



To: MAYOR AND COUNCIL

Agenda Item #: VIII. E

From: Scott H. Neal, City Manager

Action

Discussion

Date: May 20, 2014

Information

Subject: Authorize Financial Assistance to Fairview Southdale Hospital

Action Requested:

Authorize \$2,000,000 for financial assistance to Fairview Southdale Hospital.

Information / Background:

Background

Fairview Southdale Hospital (FSH) is engaged in a large improvement project intended to dramatically upgrade the Emergency Department. The project broke ground on September 26, 2013 and is estimated to cost \$42 million. Unlike previous improvement projects at FSH, the corporate board of Fairview Health Services has directed local leaders of FSH to solicit the public for private gifts and contributions to assist with the capital finance of the Emergency Department project.

Mayor Hovland and I met with FSH leaders on a number of occasions in 2013 to hear the details of the proposed Emergency Department project and their solicitation for public financial assistance from not only the City of Edina, but the cities of Bloomington, Richfield and Eden Prairie as well. To date, none of the aforementioned cities have committed public funds to the project.

FSH leaders made a direct appeal to the City Council for public financial assistance at the Council's September 3, 2013 work session. While the City Council did not commit to providing direct financial assistance to the hospital, the Council did ask City staff to investigate possible avenues of public financial assistance to the hospital for the Council to consider later.

Local leadership of FSH requested the opportunity to appeal to the City Council in an open Council meeting setting to reaffirm their request for financial assistance. That appeal will be made at the Council's May 20 meeting.

Request

FSH leaders have requested \$2,000,000 from the City of Edina as a contribution to the Emergency Department project. The requested contribution would be in the form of a gift/grant, which means the City

would not be repaid. If the City provides the \$2,000,000 contribution to FSH, FSH will be able to finish the interior improvements for the Chronic Care Center. If the City does not provide the requested contribution, FSH will not be able to complete the proposed interior improvements to the Chronic Care Center at this time.

There are several possible avenues available if the City Council wishes to provide the requested financial assistance to the FSH project: General Fund tax levy, HRA tax levy, Capital Improvement Program (CIP) and property tax abatement. Because FSH is exempt from local property taxes, tax increment financing (TIF) is not an available tool to assist FSH with this project.

One option is to assess a General Fund property tax levy in an annual amount over a number of years to equal the requested contribution. For example, the requested contribution is \$2,000,000. If the City Council approves an annual contribution of \$400,000 for five years, the Council would approve a designated \$400,000 property tax levy during its budget process each year for five years. Using current tax rates and projected market values, staff estimates the cost of this option for the median single family home to be an additional tax burden of \$17.50/year.

A second option would be to use the same property tax mechanism, but assess the tax from the City's Housing and Redevelopment Authority (HRA). The City's HRA does not currently impose a property tax levy, but it has the statutory authority to levy a tax for this purpose. The levy and tax burden impacts would be the same as the General Fund option. A possible benefit of the HRA levy for this purpose is that it provides a degree of transparency that is not present in the General Fund tax levy. It is more transparent than the General Fund levy because the City's sole use of the HRA levy would be for the purpose of providing the financial assistance to FSH and the HRA levy is displayed as a separate line item on a property tax bill.

A third option would be to provide cash assistance from the City's Capital Improvement Program through the Construction Fund. The budgeted beginning balance of the Construction Fund on January 1, 2014 was \$5.8 million. Staff anticipates adding \$5 million new revenue into the fund and spending \$9.4 million this year on capital improvements from the fund, for an anticipated net decrease in the balance of the fund of \$1.6 million by the end of the 2014. However, if the Council desires to provide financial assistance to FSH without creating net new tax burden, the Council could reprioritize the previously authorized projects in the CIP and authorize a cash transfer of CIP dollars to FSH.

The final option we have identified is property tax abatement. The City of Edina has not previously used tax abatement. Tax abatement in Minnesota is similar to tax increment financing (TIF) in that it redirects the flow of property taxes from the City to a private party. But it is different in two key respects. In a conventional TIF, the City is redirecting the new property taxes paid by the party that is both increasing the City's tax base and is benefitting from the TIF itself. In a tax abatement, that might also be true, but the benefitting party might also be receiving redirected property taxes from other property owners in a larger geographic area if it can be determined that adjacent properties have a connection to the improvement and

are directly or indirectly helped by the improvement. That is, in fact, what would happen in this situation if the Council ultimately approves a tax abatement benefit for FSH.

The necessary findings that form the basis of the tax abatement district are also different from the findings that are necessary for TIF. For a TIF benefit, the proposed level of assistance must meet the “but for” test. For tax abatement, the Council must declare that the benefits received by the City that are created by the project are roughly equal to or greater than the cost of the tax abatement provided by the City to the project. While bond counsel hasn’t formally reviewed this proposed transaction, they have said the tax abatement standard is easier to meet than the TIF standard and that the proposed FSH tax abatement would likely meet that test.

