

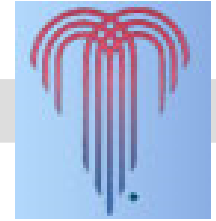


Sustainable Economic Development

May 17, 2007

**A Presentation to the City Council
City of Kansas City, Missouri**

Presenters.



❖ CSG Advisors

❖ Robert Cornwell

CSG | advisors

❖ Columbia Capital Management, LLC

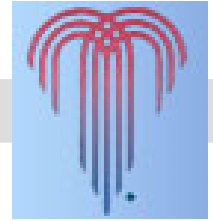
❖ Dennis Lloyd



❖ Economic and Planning Systems

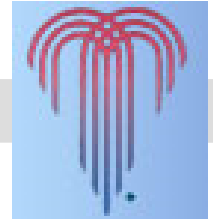
❖ Richard Berkson

Economic & Planning Systems
Public Finance Real Estate Economics Regional Economics Land Use Policy



- ❖ Recommendations geared toward enhancing the *sustainability* of the City's economic development program
 - ❖ Based upon best practices regionally and nationally
 - ❖ Policy
 - ❖ Process
 - ❖ Based upon new fiscal model
 - ❖ Aligning the right tools with the right project
- ❖ Implementation will require significant change from current practices

What is Sustainability?



- ❖ Allows the City to continue to provide targeted incentives to encourage economic growth
- ❖ Provides incentives only to those projects that need it...and only in the amount necessary to make the project feasible
- ❖ Allows the City and other governments to share immediately in the benefits of economic growth, rather than waiting 10 to 25 years
- ❖ Does not increase the burden on existing taxpayers
- ❖ Provides resources to cover operating costs resulting from new development

What Sustainability is Not?



- ❖ An absolute prohibition to the use of economic development incentives
- ❖ A set of hard and fast rules that can never be broken or changed
- ❖ A competitive disadvantage for Kansas City



- ❖ Significant economic development success in last decade
- ❖ Implications of success
 - ❖ Positives
 - ❖ Revitalized downtown
 - ❖ Exciting new entertainment, retail destinations
 - ❖ Key business recruitments and retentions
 - ❖ Kansas City has gained “caché” regionally and nationally
 - ❖ Challenges
 - ❖ Returns on investment are not known yet for many large investments
 - ❖ Significant leverage of City balance sheet (\$550+ million General Fund backed economic development bonds)
 - ❖ Significantly expanded levels of economic development incentives and increased developer expectations about incentive grants

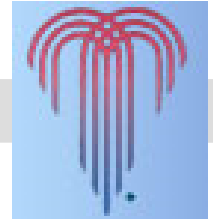


- ❖ Importance of commercial use revenues
 - ❖ 70% of City tax revenues from sales and earnings taxes
 - ❖ As a result, not all projects are created equally
- ❖ Investments in economic development are not free
 - ❖ Guarantees and foregone revenues have real costs
- ❖ City has no operative economic development strategy
 - ❖ Priorities
 - ❖ Processes
- ❖ City has fragmented investment decision process
 - ❖ Participants (City, LCRA, PIEA, EDC, IDA, Port Authority)
 - ❖ Lacks a consistent unified evaluation process



❖ General Fund guarantees

- ❖ Over \$550 million in economic development related debt; \$32 million in projected debt service payments in FY08
- ❖ \$9.6 million paid out of General Fund for debt service through FY06 to support projects not meeting revenue expectations
- ❖ Substantial risk to General Fund because payments to support debt result in a dollar-for-dollar reduction in moneys available to provide city-wide services
- ❖ To our knowledge, other major American cities do not regularly provide general fund guarantees on economic development bonds
- ❖ The City is not being compensated to provide credit enhancement



❖ Tax abatement

- ❖ Used extensively in condominium projects, especially Downtown
- ❖ Assumption in development community is that the award of abatement is almost automatic...even for the last projects in a redevelopment area
- ❖ Schools lose revenues when abatements are used
- ❖ Abatements probably distort market values for land in some markets
 - ❖ Higher sales prices (abatement assumed)
 - ❖ Squeezing out other uses

Study Findings—5.



