

## **IN\$IGHT ST. PAUL'S ANALYSIS OF TAX INCREMENT FINANCING (TIF)**

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Tax Increment Financing (TIF) is a public financing method a Minnesota city can use to provide a subsidy to private developers (and eventual property owners) to facilitate taxable development on property that is vacant, blighted or underutilized. TIF can only be used if it can be proven that private development would not otherwise be feasible without a public subsidy. TIF can however be easily overused or abused and cause negative consequences to nearby properties. It is important to note that the property taxes paid by the new development for the next 26 years are used to pay for the public subsidy provided, while the added cost for providing government services to the new development is shifted to all other taxpayers outside of a TIF District. Granting TIF should therefore be carefully analyzed and wisely used.

St. Paul is the state's biggest user of TIF. In\$ight St. Paul's October 2024 report, called on the city to be forthcoming in telling its citizenry about its TIF activities. Our report noted that St. Paul, unlike Minneapolis, does not disclose any details about its many TIF districts, which handle millions of dollars of taxpayers' money. It is this situation -- the need for basic accountability -- that has motivated In\$ight St. Paul to better understand and explain TIF and to look into the city's past and future use of it. Both the St. Paul Housing and Redevelopment Authority and the St. Paul Port Authority use TIF to expand St. Paul's taxbase.

For an underdeveloped area proposed to have new development, the City determines the existing Taxable Value for the project area, which is then designated as a Tax Increment Financing (TIF) district. Then the City issues long-term general obligation bonds or short term pay-as-you-go notes to provide the private developer with a public subsidy, pay financing expenses and provide money for the City to pay debt service on the bonds for the first three years, until new property taxes begin coming in.

Once the development project is completed and the property owners within the TIF District start paying property taxes, Ramsey County Taxation subtracts the original taxable value (when the TIF district was created) from the new, current higher taxable value. This captured taxable value then has the current total tax rate applied to it, and all the new incremental taxes collected go to pay for debt service for the debt issued to subsidize the new development. This amount is the district's captured taxes.

After the bonds are paid off with the tax increments collected in future years, the TIF district is supposed to shut down, and all taxes collected that are no longer needed for debt service become a part of the general tax base used by all local taxing units.

In theory, TIF districts have facilitated new developments that have been deemed beneficial, and the districts have closed ahead of the schedule that was estimated at the time the bonds were issued. While those projects appear favorable, one must remember that all the new development requires costly city services that are not paid for by the properties inside the TIF districts. Those property owners don't pay for the government services they receive until all the outstanding debt issues are paid off. To cover the cost of government services inside a TIF district, the rest of the tax base then must pay more taxes.

And for some TIF districts, the new anticipated development did not fully materialize, resulting in a shortage of estimated property tax collections. To solve this dilemma, policymakers have pooled excess tax increments from successful TIF districts to use for debt service on unsuccessful TIF districts. When this happens, the city taxpayers outside TIF districts must continue to pay higher property taxes for the services being provided to properties inside of TIF districts.

Minnesota Department of Revenue's statistics for TIF districts reveal that the St. Paul's tax levies to service debt for TIF districts from 2015 to 2024 INCREASED 40.1% from \$31,603,964 to \$44,274,052. During that same ten-year period, Minneapolis's tax levies for TIF districts DECREASED 52.1% from \$50,105,971 to \$24,013,786.

The Metropolitan Council recently released its Fiscal Disparities Report for Property Taxes Payable in 2024. That report also provides information about the use of Tax Increment Financing for the metro area. The City of St. Paul had \$34,601,887 of taxable valuation captured in TIF districts, and that was the largest capture of any city in Minnesota. This taxable value represents about \$2.6 billion in Estimated Market Valuation. Minneapolis was the second largest user of TIF in Minnesota, and it had only \$21,471,921 of Taxable Value captured in TIF districts.

