Senate Fiscal Agency
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BILL ANALYSIS

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Senate Bill 992 (as enrolled) **PUBLIC ACT 269 of 1996**
Senate Bill 993 (as enrolled) **PUBLIC ACT 270 of 1996**
House Bill 5072 (as enrolled) **PUBLIC ACT 271 of 1996**
Sponsor: Senator Mat J. Dunaskiss (Senate Bill 992)
Senator Leon Stille (Senate Bill 993)
Representative Gregory E. Pitoniak (House Bill 5072)
Senate Committee: Economic Development, International Trade and Regulatory Affairs
House Committee: Local Government

Date Completed: 8-7-96

RATIONALE

Under various statutes, tax increment financing authorities (TIFAs) are permitted to "capture" the growth in tax revenue in a designated development area for improvements to a variety of public facilities, such as streets, parks, parking facilities, and recreational facilities. These improvements typically are financed through bond issues that are repaid from the increased tax revenue. Since school financing reform measures reduced local property taxes following the approval of Proposal A in March 1994, TIFAs have been allowed to capture State and local school taxes as necessary to repay "eligible advances", "eligible obligations", and "other protected obligations". "Eligible obligations" are those obligations lawfully issued before August 19, 1993, and "other protected obligations" are those obligations issued after August 19, 1993, but before December 31, 1994, that meet certain other requirements. In addition, the Legislature is required to appropriate funds to a TIFA if the reduction in taxes as a result of school finance reform makes the captured tax increment revenue insufficient to repay an eligible advance or eligible obligation. (These appropriations are commonly called "hold harmless" distributions.)

Although a municipality may issue refunding bonds to retire existing bonds or repay existing obligations, it could not capture school taxes or receive hold harmless distributions to pay for the refunding bonds. This restriction proved to be problematic, since the decline in interest rates has made it attractive to refund bond issues. Municipalities or authorities are able to save money by issuing bonds at lower interest rates and using the proceeds of that sale to retire or refund existing bonds that carry a higher interest rate. As the TIFA statutes were written, however, a municipality or authority that refunded an "other protected obligation" would lose the ability to capture tax increment revenues from the State and local school districts, and, if it refunded an "eligible obligation", it would no longer be eligible for State reimbursement. It was suggested that the TIFA laws be changed to allow TIFAs to refund obligations without jeopardizing their right to capture tax revenue or receive hold harmless distributions.

A second issue concerning the capture of tax increment revenue also was raised. Apparently, a municipality that had a downtown development authority tax increment financing plan in effect before Proposal A was passed inadvertently let the plan expire. When the municipality attempted to amend and expand the plan, it found it necessary to reinstate the plan first. After Proposal A passed, the municipality decided to issue bonds to capture non-school taxes but discovered that the expiration and reinstatement of the plan made it unclear as to which date was to be used to determine the base year for purposes of calculating increased tax revenue. It was suggested that the downtown development authority Act be amended to allow the municipality to use as its base year the year that the plan was originally approved, rather than the year the plan was reinstated.

CONTENT

The bills amended several acts to enable TIFAs (tax increment finance authorities, downtown development authorities, and local development finance authorities) to refund obligations for which State and local school tax revenue may be captured, without losing that revenue as a result of the refunding; and to refund obligations that are eligible for hold harmless distributions, without compromising that eligibility. Under the bills, a TIFA may issue or incur such a "qualified refunding obligation" only if, generally speaking, it will have the effect of reducing the net present value of principal and interest to be paid on the obligation being refunded, as well as the net present value of tax increment revenue and the amount of hold harmless distributions needed from the State to repay the obligation being refunded. If the State Treasurer determines that a TIFA can issue a qualified refunding obligation and does not make a good faith effort to do so, the State Treasurer may reduce the amount of the authority's hold harmless distributions or the amount of school tax increment captured.

Senate Bill 992 amended the downtown development authority Act. Senate Bill 993 amended the Local Development Financing Act. House Bill 5072 amended the Tax Increment Finance Authority Act. The bills are described in detail below.

The bills amended the Acts' definitions of "eligible obligation" and "other protected obligation" to include qualified refunding obligations, and authorize TIFAs to issue bonds to refund bonds "in advance".

Prior to amendment, the Acts defined "eligible obligation" as an obligation issued or incurred by an authority or by a municipality on behalf of an authority before August 19, 1993. The bills add, "and its subsequent refunding by a qualified refunding obligation".

The Acts' definitions of "other protected obligation" included an obligation issued to refund a bond or note that was an eligible obligation, or an obligation that was issued or incurred after August 19, 1993, and that meets certain criteria (or, under the downtown development authority Act, an obligation to purchase or develop certain real estate purchased in 1993). Under the bills, "other protected obligation" means a qualified refunding obligation issued to refund an obligation described in the existing definitions (concerning an obligation incurred to finance a project described in a TIFA plan or to reimburse a party to a development agreement for a project described in a TIFA plan). It also includes an obligation that is not a qualified refunding obligation that is issued to refund an eligible obligation, or a qualified refunding obligation issued to refund an obligation described in this provision. In addition, the term includes an ongoing management or professional services contract with the governing body of a county that was entered into before March 1, 1994, and that was preceded by a series of limited term management or professional services contracts with the governing body of the county, the last of which was entered into before August 19, 1993.