❖ National comparisons

Tool	Kansas City	St. Louis	Chicago	Washington, D.C.	Denver	San Francisco
General Fund Guarantees of Economic Development Debt	15 Projects	1 Project (old project)	1 Project (7 yrs ago)	No	No	No
Super TIF	22 Projects (15 Active)	Yes	No	No	Yes (property & sales taxes only)	No (property taxes only)
TIF	Yes	Yes	Yes	Yes	Yes	No
Tax Abatement	Yes	Yes	Yes	No	No	No

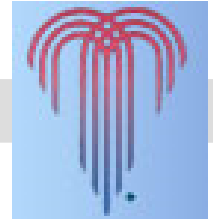
Source: Research by the study's authors; publicly available records; City of Kansas City Finance Department



❖ Special business districts

- ❖ State of Missouri Audit (Transportation Development Districts – March 2006)
 - ❖ Separate political subdivisions
 - ❖ Ability to tax and issue debt
 - ❖ 69 TDDs in the state (5 in Kansas City) – as of December 2004
 - ❖ **Disclosed numerous issues in the areas of public awareness/involvement, accountability and compliance**
 - ❖ **Other states are expressing the same concerns**
- ❖ True also for other business districts operating in KC (CID, NID)
- ❖ Great tool, but presents governance challenges for City
 - ❖ Needs to be a part of economic development policy to ensure oversight

Competition.



- ❖ Kansas City's economic development program needs to be competitive regionally to retain and recruit business
- ❖ Fortunately, Kansas City has a wide array of tools that allow it to compete with other communities
- ❖ More coordination is imperative

Economic Development Tools—Comparison.



Tool	Kansas City, Missouri	Cities in Kansas	Comparative Advantages
Tax Abatement	<ul style="list-style-type: none"> • Commercial, industrial, residential • Up to 25 years at 100% 	<ul style="list-style-type: none"> • Commercial, industrial • Up to 10 years at 100% 	<ul style="list-style-type: none"> • KCMO can abate for a much longer period as long as KS • KCMO can use abatement for residential projects; KS can't
Tax Increment Finance (TIF)	<ul style="list-style-type: none"> • Recommendation by TIF Commission; approval by City Council • Capture of up to 100% of incremental property taxes, with Super TIF, up to 100% of EATs (sales, earnings taxes), and up to 90% of hotel/motel tax • Term of up to 23 years • Generally available for all development costs and public or private improvements 	<ul style="list-style-type: none"> • Approval by City Council subject to veto of affected counties and school districts • Capture of up to 100% of property, local sales, county sales, transient guest taxes, and franchise fees • Term of up to 20 years • Generally available for all development costs and public improvements • GO-credit support sometimes permissible 	<ul style="list-style-type: none"> • KCMO can capture larger increment (earnings taxes) • KCMO can capture increment for a longer period of time • KCMO can use TIF proceeds for private construction costs • KCMO TIF plans not subject to veto by schools or counties • KS can issue GO-backed TIF bonds in some cases
State-Level TIF	<ul style="list-style-type: none"> • State TIF and MoDESA • Same basic rules as TIF • Requires approval of Missouri Dept. of Economic Development • Captures 50% of State EATs and 50% of State income tax (MoDESA) • 23 to 25 year term • Use in downtown area and for “major initiatives” 	<ul style="list-style-type: none"> • STAR Bonds • Same basic rules as TIF • Requires approval of KS Secretary of Commerce • Captures 100% of State sales tax • 20 year term • Generally requires a \$50 million capital investment and \$50 million per year in sales 	<ul style="list-style-type: none"> • MoDESA program has lengthy application process • STAR bonds' capital investment threshold is prohibitive • STAR program only used 4 times • KCMO can capture share of income tax; KS state sales tax capture higher • KCMO has longer capture period
Condemnation for Economic Development Purposes	<ul style="list-style-type: none"> • Available to TIF Commission, LCRA, Chap 353, PIEA 	<ul style="list-style-type: none"> • Not permitted without an act of the Kansas Legislature 	<ul style="list-style-type: none"> • This tool effectively no longer available in KS



