From: Blake 01/28/2015
RE: Info. relative to SB 2375

Special Purpose Taxing Districts – Tool to Reduce the Cost of Housing & Real Estate in ND

Development Finance Challenge
Many western North Dakota communities have taken the position that they will not finance the infrastructure in a development and special assess it back to subsequent property owners due in no small measure to the amount of debt the cities carried after development ceased after 1985. (Please note: this position is not being criticized or questioned nor is it suggested to be changed.)

Side Effect - Land developers are funding projects primarily through equity and private lending. The average cost of debt capital has been described to be in the 13% to 15% range or higher. The cost of equity is easily at that rate and ranges much higher. The result is millions of dollars in added cost for the same infrastructure that could have been financed at 4-5% municipal bond rates.

Special Purpose Taxing Districts – One Possible Solution
Special District ("Special District") financing involves the issuance of tax-exempt bonds to finance public improvements within a specified geographical area, or district. Districts may construct public improvements ("Construction District") and/or purchase public improvements ("Acquisition District") that have been constructed by the developer through bond proceeds. The bonds are repaid from the special taxes, assessments, and/or an ad valorem property tax imposed on the land within the district. Property owners in the district thus finance the improvements without any city-wide taxpayer subsidy. The bonds are typically underwritten in private offerings managed by underwriting firms who specialize in this type of land-secured financing.

Special Districts are typically, but not always, separate political subdivisions from the jurisdiction that creates the Special District. The obligation to repay the Special District bonds is passed on to the end users of the property located within the Special District's boundaries. Based upon the type and location of the Special District, the district may issue general obligation, revenue, special assessment and/or special tax bonds to finance eligible public improvements. The bonds issued by Special Districts typically have terms ranging from 20 to 40 years, with tax-exempt interest rates ranging from 3 to 7 percent. Typically, the only security for the bonds is the property located within the Special District itself— no other forms of developer financial assurance is required. As the Special District is typically a separate political subdivision from that of the establishing jurisdiction, the establishing jurisdiction does not have to repay bondholders should the developer or property owners default on the debt obligations of the Special District.

Benefits:
- The City (or political sub in which the district was created) is not liable for the bonds, the Special District is the responsible party
- Special Districts cover a specific geographic area and as such there is a clearer connection between the taxes/assessments being levied by a Special District and the benefits that the residents in the Special District are receiving.
- Special District taxes / assessments are levied on an annual basis and therefore are not rolled up into the home price/mortgage as is the case with impact fees.
- Over time Special Districts draw upon a large pool of citizens to finance public infrastructure and don't place this financial burden solely on new residents as is the case with impact fees.
- Special Districts often require the preparation of an annual budget thereby making them more accountable and transparent to the residents.

- Special Districts may be used in combination with other financing mechanisms thereby accelerating the financing of public improvements in advance of growth.
- Impact fees do not readily allow for the issuance of bonds to finance the construction of infrastructure in advance of growth.

Financing Benefits

- *Non-Recourse Financing* – In most cases, Special District financings are non-recourse borrowings to the developer, meaning that if the developer defaults on the bonds, the only recourse to the Special District is to foreclose on the property. The security for the bonds is either an assessment lien on the individual lot or parcel in the case of a special assessment or special tax levy bond; an increase in the ad valorem property taxes of the property contained with the Special District in the case of a general obligation bond; or the revenue stream created by an asset financed by the Special District, such as a water treatment facility or parking garage in the case of a revenue bond.
- *Long-Term Financing* – Unlike traditional construction financing, which has a 2 to 3 year term, the typical term of Special District bonds ranges from 20 to 40 years.
- *Reduces Equity/Third Party Borrowings* – The use of Special District financing to finance a portion of the project's public improvement costs reduces the amount of equity and/or traditional lending required.
- *100% Debt Financing* – Conventional financing sources typically require equity contributions, whereas Special District financing is 100 percent debt financing. Additionally, no personal and/or corporate financial guarantees are required with Special District financing.
- *Tax-Exempt Interest Rates* – Special District bonds are issued at tax exempt interest rates and therefore are less expensive than the interest cost of borrowing from conventional sources (including potential lender participation).
- *Interest Reserves* – Special Districts may borrow up to 3 years of capitalized interest to fund debt service requirements while the project is under construction. During the capitalized interest period, property owners within the district are not required to pay debt service on the bonds as this is funded by the Special District.
- *No Acceleration Provisions* – Development loans typically have an acceleration provision in which the lender may foreclose on property for the entire loan amount; whereas with Special District financing, the district may only foreclose on the property for which the assessments and/or taxes are levied and unpaid.

Resources

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