

BEFORE THE DEPARTMENT OF REVENUE
OF THE STATE OF MONTANA

In the matter of the adoption of New)	NOTICE OF ADOPTION
Rules I (42.19.1401); II (42.19.1402);)	
III (42.19.1403); IV (42.19.1404); V)	
(42.19.1405); VI (42.19.1406); VII)	
(42.19.1407); VIII (42.19.1408); IX)	
(42.19.1409); X (42.19.1410); XI)	
(42.19.1411); and XII (42.19.1412))	
relating to local government tax)	
increment financing districts (TIFD))	

TO: All Concerned Persons

1. On March 27, 2008, the department published MAR Notice No. 42-2-793 regarding the proposed adoption of the above-stated rules at page 548 of the 2008 Montana Administrative Register, issue no. 6.

2. A public hearing was held on April 23, 2008, to consider the proposed adoption. Oral and written testimony received at the hearing and subsequent to the hearing is summarized as follows along with the response of the department:

COMMENT NO. 1: Mr. Brent Brooks, representing the City of Billings stated the City of Billings has one basic difficulty with the rules, which is the rules assume that there is overall supervisory authority of the Department of Revenue over the creation of tax increment finance districts both at the county and the city level. He has not seen any case or any statute that says the Department of Revenue will have other than its own required statutory responsibilities in the tax increment finance districts. These are very limited and very specific statutes. It is the position of the City of Billings that without the specific direction of the Legislature, the Department of Revenue is proceeding with unauthorized and therefore, unlawful rulemaking.

Mr. Brooks further stated that there is at least some attempt to exercise some control over zoning that may have occurred at the city or the county level. This is something that is appropriate only for the Legislature to determine the extent of the Department of Revenue's supervision over tax increment finance districts. The City of Billings' position is that the Department of Revenue should hold in abeyance any final rulemaking that it may engage in pending the termination and final resolution of the Fallon County litigation.

RESPONSE NO. 1: These rules are the result of a cooperative effort between the state and local governments and represent the general consensus reached by that cooperative effort. The rules were drafted with the separate and distinct rights and duties of both the state and local governments in mind. The rules have been reviewed by the Legislative Services Division and they have been found to conform with the department's authority as defined by the Legislature.

The department's authority to adopt these rules is based upon Montana's

Constitution and 15-1-201, MCA. The rules conform with the constitutional mandate of Article VIII, Section 12 to "insure strict accountability of all revenue received and money spent by the state and counties, cities, towns and all other local governmental entities." The rules allow the department to exercise the Legislature's grant of "general supervision over the administration of the assessment and tax laws of the state;" the department's duty to "confer with, advise, and direct officers of municipal corporations concerning their duties, with respect to taxation, under the laws of the state," and "the duty of all public officers to fill out properly and return promptly to the department all forms and to aid the department in its work," all of which are provided for in 15-1-201, MCA.

The annual certification of property values within each taxing jurisdiction is an important function of the department. If the department fails to adopt rules relating to its certification of tax increment financing district values, the validity of its decisions relating to those districts may be challenged (see Minnesota Power and Light Company v. Department of Revenue). It is in the interest of local governments and their bond holders that a formally adopted set of rules relating to the department's certification of tax increment financing district values exist and that the department's decisions regarding such certification be consistently made based upon those formally adopted rules.

The rules do not, and are not intended to, provide the department with any control over a local government's exercise of the local government's statutorily granted authority. The rules are designed to create a check-list of the statutorily prescribed steps a local government must take in order to create a valid tax increment financing district and to redirect state revenues that would otherwise be directed to the general fund and school equalization. These rules simply require local governments to provide the department with documentary proof that a valid tax increment financing district has been created before the department may allow state and other property tax revenues to be redirected.

The department does not believe it is in the best interest of the parties involved with and affected by the proposed tax increment financing rules to hold the rulemaking process in abeyance pending the outcome of the Fallon County litigation. On the contrary, these rules facilitate the consistent and effective use of tax increment financing by compiling the statutory requirements into one comprehensive list. The rules constitute a helpful guide to allow all local governments the ability to properly utilize tax increment financing as an effective economic development tool.