St. Paul's total taxable value outside of TIF districts was \$420,500,432. Minneapolis' total taxable value outside of TIF districts was \$848,580,723, more than twice St. Paul's. Yet St. Paul's use of TIF is 61% greater than in Minneapolis.

### **Saint Paul's Overuse of TIF Has Negative Consequences**

Tax increment financing (TIF) is a public financing tool employed with the long-term objective of expanding the City's tax base. It seeks to accomplish that goal by subsidizing redevelopment, infrastructure, and community improvement projects such as:

1. Upgrading obsolescent facilities.
2. Eliminating blight.
3. Remediating pollution

4. Expanding affordable housing choices.
5. Enhancing private sector employment growth.
6. Encouraging redevelopment activities that enhance urban features, amenities, and historic structures.

There is growing concern that TIF has been overused and that it has not delivered hoped-for results in addressing City goals. Other municipalities concerned about the efficacy of TIF have concluded that it places an undue and unfair burden on taxpayers and are reducing the use of TIF.

When using TIF, the City typically provides a subsidy to developers to engage in a project and then diverts property tax revenue from the project using those funds for up to 26 years to repay the City for the upfront money it spent to induce the private development activity. The City's tax base is not increased during this period. TIF is not a loan to a developer that the developer pays back to the City. TIF is a tax-free gift to the developer. The City provides the developer with a public upfront subsidy (the gift) and then the City must incur long-term debt to cover all costs associated with providing the gift.

During the first 26 years of a TIF District new property taxes captured in the district are first used to retire the debt incurred by the City and to finance city staff costs. And if tax increments collected are greater than debt issued and associated staff costs, the excess increments can be used for two other options. They may be used for secondary development opportunities within the district and, or to help pay debt service in another TIF District where captured tax increments are not sufficient to cover their existing debt service. The new captured taxes are not shared with the nine units of government that service the St. Paul taxbase. None of the new tax revenue is used to pay for public services provided within the TIF District such as fire, police, streets, bridges, libraries, parks, recreation facilities, public schools, social services and courts. Those cost obligations are passed on to all other St. Paul taxpayers living outside a TIF District.

In 2024 the City of Saint Paul had over 7.9% (\$2.8 Billion) of taxable property captured in TIF projects – the largest amount of any city in Minnesota. Given the significant need for redevelopment in Saint Paul's downtown, there will be mounting pressure to increase the use of TIF.

## **TIF IS A SEDUCTIVE TOOL**

Many City constituencies view TIF as an efficient and constructive solution to the achievement of one or more of the City's goals. City leaders may view TIF as an easy and attractive method for developing the City's tax base – an important goal of the City. The building trades may view it as an effective method for creating construction jobs – also an important goal of the City. Developers

view it as “free money” enabling them to pursue and profit from development opportunities. Taxpayers, unaware of the increased tax burden they will bear, may be pleased that the City is focusing on development opportunities. Accordingly, the pressure to use TIF can be persuasive despite negatives associated with its use.

## **TIF IS AN IMPERFECT TOOL**

There are significant negatives associated with the current use of TIF:

- It is a complex tool with many permutations making it difficult for the public to understand how it works, and the City websites provide little information about TIF projects and the impact on taxpayers.
- Its ultimate impact often cannot be assessed for years after its implementation.
- The predicted success of the project is often based on difficult-to-make financial projections.
- TIF obligations are not identified in annual City budgets.

## **USE OF TIF REQUIRES CAREFUL ANALYSIS**

Careful and rigorous consideration needs to be given to the approval of each TIF project to increase the probability that the project will benefit the City and its taxpayers. To ensure that it is the right solution for any given project requires a thoughtful understanding and analysis of the following issues:

- Is there a clear and compelling public purpose served by the proposed project?
- What are the barriers to private sector funding of the project that make it necessary to use public subsidies – TIF – on a given project? To what extent has the City or a developer explored other funding sources? What keeps a developer from tackling a project without a public subsidy?
- The “but for” test – a test that the project would not occur without the assistance of a public subsidy – must be rigorously applied. If a pattern develops that TIF is readily granted, it provides an incentive for all developers to ask for a public subsidy.
- TIF can incentivize development that results in over-building and thus the sub-optimal use of existing facilities. This can in turn reduce the net operating income for other competing properties and reduce the City’s overall tax capacity.

