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January 12, 2016

Mike Nugent  
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*Via E-mail: [mnugent@lso.idaho.gov](mailto:mnugent@lso.idaho.gov)*

Re: *Urban Renewal Legislation*

Dear Mike:

**A. Introduction**

I write this letter at the invitation of Senator Charles Winder, who indicated that he felt it worthwhile for an Idaho bond counsel law firm to be on record regarding potential legislative changes that could impact the ability of urban renewal agencies across the State to issue bonds and notes and otherwise access capital markets. Accordingly, the intent of this letter is not to advocate on behalf of any particular urban renewal agency or to argue for or against any specific proposal, but rather to comment generally regarding the effect of potential legislative change on the ability of Idaho urban renewal agencies to access capital markets.<sup>1</sup> Further, this letter focuses on legislative changes that could affect an urban renewal agency's legal status. I understand that there are some proposals that might alter the tax increment cash flow of an urban renewal agency. Of course, any change that makes an urban renewal agency less financially strong would adversely affect its access to lending and capital markets. However, I will leave further commentary on those types of changes to the financial analysts.

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<sup>1</sup> Our firm has acted as bond counsel to a number of urban renewal agencies, but acts as general counsel only to "Ignite CDA," the urban renewal agency of the City of Coeur d'Alene.

**B. Analysis**

Legislative proposals of concern can be viewed in two categories: (1) altering the factual basis upon which the Idaho Supreme Court has ruled that an urban renewal agency is not the “alter ego” of the municipality that creates it, and (2) eliminating the eminent domain power of urban renewal agencies.

**1. It is imperative that urban renewal agencies remain separate and distinct from the municipality.**

The concern that has been raised, and in two instances rejected, by the Idaho Supreme Court is whether an urban renewal agency’s use of revenue allocation financing is really action by its sponsoring municipality -- that agencies are merely “alter egos” of their sponsoring municipalities -- and thus whether the use of revenue allocation financing by urban renewal agencies violates Article 8, §§ 3 of the Idaho Constitution. As foreign as it may seem, the Idaho Supreme Court has repeatedly held that urban renewal agencies are not fundamentally units of local government even though the statute for their creation requires a finding of necessity by the local governing body of the municipality:

[t]he legislature, in what we may assume to be an effort to maintain some local voice in the question of whether a particular municipality had a need for urban renewal, required a finding of need by a municipality prior to the time an urban renewal agency could come into existence. **While the particular city may trigger the existence of the [urban renewal agency], it cannot control its powers or operations.**

...

We conclude that the statutory provisions allowing a local voice in the creation of the [urban renewal agency] do not result in a finding that [the urban renewal agency] is simply the alter ego of the City.... **The degree of control exercised by the City ... does not usurp the powers and duties of the [urban renewal agency], and the close association between the two entities at most shows two independent public entities closely cooperating for valid public purposes.**

Urban Renewal Agency of City of Rexburg v. Hart, 148 Idaho 299, 302, 222 P.3d 467, 470 (2009) (citing Boise Redevelopment Agency v. Yick Kong, 94 Idaho 876, 881–82, 499 P.2d 575, 580–81 (1972)) (emphasis added). As a consequence, Article 8, § 3 of the Idaho Constitution,

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which mandates voter approval and a tax levy for incurrence of indebtedness is inapplicable to urban renewal agencies. .

The foundational basis for the Court's holdings in Yick Kong and City of Rexburg was the existence of the urban renewal agency as a separate and distinct entity from the sponsoring municipality. Thus, if legislative changes place more control over the agency in the hands of the municipality through its council members or otherwise, the Supreme Court's decisions would be called into question because then the facts upon which the Supreme Court based its decisions would now be changed<sup>2</sup>, In addition an unsettling of the market will occur. As the Court itself recognized:

If we were to . . . accept that urban renewal agencies are merely alter egos of their respective municipalities, we would overrule unanimous, long-standing precedent and thwart the reasonable expectations of numerous bondholders.

City of Rexburg, 148 Idaho at 303, 222 P.3d at 471.