COMMENT NO. 2: Ms. Linda Stoll, representing Missoula County stated the County strongly objects to the proposed rules requiring copies of growth policies and zoning ordinances as part of the submittal requirements for the department's taxable value certification. The implication of having local governments submit zoning and growth policy documents after those governments have certified compliance with zoning and growth policy suggests that the Department of Revenue will be assuming a position of judgment over a purely local matter of policy. We suggest that the statutory requirements for such certification (from governing bodies and planning boards) are sufficient for the purpose of determining compliance.

RESPONSE NO. 2: Current tax increment financing law establishes specific

zoning requirements. By law, a local government is required to have adopted a growth policy in order to legally exercise its zoning authority. Current tax increment financing law further requires a local government's tax increment financing plan conform with the local government's growth policy. Proper zoning and the adoption of a growth policy are both prerequisites to the establishment of a valid tax increment financing district and, therefore, documentary evidence of both should be provided to the department before the department is required to redirect tax revenues that would otherwise be directed to the general fund and school equalization.

The department has become aware of at least one instance where a local government has asserted, as part of its request for certification of tax increment financing district values, that it had properly zoned the land within the district when, in fact, it had not. The Legislature has established specific requirements that a local government must meet in order to establish a valid tax increment financing district. These rules allow the department to ensure that those requirements have been met before state tax revenues are redirected to the tax increment financing district for use by the local government.

With regard to the comment concerning the implications of local governments submitting zoning and growth documents to the department, please see paragraph 3 in Response No. 7.

COMMENT NO. 3: Linda Stoll provided comments pertaining to the definitions of "secondary value-adding industry" and "value added". She stated those two definitions narrow the uses available in industrial districts. Current law requires the use to be tied to the underlying zoning of industrial or light industrial property. Such limitations may restrict economic development opportunities for local governments. Missoula County is curious if the department has had any experience related to the property tax administration and function of the TIFD that requires defining those two terms? If the answer to that is yes, they would like to know more about that.

RESPONSE NO. 3: Section 7-15-4299, MCA, requires that an industrial tax increment financing district "has as its purpose the development of infrastructure to encourage the growth and retention of secondary, value-adding industries." The definitions of "secondary value-added industry" and "value added" are consistent with other current statutorily established definitions of those terms.

The department is aware of at least one situation in which a local government attempted to create an industrial tax increment finance district, the intent of which was to develop infrastructure for service related and general commercial development rather than the statutorily mandated secondary-value added industrial development.

COMMENT NO. 4: Linda Stoll offered an amendment to New Rule VII (42.19.1407), which relates to the determination of the base year taxable value for a newly created TIFD. She stated Missoula County appreciates the department's desire to clarify the timing of this calculation and would suggest inserting the word "calendar" to the definition so it would read: "If the notice or supporting documentation, or both, required by New Rule III through New Rule VI is received by the department on or

before February 1 of the calendar year following the creation of a valid TIFD, the department will determine the base year taxable value of the district as of January 1 of the calendar year in which the valid TIFD was created".

RESPONSE NO. 4: The department agrees with Ms. Stoll and that adding the word "calendar" to the definition would aid in the clarification. The rule has been amended below.

COMMENT NO. 5: Linda Stoll offered testimony and a suggested amendment regarding New Rule XI (42.19.1411), determination of base year taxable values of an amended TIFD. She stated the proposed language under (2) could lead to calculations of negative incremental value when property is removed from the district because the base value is not going to be changed. For example, let's say a local government creates an industrial TIFD from undeveloped land, zoned light industrial, with a total value of \$100,000. Then the zoning changes to commercial on half the land, while it is still undeveloped, and the newly zoned commercial half needs to be removed from the TIFD. Under the proposed rules, the base value remains \$100,000, but the market value will be \$50,000 if half of the property is removed. This would create a "negative increment" which does not make sense in this context. Missoula County suggests the language be changed to say that the base value of the TIFD is amended when property is removed. Or perhaps at the least, a statement could be inserted that the incremental value could not be negative due to boundary amendments.

RESPONSE NO. 5: Section 7-15-4283, MCA states "incremental taxable value means the amount, if any, by which the actual taxable value at any time exceeds the base taxable value." Based on this definition, a "negative incremental value" cannot exist, therefore, the department does not calculate "negative incremental values." If the current taxable value of the property located within a tax increment financing district is less than or equal to the base value, the incremental value is simply zero.