The bills define "qualified refunding obligation" as an obligation issued or incurred by an authority or by a municipality on behalf of an authority to refund an obligation if the refunding obligation meets both of the following, as calculated using a method approved by the Department of Treasury:

-- The net present value of the principal and interest to be paid on the refunding obligation, including the cost of issuance, will be less than the net present value of the principal and interest to be paid on the obligation being refunded.
-- The net present value of the sum of the tax increment revenues from State and local school taxes and distributions from the State to repay the refunding obligation will not be greater than the net present value of the sum of those tax increment revenues and distributions to repay the obligation being refunded.

The bills also amended the definitions of "obligation" to specify that an obligation does not include "those bonds that have been economically defeased by refunding bonds issued under this act".

The Acts define "initial assessed value" as the assessed value, as equalized, of all the taxable property within the boundaries of the development area at the time the ordinance establishing the tax increment financing plan is approved, as shown by the most recent assessment roll of the municipality for which equalization has been completed at the time the resolution is adopted. Senate Bill 992 amended the definition of "initial assessed value" to add that if a municipality with a population of less than 35,000 established an authority prior to 1985, created a district or districts, and approved a development plan or tax increment financing plan or amendments to a plan that expired on December 31, 1991, the initial assessed value for the purpose of any plan or plan amendment adopted as an extension of the expired plan must be determined as if the plan had not expired.

Under the Acts, an authority that is eligible to receive a hold harmless distribution for a fiscal year must file a claim for distribution with the Department of Treasury at least 30 days before the first day of the fiscal year. Under the bills, an authority must file a claim if it is eligible for a hold harmless distribution or eligible to retain tax increment revenues from State or local school taxes. Under the Acts, a claim must contain certain information, including a list of eligible obligations and eligible advances and the payments due on each. The bills require a claim to include documentation, as well as a list, of these items and to list other protected obligations.

Each bill provides that, notwithstanding any other provision of the Act, if the State Treasurer determines that an authority or municipality can issue a qualified refunding obligation and the authority or municipality does not make a good faith effort to do so, the Treasurer may reduce the amount claimed by the authority or municipality by an amount equal to the net present value saving that would have been realized had the authority or municipality refunded the obligation, or the Treasurer may require a reduction in the capture of tax increment revenues from school taxes by an amount equal to the saving that would have been realized. The bills specify that this provision does not authorize the State Treasurer to require the authority or municipality to pledge security greater than the security pledged for the obligation being refunded.

The Acts provide that, by resolution of its governing body, an authority may authorize, issue, and sell tax increment bonds to finance a development program, and the downtown development authority Act permits an authority to sell bonds to refund these bonds. Senate Bill 993 and House Bill 5072 also permit a local development finance authority and a tax increment finance authority to issue refunding bonds. All of the bills permit an authority to issue bonds to "refund in advance" obligations issued under these provisions.

In addition, the Senate bills define "assessed value" as one of the following:

-- For valuations made before January 1, 1995, the State equalized valuation as determined under the General Property Tax Act.
-- For valuations made after December 31, 1994, the taxable value as determined under Section 27a of the General Property Tax Act (which implements the constitutional assessment cap pursuant to Proposal A).

The bills are tie-barred to each other.

MCL 125.1651 et al. (S.B. 992)
125.2152 et al. (S.B. 993)
125.1801 et al. (H.B. 5072)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bills allow for the financially advantageous refunding of certain TIFA bond issues and other obligations, by permitting the continued capture of school tax revenues to pay for the new (refunding) obligations, and allowing municipalities to receive "hold harmless" distributions from the State to help pay off the obligations if needed. The bills also preserve certain management service contracts entered into under the various TIFA Acts by Ingham County and some local units of government.

Supporting Argument

Senate Bill 992 clarifies the status of a downtown development authority's plan that inadvertently expired and was subsequently reinstated. The bill allows the authority to conduct its business as if the unintended expiration had not occurred and, thus, for tax increment purposes, to base its incremental value on the initial assessed value that existed when the authority was first created (and not when it was reinstituted).

Response: Senate Bill 992 enables a local unit to circumvent an important oversight protection by allowing it to reinstate an expired TIFA without obtaining the consent of the county for the capture of county tax revenue. Such approval from the county has been required since 1994.

Legislative Analyst: L. Burghardt

FISCAL IMPACT

Local units, in which authorities refund obligations, and the State will realize decreased costs associated with refunding of the obligations. The saving will depend on the interest rate of the existing obligations and the lower interest rate obtained.

Municipalities that have a population less than 35,000 and that established an authority prior to 1985, and established a development plan or tax increment financing plan that expired by December 31, 1991, will be able to capture some county tax revenue.

Fiscal Analyst: R. Ross