

June 23, 2013

Ms. Patsy Horton
Long Range Planning Manager
Community Planning and Development Services
City of Rapid City

Dear Patsy:

Many thanks for taking time to speak with me last Thursday. Because I had many questions about TIF 74 and your time was limited, you asked that I submit my questions in writing. Here they are. Because some questions will not be easy to answer, and because they cover a number of topics, I trust you will circulate certain questions to others. I encourage you to send this letter to the TIF applicants, who may have some of the information readily at hand, and who in any case are entitled to know about my concerns. Likewise, I will forward this letter to Mayor Kooiker, the news media, and others.

By nature of disclosure: I am a consulting economist with a national practice, providing economic analyses and feasibility studies to clients who engage me. I have no economic interest, vested, pending or contingent, in TIF 74. I know the Zandstras only peripherally. I have a high personal regard for Hani Shafai, and bear him no ill will for seeking subsidies from the City. What developer in his right mind would turn down free money?

As you know, when I was in the legislature years ago, I was the prime Senate sponsor of South Dakota's TIF legislation. I continue to believe that Tax Increment Financing is a legitimate tool for some development. Yet Rapid City's approach to TIFs, historically, has been chaotic and undisciplined, with the result that taxpayer funds have sometimes been squandered. Generally, when I have testified before the City Council about a proposed TIF, I have pronounced myself agnostic about the TIF itself, only suggesting that the City's discipline and due diligence leave much to be desired. I am adamantly opposed to the enactment of TIF 74. I hope the City Council acts prudently to reject this large and unjustified raid on the city treasury.

My questions and concerns fall into two general categories. The first is statutory:

Related to SDCL 11-9-7: What is the aggregate assessed value of taxable property within the city? What is the tax incremental base of all other existing districts? I know the aggregate limit is 10% of assessed value, and that Rapid City's percentage far exceeds that of any other community, but I do not know the precise magnitude of our use.

Related to SDCL 11-9-8: Can you identify the 25% of the affected area that is blighted, and explain why it is blighted? The map of the proposed

district seems to show a small area that already has been developed for residences. How will the creation of this district improve the real property values for these residences, as the law seems to require. Have appraisals or other economic analyses been performed to demonstrate that “substantially all” of the remaining district will show increases in value?

Related to SDCL 11-9-9: What diseases or crimes have been reported in the proposed district over, say, the last five years? In particular, have cases of West Nile disease been reported which can be linked to the district in any way? What other evidence exists to prove that the existing area is “...detrimental to the public health, safety, morals or welfare...” of the area? Note that blight is defined by the conditions of “...structures, buildings or improvements...” Raw or undeveloped land is not mentioned in the definition of blight. To my knowledge, there are few structures, buildings or improvements within the identified area (save a small number of up-to-date residences). Can you identify “structures, buildings or improvements” which meet the statutory requirement for defining blight?

Related to SDCL 11-9-10: This section of statute survives without amendment from the time I wrote it in 1978. In my view, the language I wrote does not justify defining the TIF 74 property as blighted. Legislative intent has weight on the decision to call this a blighted area. (Since I was not the only legislator, maybe you should ask former Senator Lyndell Petersen, who was present at the creation, for his interpretation of blight.)

Related to SDCL 11-9-13: Subsection (2) of this section requires “An economic feasibility study.” Such a study, prepared by an independent third party, would bear heavily on the vital question whether this project is feasible without a taxpayer subsidy. In searching the documents submitted with the TIF application, I have found no such independent study. Does one exist as the law requires, and if so, is it not in the public domain? (I acknowledge that it may exist, and that I have simply overlooked it. If so, please tell me where to look.)

Related to SDCL 11-9-42: This section is entitled, “Tax Increments not to be used for residential structures.” While arguably this TIF is devoted to infrastructure, it is clear that nearly all of the underlying development is for residential construction. According to the applicant, these residential structures will not be built but for the TIF. Clearly, the TIF is being “used for residential structures,” however artfully one may try to avoid this fact. Is the City prepared for litigation arising from thumbing its nose at the law?

And here are some questions related to non-statutory arguments that bear on whether authorizing this particular TIF is a good idea:

First, the development project envisions \$25 million in commercial development and \$10 million in industrial development, yet there seems to be no documentation or justification for these figures. They seem to materialize out of thin air (with a vague reference to development in 2017 and 2020). These figures do not seem to be reflected, as required, in pro forma projections. If the figures are realistic and can be documented, the financing schedule could be substantially reduced from the astonishing 20 years that is now contemplated.

Second, there are other developers in the area who are developing without a TIF subsidy. This suggests that the “increment” argument associated with this TIF is suspect, since other developers are developing without it. And how does the City justify subsidizing one developer at the competitive expense of another? One of the criteria developers claim they meet is that “The project will not provide direct or indirect assistance to retail or service businesses competing with existing businesses in the Rapid City trade area.” Clearly, the project competes with other developers, who are of course service businesses. Also, while we can’t know for sure because the developers won’t tell us, the unspecified “retail” sector (claimed in Exhibit 8 of the application to create nearly 80% of the 102 “new” jobs) will likely compete with other retailers. As is almost always the case, “new” retail jobs are seldom really new. Unless a new retailer creates new retail trade in the community (very unlikely; will you buy more food if a new grocery store opens?) they simply shift jobs from an old employer to a new one. That is why retail development is almost always prohibited by TIF laws (and South Dakota’s omission of this is a serious oversight on my part as the author).

Third, the defining characteristic of a TIF is that incremental taxes generated by the occupants of the district will go not to the City but (indirectly) to developers; in the case of TIF 74 this diversion of tax dollars continues for a breathtaking 20 years, with apparent financing costs in excess of \$10 million. Yet the project, which calls for 470 residential units and \$35 million of commercial and industrial development, will clearly require city services, including police, fire, utilities and the like. Providing these services without compensation will create an inevitable drain on the City treasury. The rest of us taxpayers must therefore make do with fewer services (unlikely), or pay higher taxes for the same services (highly likely). Any project analysis should include *both* costs and benefits, yet here only benefits are asserted.

Finally (for now), I invite your careful inspection of BankWest’s financial “commitment,” which is highly conditional. Even if all conditions are met, including some that the bank hasn’t yet specified, the loan is for three years only, not the twenty called for in the project. It specifies an interest rate of 6% if the loan is closed by June 1, 2013. That date is now passed, and interest rates are substantially higher than they were on January 31, 2013 when the bank’s letter was issued. There remains the unresolved question of whether

6% or 9% is the operative rate, as various documents are inconsistent in this regard.

In short, the original TIF 65 was controversial, and took effect without the signature of Mayor Hanks. The applicant had five years to act, and failed (thus delaying for five years any development of the district, whether subsidized or not). The first TIF was a huge error, one in which none of the existing Council members was complicit. There is no reason to compound that error now

Sincerely,

A handwritten signature in cursive script, appearing to read "Don Frank", followed by a long horizontal line extending to the right.

Don Frankenfeld
Consulting Economist
348 8441
donlfrank@gmail.com