The required degree of separation between the sponsoring municipality and the urban renewal agency could be eroded in a number of ways. First, allowing the sponsoring municipality to exercise the power of eminent domain on behalf of the agency further entangles the municipality with the agency by allowing the municipality to control a significant power of the agency. As indicated above, the lack of such control over the powers and operations of the agency was at the heart of the Court's decisions in Yick Kong and City of Rexburg. Accordingly, if such a bill is passed, it would become more difficult, if not impossible, for bond counsel to render an approving legal opinion on urban renewal agency bonds unless the bonds were approved by the electors pursuant to Article 8, § 3 of the Idaho Constitution.

Second, amending the ability of an urban renewal agency to incur debt -- for instance, by mandating the approval by the sponsoring municipality of the incurrence of agency debt -- likewise allows the municipality to control a significant power of the agency and makes it more difficult for bond counsel to render its approving legal opinion on urban renewal agency bonds unless approved by the voters.

Additional examples of problematic changes include altering the appointment process for agency commissioners or allowing for the potential of city council members to control a majority of the agency board. These types of governance changes would undermine the precedential

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<sup>2</sup> If the debt issuing powers of urban renewal agencies are thrown into limbo, it is unlikely that agencies will undertake additional projects until a new ruling from the Idaho Supreme Court is obtained.

value of the Supreme Court's holdings and create the potential of another Supreme Court challenge to affirm the agency's authority to issue long term debt.

Other changes could have a similar effect. Any of them would need to be analyzed for the principle of whether the degree of separation is called into question. For these reasons, it is imperative that urban renewal agencies remain separate and distinct from the municipality.

**2. Changes to the Urban Renewal Law may result in urban renewal agencies losing their ability to issue tax-exempt bonds.**

In order to issue tax-exempt bonds, the issuer of the bonds must either be a "political subdivision" of a state or be an issuer which is issuing "on behalf of" a "political subdivision" of a state. To qualify as a "political subdivision," the entity must possess by statute one of the following three powers: (a) general taxing power, (b) power of eminent domain, or (c) police powers. Cities, towns and counties, as well as certain other political entities, are generally "political subdivisions" because they possess all three powers. With respect to an Idaho urban renewal agency, the agency itself does not possess general taxing power. The fact that the urban renewal agency receives tax revenues does not mean that it possesses taxing power; the taxing power is exercised by the taxing districts within the agency's jurisdiction. Also, while "police powers" is a somewhat amorphous term under the tax laws, the Urban Renewal Law does not give urban renewal agencies any powers that could be characterized as "police powers." Accordingly, an urban renewal agency must possess the power of eminent domain to be classified as a "political subdivision" for the purpose of issuing tax-exempt bonds. If urban renewal agencies' power of eminent domain is eliminated, then urban renewal agencies, both existing and new, will not be a "political subdivision" for the purpose of issuing tax-exempt bonds. The fact that the local governing body can exercise this power on behalf of the agency does not change this conclusion. It is the issuer of the bonds that must qualify as a political subdivision.

As indicated above, bonds issued by an Idaho urban renewal agency (which does not have eminent domain power) could still be tax-exempt if the urban renewal agency is issuing bonds "on behalf of a "political subdivision." The sponsoring municipality of each urban renewal agency is clearly a "political subdivision." Thus, if the urban renewal agency's relationship to the sponsoring municipality meets the requirements for an "on behalf of issuer for federal income tax purposes, the bonds issued by the urban renewal agency can be tax-exempt. The Internal Revenue Service has issued revenue rulings delineating the requirements which must be met to satisfy the "on behalf of" status. While Idaho urban renewal agencies meet 5 of the 6 requirements, they do not appear to meet the requirement that upon dissolution title to all bond financed property must revert to the sponsoring municipality as there is nothing to this effect in Chapter 20 or Chapter 29 of Title 50, Idaho Code, as amended. Therefore, if urban renewal agencies' power of eminent domain is eliminated, urban renewal agencies will not be a

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“political subdivision” and, in all likelihood, will not be an “on behalf of issuer” for federal income tax purposes. Accordingly, they will be unable to issue tax-exempt bonds.

**C. Conclusion**

Legislative changes to the Urban Renewal Law could significantly impact the established ability of urban renewal agencies across the State to access capital markets. For this reason, any such changes ought to be approached with appropriate consideration for long-standing legal precedent, the expectations of bondholders and the ongoing effectiveness of urban renewal agencies.

Sincerely,

HAWLEY TROXELL ENNIS & HAWLEY LLP



Nicholas G. Miller

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cc: Honorable Senator Charles Winder  
Statehouse, Boise, Idaho