Like TIF, properties within a tax abatement area are not affected financially by the tool. Tax abatement involves the redirection of only the City’s portion of the property taxes payable. It does not raise or lower the tax burden or estimated market value of properties included in the tax abatement district. City Assessor Bob Wilson has estimated there is just over \$300,000 of City property taxes currently paid in the potential tax abatement district (see attached map) that could be redirected to FSH annually for the project. The Council could choose to redirect some or all of these property taxes to FSH through the tax abatement process. Alternatively, the Council could also choose to set a baseline year and commit property taxes over and above those of the baseline year to FSH through the tax abatement tool. This would require new construction or significant increases in future valuation to meet the \$2,000,000 request.

Fiscal and Process Considerations

The four identified funding options come with their own advantages and disadvantages. For example, the HRA tax levy is transparent and easy for property taxpayers to identify on their tax bills. Because it would create net new revenue, the HRA tax levy has minimal impact on the City’s other operating and capital funds.

The tax abatement option has some elements of transparency, but it is more complex to impose than a simple HRA tax levy. And, unless the Council increases the General Fund levy by the amount of the tax abatement, the tax abatement may negatively impact the City’s other operating and capital funds because it is a net transfer of existing tax dollars received by the City to FSH. This issue could be mitigated by developing a base year for the tax abatement and then committing only new property taxes received to the tax abatement district in the future, but that would substantially decrease the amount of tax abatement value available to FSH in the short run and increase the term of assistance..

The General Fund tax levy is simple to impose, but has the effect of increasing the City’s total tax levy, which makes the City less tax competitive with our neighboring cities. The Council should also consider that it has previously approved an increase of 5-7% in the proposed 2015 General Fund levy in order to fund the expected debt service for the Sports Dome project. In addition, the City’s 2015 preliminary budget

(tentatively approved by the Council in December 2013) anticipates an additional increase of 3-4% in the General Fund levy for projected increases in general operating costs for 2015.

Providing direct financial assistance to FSH from the City's Construction Fund would have an immediate negative impact on the City's ability to deliver on capital improvement projects that the Council has previously approved and that have been waiting in the funding queue for years. There is no doubt that Council and staff could reprioritize the City's current CIP to accommodate this option, but it would be disruptive to our infrastructure preservation projects and likely cause concern among residents who have been anticipating the planned projects that would need to be cancelled or delayed.

Other Considerations

There are a number of other factors the Council should consider before making a decision on this request. Some of those factors support a decision to provide the requested assistance, while others make that decision more difficult for you.

- Fairview Southdale Hospital is Edina's largest single employer. Its economic health is important to the economic health of the community. While FSH is a non-profit hospital and does not pay property taxes, its economic presence in the community is important. Its ability to grow and prosper stimulates the growth of private medical services and businesses in the community who contribute to Edina's tax base, many of whom would not be in Edina but for the presence of FSH.
- The City has not previously provided financial assistance to the hospital. It is not a common practice for cities in Minnesota to provide financial assistance to their local hospitals, unless they are organized as a municipal hospital, which FSH is not.
- The City of Edina has a strong relationship with Fairview Southdale Hospital. We have partnered with FSH on many common initiatives and interests over the years, including a very important cardiac care partnership with our Fire Department.
- FSH probably has a large share of the healthcare market of Edina residents, but it does not have 100% of that market. Does the City open itself to criticism if it provides financial assistance to FSH that is generated from taxpayers who obtain their healthcare from a system other than Fairview?
- FSH contributes positively to the community through its contributions to such things as 4th of July fireworks, membership in the Chamber of Commerce and regular direct contributions of money or equipment to our Fire Department.
- Fairview Southdale Hospital is a corporate subsidiary of Fairview Health Services. In 2013, Fairview Health Services' audited unrestricted revenue was \$3.3 billion. The City of Edina's unrestricted revenue was just over \$90 million during the same time period. Should the City provide financial assistance to a Fairview Health Services' hospital when Fairview's annual unrestricted revenue is 35 times greater than the City's?

- The City does not have a policy for how it will consider or grant financial contributions to property tax exempt non-profits. In most situations, State Statute prohibits the City from making financial contributions to non-profit organizations. There is an exception, however, that allows such a contribution to a local non-profit hospital. Should the City establish a precedent for other non-profit employers in Edina such as MN Heart Association, Volunteers of America, Children's Heartlink (all have aging facilities in the City) to enable them to request public financial assistance? Council Members should consider the precedent the City might be setting with this decision.
- As a non-profit hospital in Minnesota, Fairview Southdale Hospital is exempt from local property taxes. The state created this property tax exemption for non-profit hospitals to allow hospitals to dedicate their revenues exclusively to healthcare related costs and to help them contain their costs in order to contain the ultimate cost of healthcare for consumers. The current (2010) estimated exempt valuation of FSH is \$39,193,200. If FSH paid property taxes based on their 2010 exempt valuation and 2014 tax rates, FSH's total estimated annual property taxes payable would be \$1,550,000. Of that total, \$675,000 would have been received by City. Given that the City forgoes an estimated \$675,000 in property taxes annually from FSH, is it necessary to provide additional financial assistance to FSH for this project?