❖ Description

- ❖ Estimates annual City costs, revenues and net impact of development
- ❖ Calculates and deducts City tax incentives
- ❖ Tests alternatives, forecasts results annually or at buildout

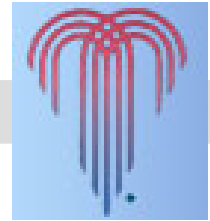
❖ Design/Approach

- ❖ Based on interviews with City departments
- ❖ Evaluation of City budget documents
- ❖ Review of market conditions and trends

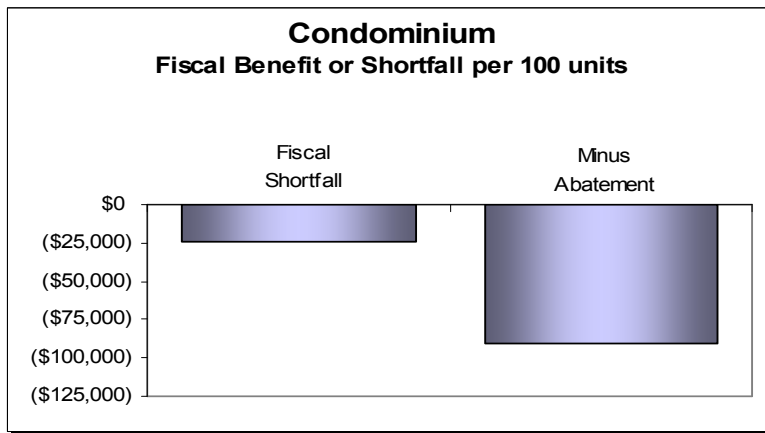
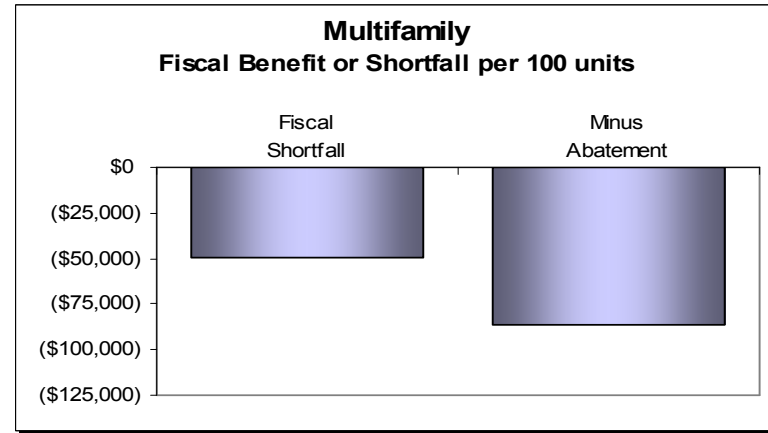
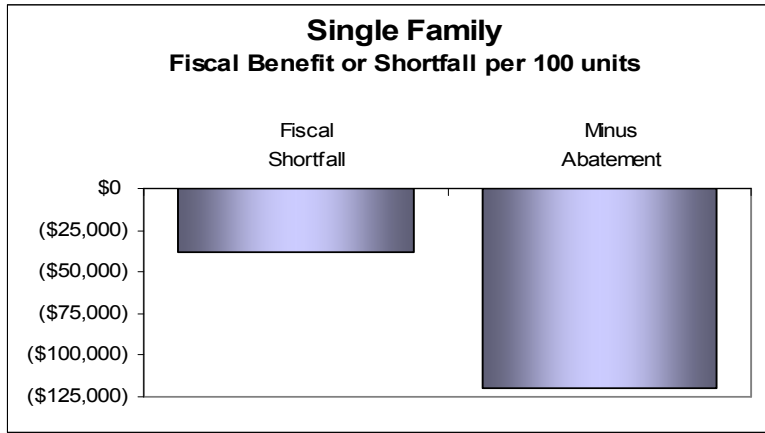
❖ Uses

- ❖ Land use or project-specific fiscal impacts
- ❖ Fiscal effects of citywide development
- ❖ Fiscal impacts of alternative TIF policies

Summary of Fiscal Model Findings—1.