- Should TIF be awarded to local or non-local developers? Providing TIF financing to non-local developers gives the financial advantages of TIF financing to those developers outside of the City.
- If a local developer has a project not financed with TIF and is confronted with a competing project financed by TIF, that creates an unfair advantage for the TIF financed project. Such conflicts should be avoided in the awarding of TIF.
- Will the impact of a TIF project on other properties be positive or negative?
- When a project involving the conversion of a commercial structure to a residential structure is considered for TIF, decision-makers need to understand that residential structures pay only about half the tax that commercial structures pay.
- The City needs to analyze the difference between poorly performing and successful districts – both past and present – to assist in the decision making about whether a proposed district is likely to be successful and provide a benefit to the entire **City**.

## **INFLECTION POINT CALLS FOR CAUTIOUS AND PRUDENT USE OF TIF**

The City of Saint Paul will be making critical decisions in the coming months concerning development opportunities in the downtown area. At least ten buildings in the center of downtown will be candidates for redevelopment. There will be increasing pressure to utilize TIF despite the negatives associated with its use. Many have expressed concern that TIF has been overused and that City goals for its use have not been accomplished. The cautious and prudent analysis of upcoming TIF proposals is a wise course of action. The long-term financial health of the City is at stake.

## **SAINT PAUL'S USE OF TIF HAS FINANCIALLY STRESSED ITS TAXPAYERS**

Saint Paul seems poised to again use Tax Increment Financing (TIF) to help solve its high-stress fiscal environment. The city is in this situation largely from many years of TIF overuse while accepting debt to create quick development. It feels good to build new, but when that occurs using public subsidy and without adequate demand, new development depletes existing tax base and pushes out existing taxpayers. Over the long term, additional taxes are required to pay for the debt and in turn drive away even more user demand. Saint Paul is now the largest user of TIF in Minnesota, a state that already ranks high nationally in taxes. We are unable to carry even more of this burden.

Our city has not been forthcoming on its extensive use of TIF. Unlike Minneapolis, Saint Paul has not disclosed publicly any details about its many TIF districts.

#### **WHAT YOU SHOULD KNOW ABOUT TIF:**

- Tax increment financing (TIF) is a gift to a developer but paid for over many years by city taxpayers. Those taxpayers have no say in the debt burden placed on their property. They are not aware of such payments that must be paid, without the debt even identified in the city budget or reports.
- TIF is a primary reason for our Downtown's high level of vacancy.
- Almost one billion public dollars have been used to pay principal and interest over 42 years to service TIF Districts.
- While creating service needs, TIF Districts do not contribute to the costs of city services. If TIF Districts didn't exist, homeowners for an average value of \$275,000 would save \$13.6% or \$565 each year in service costs.

#### **WHAT WILL INSIGHT ST. PAUL BE DOING NEXT:**

- We will broadly define what a successful TIF District is.
- We will be analyzing past TIF Districts to determine what things make a district successful, and what things may have made a district unsuccessful (captured increments did not fully cover debt service).
- We will be advocating the early decertification of successful districts.
- We will be recommending TIF District Creation Policy Statements for formal adoption by both the St. Paul Housing and Redevelopment Authority and the St. Paul Port Authority.
- We will be seeking public access to important TIF District history, reports, projections and policies on both the HRA and Port Authority websites.
- We will be analyzing future proposals for new TIF districts and then provide elected policy makers with both our concerns and positive suggestions.
- We will be monitoring outstanding TIF Bond Issues and Pay-As-You-Go Notes.
- We will seek to have all those obligations included in a Comprehensive Debt Policy for the City of St. Paul

