending needs of jurisdictions vary and tax base is not necessarily a good predictor of those needs. Hinze and Baker note the inherent challenges to altering the formula to account for thisare both political and technical.

- *Stability of the Program.* It has been noted on several occasions that the program is seen as stable and not subject to a political process. This is seen as both an advantage and a disadvantage. An advantage in that it occurs as a matter of course and allows for relative stability in local funding availability. On the other hand, its legacy as a program from the 1970s that has not been modified and is not part of any political process leads to some criticism.

- *Long-term impact.* Another point made by stakeholders consulted for this study is the rapidly developing areas ("younger communities") may be experiencing an increase in commercial/industrial growth relative to population growth and therefore may be a net contributor. As these communities mature and begin to buildout, they may remain net contributors but at a smaller margin or may see decline in value causing a transition to net recipient status. This changed status allows for additional resources to make up the shortfall and potentially support redevelopment efforts, which over time may transition the community back to net contributor status.

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[12]Hinze and Baker, 2005, p., 31.
[13] Id., p. 32
[14]Id., p., 32.

Overburden

The overburden question has different answers depending on the unit of government. For some levels of government, as evaluated in this study, certain land uses do not cover their costs when looking at them as discrete land uses. For example, retail development does not generate sufficient direct revenues to cover its direct costs at the city level both with and without the Fiscal Disparities Program for both net contributors and net recipients. For other levels of government, the result for retail development is flipped. The overburden question depends not only on the level of government, but the locality itself. Levels of service, tolerance for tax increases, and the types of services provided are all contributing factors. It is interesting to note, however, that the Local Government Aid (LGA) formula includes a service "needs" component.

Another related point is the changes in school funding over the 40-year history of the program. While school funding is complex and an analysis of its relationship to Fiscal Disparities is beyond the scope of this study, one point made is that at the inception of the Fiscal Disparities program, the majority of funding for schools was from local property taxes. Therefore, those localities with high property tax wealth were able to more easily fund school operating and capital needs, and in particular, those communities with a large nonresidential tax base would be in a much better fiscal position. Critics note that because school funding has shifted from primarily being funded from local sources to state sources that the need for redistribution of the commercial/industrial tax base is less important today than it was prior to that shift.

Business Location Decisions

Business location decisions are driven by a range of factors first driven by the type of industry or business (e.g., manufacturers have different location needs than retail) as well as size of the firm, location decision stage, stage of firm life cycle, and economic environment.

Because there are so many interrelated variables in a site selection process, it is not feasible to isolate any one element for purposes of this study. Even if this were done as an academic exercise, the reality in a region like the Twin Cities is that other qualitative factors unique to each locality are likely to influence the decision and not be quantifiable. A recent report by the Itasca Project identified several strengths and weaknesses of the Minneapolis-St. Paul region related to business location decisions. Among the findings is a discussion of tax structure, and the region's high relative tax burden when compared nationally and the disadvantage this puts the Metro region when competing nationally and internationally for business locations and relocations. However, the focus of their tax discussion is primarily on state and federal taxes, which according to the report already puts the region at a relative disadvantage even before adding the local tax burden.[15]

[15] Itasca Project, "Charting a New Course: Restoring Job Growth in the Minneapolis-St. Paul Region," April 2010.

In discussions with representatives from the regional business community, the Fiscal Disparities program does not appear to be a factor in development or relocation decisions. However, it is not possible to determine whether this is due to the very existence of the program—that is, if there were more disparity in tax rates among jurisdictions in the region, perhaps it would be a pronounced factor in location decisions.

However, one common theme from the business community is opposition to "raiding" the revenue generated by the program for specific purposes. The general concern is that if revenues were diverted from the pool, localities would need to fill the gap left by this reallocation of funds and would potentially raise taxes on local businesses.

Influence on Development Activity

The desire from a local perspective for commercial and industrial development is often driven by other factors in addition to an expansion of the tax base. Other reasons include:

- "Placemaking"—providing a gathering place for community with retail, entertainment, and cultural options (promoting a "Creative Culture"),
- Creating jobs where people live in mixed-use communities, which allows for reduced commuting times and a greater attachment to community,
- Creating jobs for purposes of "bragging" rights, particularly in this era of prolonged economic downturn and joblessness, and
- Enhancing the overall quality of life through all of the above.

Related to this phenomenon is a statement from Myron Orfield that the Fiscal Disparities program "reduces the incentives for communities to compete for tax base, because they do not keep all of the resulting revenues. On the other hand, because localities retain enough of the tax base to cover the costs of growth, the incentive is not so strong that local areas will be unwilling to allow new development."[16] There does not appear to be a clear-cut answer to this asssumption, particularly in a seven-county region with almost 200 municipalities. NAIOP in its "Fiscal Disparities Task Force Report" notes the following:

> *Among the unforeseen consequences of fiscal disparities is its influence on land use and development decisions by local government officials. Fiscal disparities may lead communities to focus their efforts on new and higher valued residential development (which is not required to contribute to the fiscal disparities pool), while viewing fiscal disparities as a disincentive to expanding their own local C-I tax base.*[17]

[16] Orfield, 2009, p. 38.
[17] NAIOP, 2007.

That said, tax increment financing (TIF) is used throughout the region to encourage development projects—both nonresidential and residential development with many of the projects appearing to be driven by the "quality of life" factors identified above. While it has been mentioned that most significant development projects in the Twin Cities Metro region include a TIF district, the share of TIF net tax capacity over the past 15 years has remained at 4 to 7 percent of total tax capacity in the region. What is more, a State Auditor's report on TIF districts (evaluating 2009 data) found that from 2005-2009, the number of districts certified decreased by 43 percent. The Auditor's study also found that in 2009, 34 percent of the number of TIF districts were in the Metro Area and 66 percent were located in Greater Minnesota, but the amount of tax increment revenue was predominantly generatedin the Metro Area at 83 percent.[18]

Regional Services

From our discussions with communities, another theme that emerged is the notion of "regional services" that may or may not be universally thought of as services. Examples include provision of housing (i.e., serving as a bedroom community for nearby employment centers); protection of wetlands; and provision of institutional (tax-exempt) properties such as schools and hospitals. The relation to Fiscal Disparities is that the existence of the program allows these communities to provide these "services" without placing an undue burden on its residents or its limited nonresidential tax base. By extension, an argument is that the existence of these services—and the variety of types of communities in the region—makes the region in whole more competitive.

Related to the idea of provision of regional services is the notion of "generational equity." Growth has occurred in the Metro region since the inception of the Fiscal Disparities program under the assumption that the program would be in place in the future. That is, perhaps localities did not aggressively pursue commercial/industrial development for a variety of reasons not the least of which was the "protection" of the Fiscal Disparities program.

Program Execution

Finally, a criticism of the program is the manner in which the areawide tax is conveyed to a commercial/industrial property owner on his/her tax statement. A commercial/industrial tax bill lists "Fiscal Disparity" under the Special Taxing Districts heading, and typically comprises a large portion of the overall tax burden. The argument is that by virtue of the way the tax is listed implies that if the program were eliminated, property owners would not pay that tax amount. In reality, if the program did not exist, taxes would be paid to the other taxing jurisdictions and depending on status as a recipient or contributor, the overall amount of taxes paid by the individual property owner would likely be only marginally lower or higher.

[18]Office of the State Auditor, "Tax Increment Financing Legislative Report," January 26, 2011.