

Tax Increment Financing and Tax Incremental Districts in South Dakota: Guidelines for Creation, Classification, and Annual Certification

Prepared by the South Dakota Department of Revenue
Property and Special Taxes Division
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INTRODUCTION

Tax Increment Financing (“TIF”) is a means of financing public improvements in a defined geographic area, known as a tax incremental district or “TIF district.” A TIF district can be created by either a municipality or county (“governing body”).

Governor Dennis Daugaard issued an “Executive Directive Pertaining to Tax Incremental Finance Districts” to the Department of Revenue (“Department”) on March 6, 2017, directing the Department to develop guidelines for local authorities to utilize to eliminate inconsistencies in TIF project process and classification. In addition, the Department was directed to create an annual report of all TIF projects to provide better transparency for the public and policymakers.

The following guidelines are divided into three general categories related to TIF projects: creation, classification, and annual certification. **Section 1** explains the statutory process for creating a TIF district. **Section 2** establishes the procedure for classifying a TIF district for purposes of the state-aid to education formula. This procedure includes a pre-submission process for the governing body to consult with the Department regarding TIF district classification *prior to* governing board approval of the district. **Section 3** details the annual certification process, including a description of TIF project information that must be submitted to the Department for compilation of an annual report of all TIF projects in South Dakota.

SECTION 1: CREATING A TIF DISTRICT

The specific procedures for creating a TIF district are outlined in SDCL ch. 11-9. The following is a brief summary of the process. Governing bodies should consult legal counsel throughout the process of creating a TIF district.

Preliminary Steps

- The planning commission of the governing body is required to hold hearings on the necessity of the TIF district. SDCL 11-9-3.
- Notice of the hearing must be published not less than ten nor more than thirty days from the date of the hearing. In addition, notice must be mailed to the chief executive officer of every entity authorized to levy taxes on property within the proposed boundaries of the TIF district. SDCL 11-9-3.

- If the planning commission determines the TIF district is needed, the commission must recommend creation of the district, designate the proposed boundaries of the district, and submit such recommendations to the governing body. SDCL 11-9-4.
- Further, pursuant to SDCL 11-9-13, the planning commission must adopt and submit to the governing body a project plan that includes:
 - The kind, number, and location of all proposed public works or improvements;
 - An economic feasibility study;
 - A statement regarding the fiscal impact upon all taxing entities in the TIF district; and
 - A description of the financing for the proposed project.

Governing Body Approval

- The governing body receives the recommendations from the planning commission and considers whether to approve the recommendations.
- If the recommendations of the planning commission are accepted, the governing body is required to adopt a resolution officially creating the TIF district. The resolution creating the TIF district must name the TIF district, specify the legal description boundaries of the TIF district, and adopt a project plan for the public improvements within the TIF district. SDCL 11-9-5.
- Additionally, SDCL 11-9-8 requires that the resolution must contain the following specific findings:
 - (1) Not less than twenty-five percent, by area, of the real property within the district is a blighted area or not less than fifty percent, by area, of the real property within the district will stimulate and develop the general economic welfare and prosperity of the state through the promotion and advancement of industrial, commercial, manufacturing, agricultural, or natural resources; and
 - (2) The improvement of the area is likely to enhance significantly the value of substantially all of the other real property in the district.

Certification of Base Value

- The municipal Finance Officer or County Auditor must submit a written request to the Department to certify the **base value** of the TIF district. SDCL 11-9-20. This is the assessed value of the property that is within the TIF district as of the date it was created, as last certified by the Department as of the date the request for determining the base value is received.
- The request to certify the base value should be submitted as soon as possible after the creation of the TIF district and must include all pertinent information related to the district (resolution, project plan, and certification request form).

SECTION 2: TIF DISTRICT CLASSIFICATION

The primary purpose of TIF district classification is to determine how the increment value generated within the TIF district is treated in the state-aid to education formula.

The assessed value of a TIF district for state-aid purposes is the total assessed value of the district (base + increment = total assessed value). SDCL 13-13-10.8. What this means is that the total assessed value of a TIF district is counted as “local effort” when calculating the amount of state-aid any school district within a TIF district will receive. However, since the school district does not receive any tax revenue from the increment value, the County Auditor is required to impose an additional levy on all real property within the school district to hold the district harmless. SDCL 10-12-44(1). The effect is that all property owners within an impacted school district pay slightly higher school property taxes during the life of a TIF district.

An exception exists for TIF districts created for industrial, economic development, or affordable housing purposes. See SDCL 13-13-10.2 and SDCL 13-13-10.9. For these types of TIF districts, the assessed value for state-aid purposes is only the base value as certified by the Department. Any increment value is not considered in the state-aid to education formula. The effect is that all real property owners across the entire state pay slightly higher school taxes to make up for the reduction in local effort.

The Department is providing the following guidelines to ensure consistent classification of all TIF districts across the state. Further, the Department is establishing a pre-submission procedure to assist local authorities with TIF district classification prior to governing body approval of a district.

The four types of TIF districts are Local, Industrial, Economic Development, and Affordable Housing.

Local

Local TIF districts are created for purposes other than industrial or economic development. Many communities have used Local TIF districts to make public infrastructure improvements for various reasons, including housing development. The defining feature of a Local TIF district is that the project generally is for the benefit of the local government creating the district, as opposed to having a regional or statewide benefit.