The rules relating to the calculation of base values following boundary changes simply reflect what the department is actually capable of calculating. The department can determine what the total value of all property within a tax increment financing district was at the time the district was created. However, it is generally not possible in most instances for the department to look back and determine what the value of a given parcel, building, or improvement was when a tax increment financing district was created. Additionally, the department cannot determine what centrally assessed property existed at any specific point within a district at the time the district was created. Centrally assessed property often times comprises a significant portion of the property value within a TIFD. For these reasons, it is impossible for the department to determine with any certainty the base value attributable to property a local government may wish to amend out of a tax increment financing district. Because the department cannot calculate this value with any certainty, the department cannot adjust the base value of a district that has been amended to remove property.

COMMENT NO. 6: Mr. Mike Uda, Attorney, representing Fallon County stated they believe that these rules fly in the face of the statutes, violate principles regarding separation of powers between, for example the legislative branch and administrative branch, invade the whole rule authority of literally dozens, if not hundreds of municipalities and county governments. In fact, this is nothing more than a naked, blatant attempt to accrete power to the Department of Revenue without any statutory authority.

First, the department is attempting to adopt rules concerning economic development by local governments when its authority is expressly limited to adopting rules relating to revenue laws. Local governments appear in Title 7, the department's authority appears in Title 15. Why does the department even think it has any authority to tell local governments what to do?

Second, the department is also attempting to implement statutes in Title 7 which have nothing at all to do with the department.

Third, the department is attempting to implement statutes which involve the creation, administration, and regulation of tax increment financing districts when its only involvement with the TIFD is a property tax operation function. Mr. Uda stated that they have characterized it in their brief as a "purely and ministerial function".

Fourth, the department is attempting to adopt administrative rules in direct contravention of the finding of rulemaking authority in a legal memo issued by the Revenue and Transportation Interim Committee on February 7, 2008.

Fifth, the department is attempting to supervise the activities of local governments with no statutory authority to do so. If the Department of Revenue puts itself between the people and their elected officials on that local level, number one it removes responsibility for those local officials to do a good job because they can always blame the Department of Revenue.

RESPONSE NO. 6: Please refer to Response No. 1.

COMMENT NO. 7: Mr. Alec Hanson, Executive Director of the Montana League of Cities and Towns testified on behalf of that organization. He stated he has been in his current position for 26 years and he has been involved in a lot of the history of tax increment finance districts in the state of Montana. He said he sees no reason in the world to monkey around with tax increment financing as it applies to urban renewal. We have a track record, it is very effective, there have been very few problems and it has produced results. He stated the validity of these rules depends on a very careful separation of the administrative functions of local government, which the Department of Revenue has no jurisdiction over, and the department's authority to administer the tax laws of the state of Montana. He further stated he would argue that some of the proposed rules directly interfere with the administrative functions of local government. He stated he does not see any reason in the world why the Department of Revenue should be reviewing and passing judgment on local government zoning policy and growth policies. There has to be a very careful separation of the administrative responsibilities of local government and whatever tax authority the department asserts in regard to tax increment financing. He said that he would agree that if the boundary of a district is changed, the base year value ought to be adjusted to account for that change. The reason that is so important is because a lot of times when these districts

are put together the financing and bonds are issued to pay for the improvements, there is a contract obligation in which the bond holders interest has to be protected.

He said the rules have to be looked at in light of the failure of HB 832 in the last session of the Legislature. Possibly that bill could be revisited in the 2009 session.

RESPONSE NO. 7: The department agrees that tax increment financing as it relates to urban renewal is generally well established and has operated relatively smoothly in the past. However, the use of tax increment financing as an economic development tool for urban renewal as well as industrial and technological infrastructure development is increasing rapidly.

It has come to the department's attention that, with the increased use of tax increment financing, avoidable errors in the creation and documentation of tax increment financing districts are also increasing. These rules set-out in a very straightforward manner the statutorily established steps that must be taken in order to create a valid tax increment financing district. For this reason these rules support the effective and expanded application of TIFD by local governments in Montana.