Fiscal Impacts of Residential Economic Development Initiatives

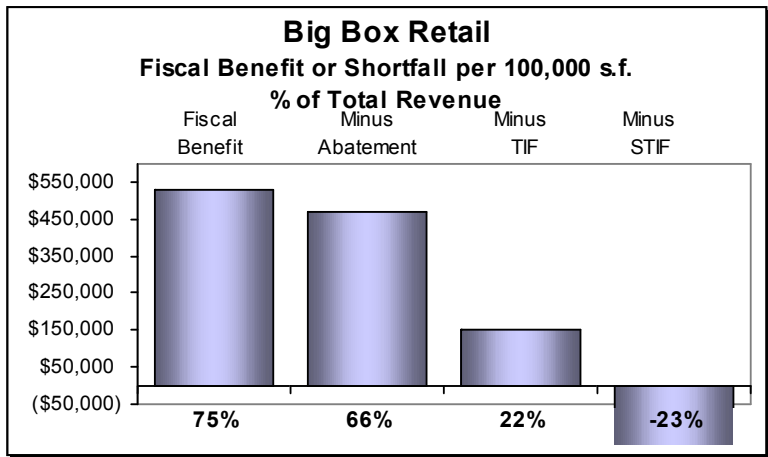
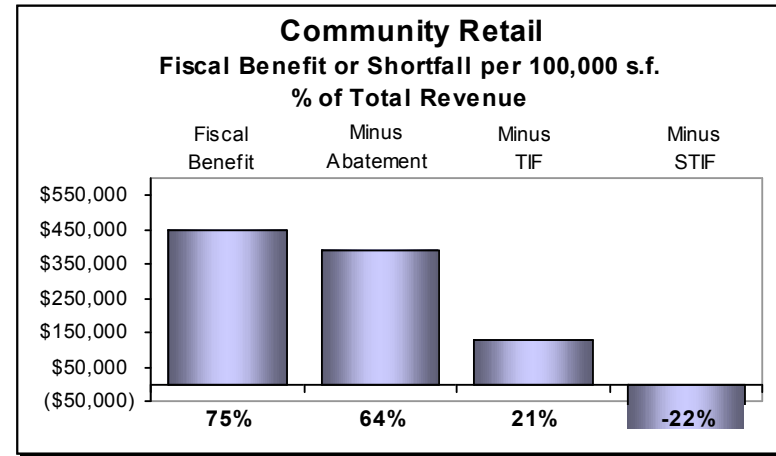
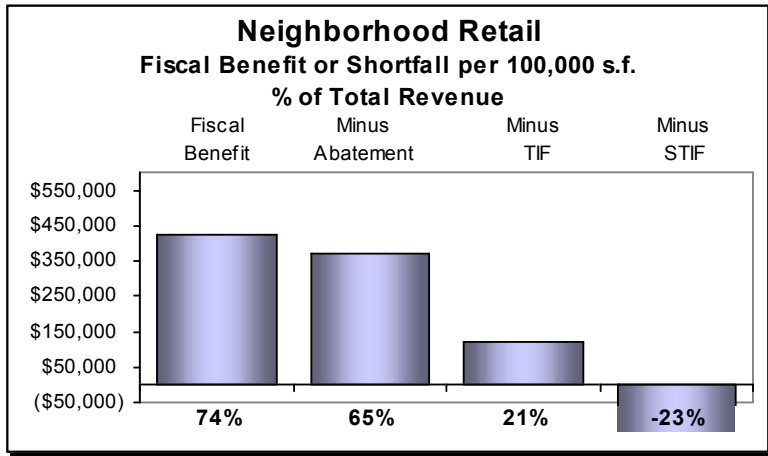


- ❖ Residential-only development negative *without* incentives
- ❖ Use self-supporting districts (NID, CID) instead

Summary of Fiscal Model Findings—2.