Local TIF districts are not presently defined in statute. Rather, a Local TIF district is the default classification. Unless the TIF district meets the statutory definition of an Industrial, Economic Development, or Affordable Housing TIF district as provided in SDCL 13-13-10.2 or 13-13-10.10, it is a Local TIF district.

The assessed value of a Local TIF district for purposes of the state-aid formula is the total assessed value of the district. The County Auditor is required to impose an additional school levy on all real property within any impacted school district to hold the district(s) harmless.

Industrial or Economic Development

Pursuant to SDCL 13-13-10.10, Industrial or Economic Development TIFs “include only those areas where there is or will be one or more businesses engaged in any activity defined as

commercial or industrial by the governing body that has zoning authority over the real property contained within the tax increment financing district.”

Both Industrial and Economic Development TIFs are exempt from the provisions of SDCL 10-12-44(1) that require the County Auditor to impose an additional school levy on real property within the district. Any increment value in an Industrial or Economic Development TIF district is not considered in the state-aid to education formula.

Examples of Industrial TIF districts include districts created to finance public infrastructure for ethanol plants and manufacturing facilities.

Examples of Economic Development TIF districts include districts created to finance public infrastructure for commercial/retail development.

Affordable Housing

During the 2018 Legislative Session, the legislature created a fourth TIF district classification for Affordable Housing. In the past, many communities created TIF districts for housing development, but classification has been inconsistent depending on when and where the district was created. The criteria for an Affordable Housing TIF are as follows:

- The original selling price of any house in the TIF district will be at or below the first-time homebuyer purchase price limit being used by the South Dakota Housing Development Authority as of the date the house is sold; or
- The monthly rental rate of all multi-family housing units in the TIF district will be at or below the calculated rent for the state’s eighty percent area median income, being used by the South Dakota Housing Development Authority, as of the date the TIF district is created, for a minimum of five years following the date of first occupancy.

SDCL 13-13-10.10. Like Industrial and Economic Development TIF districts, Affordable Housing TIF districts are exempt from the provisions of SDCL 10-12-44(1) that require the County Auditor to impose an additional school levy on real property within the district. Any increment value in an Affordable Housing TIF district is not considered in the state-aid to education formula.

Pre-Submission Classification Procedure

To ensure consistent and uniform TIF district classification, the Department will now assist local authorities in making a preliminary classification determination prior to the TIF district being approved by the governing body. This procedure applies to any TIF district created on or after June 1, 2017 and is intended to eliminate inconsistencies and prevent future disagreements.

The request should be in writing and include the following:

- Proposed boundaries and map of the TIF district, if available;
- The purpose of the proposed TIF district, including a description of the proposed public improvements; and

- Contact information of any person(s) who can provide additional information to the Department if necessary.

**Requests should be mailed/mailed to: SD Department of Revenue
Property and Special Taxes Division
445 E. Capitol Avenue, Pierre SD 57501
DOR.PropTaxIn@state.sd.us (note “TIF
classification” in the subject line)**

Upon receipt of the above-information, the Department will determine the preliminary classification of the proposed TIF district and communicate its decision to the local authorities in writing within **ten business days**. This determination will remain in place unless there are substantive changes made to the purpose of the TIF district prior to final governing body approval.

The Department requests that all TIF districts be pre-submitted for classification, even if the governing body knows the TIF is a Local TIF district. This will help ensure proper tracking of all TIF districts in the state and give the Department notice of the TIF district earlier in the process.

SECTION 3: ANNUAL CERTIFICATION

The Department is required to annually certify the total assessed value of all TIF districts. SDCL 11-9-24. This ensures that both the Department and local authorities have accurate information regarding the amount of **increment value** in each TIF district. The **increment value** is any value above the **base value**. SDCL 11-9-1(10). The following example shows how it works:

- A TIF district is created and the total assessed value of all the properties within the boundaries of the TIF district is \$100,000. This would be the **base value**.
- The following year, construction takes place within the TIF district and now there is a total assessed value of all properties within the boundaries of the TIF district of \$450,000.
- This would produce an **increment value** of \$350,000 (current value of \$450,000 less the base of \$100,000 = \$350,000).

Property taxes generated from the **base value** are distributed to all of the taxing districts that can tax the property in the same manner as before the TIF district was created. Property taxes generated from the **increment value** are dedicated to the repayment of the project costs related to the TIF district. Note that the **base value** and **increment value** are taxed the same. Only the distribution of tax revenues varies in a TIF district.

The annual certification occurs in the fall after the Department has certified the aggregate assessed value of all real property in the state. SDCL 10-11-51.

As part of the annual certification, the Department will be compiling an annual report of all TIF districts. This annual report will include project descriptions and timelines, financial information, and an analysis of the fiscal impact of TIF districts on the state-aid to education formula. Additionally, the annual report will provide the increased assessed value for each dissolved TIF

district as of the date of dissolution. Most of the information necessary for compiling the annual report will be collected at the time of initial certification. However, the Department may request additional information from local authorities if needed. See SDCL 11-9-48.

CONCLUSION

The use of TIF districts in South Dakota has increased significantly over the last decade. Due to this rapid growth in the number of TIF districts in the state and the impact of TIF districts on property owners and the state-aid to education formula, it is critical that a consistent process and uniform classification is occurring throughout the state. These guidelines are designed to give local authorities and interested stakeholders the knowledge to satisfy these requirements.

For more information on TIF districts, please contact the SD Department of Revenue, Property and Special Taxes Division, at 605.773.3311.