As noted in Response No. 1, these rules have been drafted to maintain the separation between the department's administration of state tax laws and a local government's exercise of its statutorily prescribed authority. The department does not intend to pass judgment with regard to a local government's policies governing growth, zoning, or any other matter. Nothing in these rules allows the department to exercise control over a local government's statutorily granted authority – they simply provide a method by which the department can ensure that the statutory tax increment financing requirements have been met and a valid tax increment financing district has been legally established.

The rules relating to boundary changes have been drafted to acknowledge a local government's need to ensure that its bond holder's contractual interests are protected.

The department is aware of HB832 and participated in the research and drafting of that bill. The department expects to participate cooperatively in any future attempts to pass legislation relating to tax increment financing. However, these rules reflect the current state of tax increment financing law. A proposed bill not enacted, such as HB832, does not affect the administration of current law.

COMMENT NO. 8: David Nielsen, City Attorney, City of Helena, submitted an electronic mail that was read into the record which states: He stated he had reviewed the rules on the TIFD and noticed that New Rule IX apparently gives authority to local governments to change boundaries on TIFDs. He stated that he believes the rule is too broad in its language because he doesn't think some boundary changes are permissible. For urban renewal the city has to define an urban renewal area. The city then, after hearing, establishes an urban renewal project that is only for the benefit of the urban renewal area. He further stated that he couldn't imagine that the urban renewal area would be defined as an area larger than what the TIFD would be established for. So enlarging boundaries is not as simple as voting to make it larger. He stated that he believes the process of defining an urban renewal area starts over again. He stated that he agrees that the statute doesn't address enlarging boundaries but with a strict method of defining the urban renewal area and the urban

renewal project that can only be done in an urban renewal area or its enhancement. He stated that he thinks New Rule IX may mislead cities into thinking they can easily enlarge the boundaries. If the TIFD is larger than the urban renewal areas then the taxpayers in the fringe are carrying the increment for the projects that can't benefit their property.

RESPONSE NO. 8: The department agrees with Mr. Nielsen that in order for a local government to amend a tax increment financing district's boundary, the local government must follow the same procedures set-out in law for the establishment of a new tax increment financing district. NEW RULE X (42.19.1410) describes the documentation necessary to prove that the statutory requirements have been met. In order to address the concerns raised in Comment No. 8, the department has amended NEW RULE IX (42.19.1409) to reference NEW RULE X (42.19.1410).

COMMENT NO. 9: Mr. Brent Brooks further stated he didn't think any of the opponents were trying to dictate to the Department of Revenue what its responsibilities generally are concerning property tax assessment. What they were saying is, let's work collaboratively together as teammates in this process rather than to usurp and override vital city and county government functions, including those like Billings that is a self-governing entity. The main reason everyone is having difficulty with these rules is they need more teamwork and collaboration on the rules so that they can be thought through first in order to identify what the real problem is and then fix it, if one exists.

RESPONSE NO. 9: Before drafting these rules, the department met several times with representatives of local government and other interested parties in informal meetings convened by the Governor's Office of Economic Development. During these meetings the parties defined the issues and problems relating to tax increment financing that needed to be addressed. As a result of the earliest meetings, the department drafted proposed rule language. This proposed language was shared with the local governments and interested parties and the department solicited comments and proposed amendments at later meetings. The comments and proposed amendments that the department received were incorporated and the resulting amended rules were those ultimately proposed in this rule adoption process. These rules are the result of an on-going cooperative effort between the state and local governments. The department agrees that this cooperative effort has been extremely beneficial and should continue into the future.

COMMENT NO. 10: Mr. Alec Hanson stated that they have worked cooperatively with the department in trying to figure out some of these issues and try to come to agreeable solutions. He stated many technical issues have been identified in the rules and he would hope that as the rules move forward there will be continued discussions, cooperation, and collaboration to make sure that if something is going to be imposed on local governments, they are practical, they will work, and from the department's side, they are defensible.

RESPONSE NO. 10: The department appreciates the comments made by Mr. Hanson and the League of Cities and Towns regarding the cooperative efforts of

everyone involved. We appreciate Mr. Hanson's efforts as well as those of all involved. The department believes that most of the issues that have been identified have been addressed. The department is committed to continued discussions, cooperation, and collaboration.