Fiscal Impacts of Retail Economic Development Initiatives

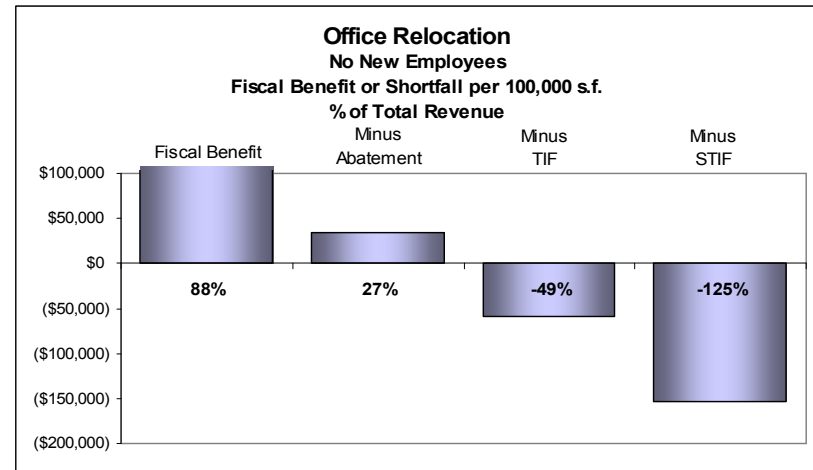
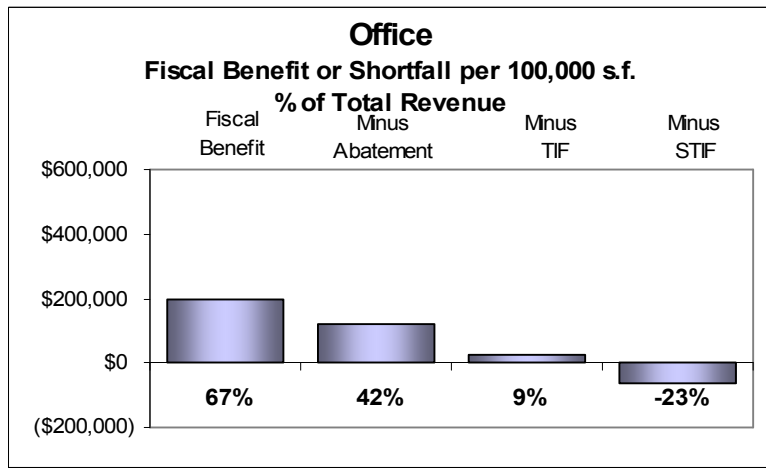


- ❖ Usually positive with some level of incentive
 - ❖ Reasonable tax abatement
 - ❖ Straight TIF
- ❖ Turns negative with SuperTIF

Summary of Fiscal Model Findings—3.

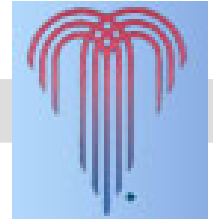


Fiscal Impacts of Office Economic Development Initiatives

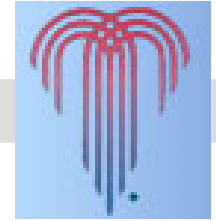


- ❖ New projects are positive with abatement and TIF, but not SuperTIF
- ❖ Relocation projects with incentives are a fiscal negative

Recommendations—Immediate



- ❖ Do not provide future general fund guarantees for economic development debt
- ❖ Do not award SuperTIF unless required to leverage State funds (State TIF and MoDESA)
- ❖ Require Council approval of individual PIEA projects and abatements
- ❖ Prohibit extension or expansion of incentives for built projects
- ❖ Implement use of self-supporting districts (CIDs, NIDs) for economic development with proper oversight
- ❖ Use the new fiscal impact analysis for *all* requests for assistance