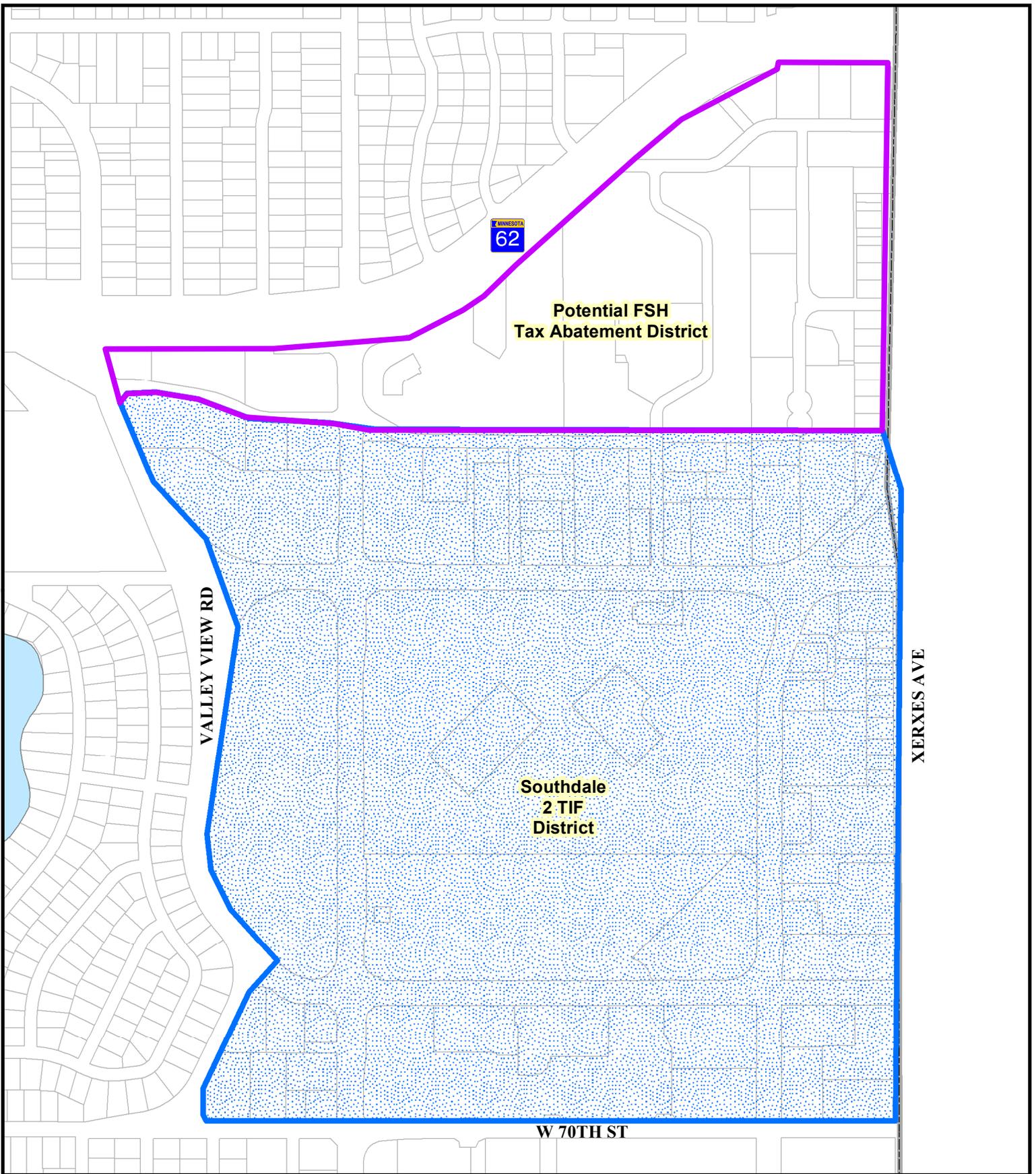
Summary

FSH's \$2,000,000 request for City financial assistance for their Emergency Department project is a request that only the Council may grant. There are tools available to the Council that could provide the requested assistance. If the Council wishes to provide FSH with the requested financial assistance, I would recommend the City impose a special HRA tax levy of \$400,000 per year for five years. The net new tax burden of \$17.50/year for the median single family taxpayer is modest, the process to impose the levy is simple and the levy is transparent to property owners. In addition, because the proposed annual levy would be static, the annual tax burden will decrease in the future years commensurate with the growth of the City's tax base.

In the long run, I also recommend the City and FSH actively collaborate to create a new fiscal tool, not unlike the Destination Medical Center concept devised in Rochester for the Mayo healthcare system, which would allow the City to more actively incent and reward Fairview Health Services to expand and improve Fairview Southdale Hospital. The medical/healthcare economy in Edina is the envy of any city in Minnesota. We should recognize and reward FSH for the important role it plays in our local economy, and for the wealth it has created in our tax base by working with them more actively in future economic development planning efforts.

Attachments:

Map of Potential FSH Tax Abatement District



Potential FSH Tax Abatement District

-  Potential FSH Tax Abatement District PIDS 582
-  Southdale 2 TIF District