3. As a result of the comments received the department adopts New Rule II (42.19.1402); VII (42.19.1407); and IX (42.19.1409) with the following changes, new matter underlined, deleted matter interlined:

NEW RULE II (42.19.1402) NOTIFICATION OF THE CREATION OR AMENDMENT OF A TAX INCREMENT FINANCING DISTRICT - TIMING (1) A local government may establish a TIFD pursuant to the provisions of Title 7, chapter 15, parts 42 and 43, MCA.

(2) Pursuant to 15-10-202, MCA, the department is required to certify the taxable value of all property located within each taxing body.

(3) In order to provide the department adequate time to certify the taxable value of property located within a newly created or amended TIFD, the department must receive notification of the creation or amendment of the TIFD and any supporting documentation required by these rules no later than February 1 of the calendar year following the creation of the TIFD.

(4) The notification required by rule must be mailed to the Department of Revenue, Legal Services Office, at P.O. Box 7701, Helena, MT 59604-7701, with a copy to the Property Assessment Division at P.O. Box 8018, Helena, MT 59604-8018, or e-mailed to DORTIFinfo@mt.gov.

AUTH: 15-1-201, MCA

IMP: 7-15-4282, 7-15-4284, 15-10-202, 15-10-420, MCA

NEW RULE VII (42.19.1407) DETERMINATION OF BASE YEAR TAXABLE VALUE OF A NEWLY CREATED TIFD (1) The base year taxable value for the tax increment financing district (TIFD) will be determined as follows:

(a) If the notice or supporting documentation, or both, required by ARM 42.19.1403 through 42.19.1406 is received by the department on or before February 1 of the calendar year following the creation of a valid TIFD, the department will determine the base year taxable value of the district as of January 1 of the calendar year in which the valid TIFD was created.

(b) If the notice or supporting documentation, or both, required by ARM 42.19.1403 through 42.19.1406 is received after February 1 of the calendar year following the creation of a valid TIFD, the department will calculate the base year taxable value of the district as of January 1 of the year in which the documentation was received. In these instances, the base year will be reported to the affected taxing jurisdictions by the first Monday in August of the calendar year following receipt of the notification.

(c) The base year taxable value of a TIFD may only be calculated as provided for in (1)(a) and (b).

AUTH: 15-1-201, MCA

IMP: 7-15-4284, 7-15-4285, 15-10-420, MCA

NEW RULE IX (42.19.1409) NOTIFICATION OF AMENDMENT OF BOUNDARIES OR CHANGES WITHIN AN EXISTING TAX INCREMENT FINANCE DISTRICT - NEWLY TAXABLE PROPERTY

(1) A local government that has amended the boundaries of or made changes within a valid TIFD pursuant to the provisions of Title 7, chapter 15, parts 42 and 43, MCA, shall ~~report the amendment~~ submit the information described in ARM 42.19.1410 to the department in the manner described in ARM 42.19.1402.

(2) Property that is removed from a TIFD as a result of an amendment or change shall be considered newly taxable property pursuant to 15-10-420, MCA.

AUTH: 15-1-201, MCA

IMP: 7-15-4282, 7-15-4284, 15-10-420, MCA

4. Therefore, the department adopts New Rule II (42.19.1402); VII (42.19.1407); and IX (42.19.1409) with the amendments listed above and adopts I (42.19.1401); III (42.19.1403); IV (42.19.1404); V (42.19.1405); VI (42.19.1406); VIII (42.19.1408); X (42.19.1410); XI (42.19.1411); and XII (42.19.1412) as proposed.

5. An electronic copy of this Adoption Notice is available through the department's site on the World Wide Web at www.mt.gov/revenue, under "for your reference"; "DOR administrative rules"; and "upcoming events and proposed rule changes." The department strives to make the electronic copy of this Adoption Notice conform to the official version of the Notice, as printed in the Montana Administrative Register, but advises all concerned persons that in the event of a discrepancy between the official printed text of the Notice and the electronic version of the Notice, only the official printed text will be considered. In addition, although the department strives to keep its web site accessible at all times, concerned persons should be aware that the web site may be unavailable during some periods, due to system maintenance or technical problems.

/s/ Cleo Anderson
CLEO ANDERSON
Rule Reviewer

/s/ Dan R. Bucks
DAN R. BUCKS
Director of Revenue

Certified to Secretary of State July 7, 2008