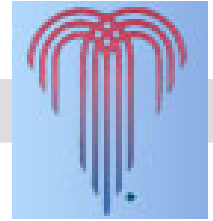
❖ Strategy

- ❖ Develop an Economic Development Plan setting priorities for location and types of desired development
- ❖ Establish an economic development incentives policy that provides more incentives for the first development in an area and no incentives after the area reaches “market conditions”
- ❖ **Establish a more rigorous “but-for” standard so that incentives are only provided to development that would otherwise not occur and provide only the level of incentives necessary to make it occur**
- ❖ **Tailor incentives by land use based on the priorities in the Economic Development Plan**
- ❖ Alter the funding of the EDC (and other partner agencies) to assure their interests are aligned with those of the City



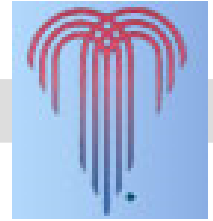
❖ Process

- ❖ All projects should be subject to a fiscal impact analysis conducted by the City's Finance Department
- ❖ **If there is any material change to a project, the fiscal impact analysis should be revised to reflect the change**
- ❖ For projects involving City-issued bonds, the City should charge an annual issuer fee against the project
- ❖ **Modify the PIEA ordinance to require council approval *both* of the creation of the PIEA district *and* any subsequent abatement**
- ❖ **Link land use approvals for an economic development project to the financial approvals through the use of a development agreement**



❖ Process, cont'd.

- ❖ Appoint a staff member in the City Manager's office with responsibility to coordinate the evaluation for all economic incentive requests
- ❖ **City financial staff involvement should begin whenever an application is submitted to any economic development agency, including PIEA, TIF Commission, LCRA, Port Authority and EDC**
- ❖ **Require passage of a single ordinance authorizing all economic development incentives granted to a project**
- ❖ Apply a single set of standards for review by all economic development agencies
- ❖ Require the creation of a service plan for special districts



❖ Sustainability

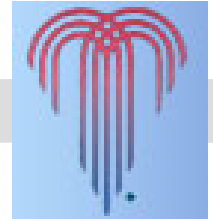
- ❖ **Allocate and prioritize incentives to commercial projects with the goal of achieving a positive margin for the City of 30% to 40% after incentives and funding services to the project**
- ❖ Provide only the amount of incentive required to make the project viable
- ❖ Provide only a level dollar amount of incentives to each project over time; do not increase incentives over the life of the project
- ❖ Significantly limit or eliminate incentives for residential projects which do not provide significant social or net fiscal benefits
- ❖ **Retain the flexibility to invest in exceptional projects without creating adverse financial consequences and major financial risks to the City in future years**



❖ Sustainability, cont'd.

- ❖ Require fiscal impact analysis for all aspects of economic development
- ❖ **Restrict the use of SuperTIF to those projects leveraging state funds through State TIF or MoDESA**
- ❖ Reduce the City's exposure to variable interest rates by converting a portion of the outstanding ED bonds to fixed rates
- ❖ Seek opportunities to convert guaranteed bonds to self-supporting TIF bonds and reduce credit exposure to ED bonds
- ❖ **Do not provide guarantees of economic development bonds**
- ❖ **Do not extend abatements or convert abatements to TIF or subsequently expand incentives**

Conclusions.



- ❖ Kansas City has terrific economic development momentum
- ❖ Economic development is not free
 - ❖ The City has an obligation to understand fiscal impacts
 - ❖ Unintended consequences
- ❖ City's economic development system needs to be streamlined; all agencies using same playbook
- ❖ A focus on sustainability will allow continued economic growth while protecting the fiscal health of the City

Contact/Additional Information.



**Dan Bagunu, Manager, Development Finance Division
City of Kansas City, Missouri
Finance Department
414 East 12th Street, 1st Floor
Kansas City, MO 64106**

**View consulting team's PPT presentations and final report at:
www.kcmo.org/finance.nsf/web/edpolicy**

**Email comments, questions to:
EDPolicy@kcmo.org**