IMPROVING TAX INCREMENT FINANCING (TIF) FOR ECONOMIC DEVELOPMENT

By David Merriman

Tax increment financing (TIF), a popular economic development tool across the United States, often falls short of its promise to revitalize struggling neighborhoods.

TIF earmarks property tax revenue increases (or "increments") in a designated area that are expected to result from new development and real estate appreciation generated by the TIF. Enabled by the state, city governments typically create new TIF districts and specify their goals, permitted expenditures, and terms of operation.

This practice allows cities to divert revenues of overlying governments—such as counties or school districts—to fund economic development, rationalizing that diverted revenues would not exist "but for" the economic activity TIF funds. Therefore, in theory, there is no loss to overlying governments, and developers receive no subsidy unless they spur development. Indeed, TIF's power lies in its potential to bring together private- and public-sector actors to stimulate growth.

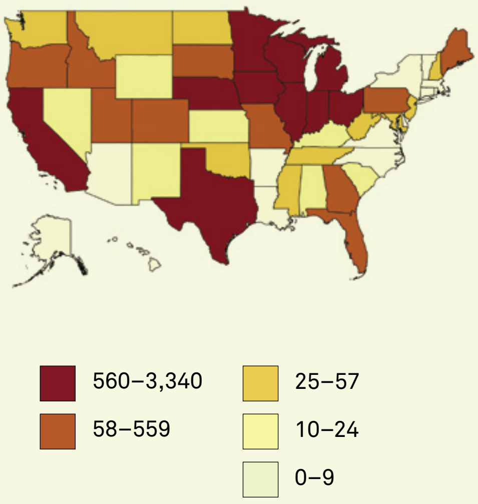
Communities should use TIF cautiously to avoid unintended consequences.

In practice, however, TIF remains highly vulnerable to exploitation, misuse, and uneven application. Additionally, many recent studies show that TIF does little to generate economic growth, and any development that emerges is not necessarily attributable to TIF. Instead, TIF can divert needed property tax revenues from overlying governments, obscure municipal financial records, and facilitate unproductive fiscal competition between neighboring jurisdictions.

Empirical studies of TIF-related impacts—such as on school finance, land uses, and budgeting—suggest communities should use TIF cautiously to avoid unintended consequences. Nevertheless, promoting economic activity is a key function of local government and requires cooperation between the government and the private sector. Used carefully, TIF can generate those desirable and positive impacts—but such results are by no means guaranteed.

Figure 1

Estimated Number of TIF Districts by State



TIF has been used very unevenly across states. It is reasonable to speculate that states' responses to their neighbors' use of TIF have contributed to this pattern of unevenness, though the reasons for the uneven use of TIF have not been rigorously studied.

Arizona is the only U.S. state that has not enabled some form of TIF, although many states use different terms for the practice, such as "Tax Allocation Districts" in Georgia.

Source: Merriman 2018. Categories for MT, NH, SC, and TN are best available estimates

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TIF in Practice

As a local program enabled at the state level, TIF varies widely by state and even locality. To date, there has been no published academic work explaining why some states use TIF more than others.

States also vary in allowed uses of TIF revenues: All permit the servicing of bonds, but in some states TIF can subsidize other development, like selling or renting real estate below fair-market value to promote construction in the TIF district. Roughly two-thirds of the states further allow some use of TIF funds for limited activities outside of the physical district's boundaries.

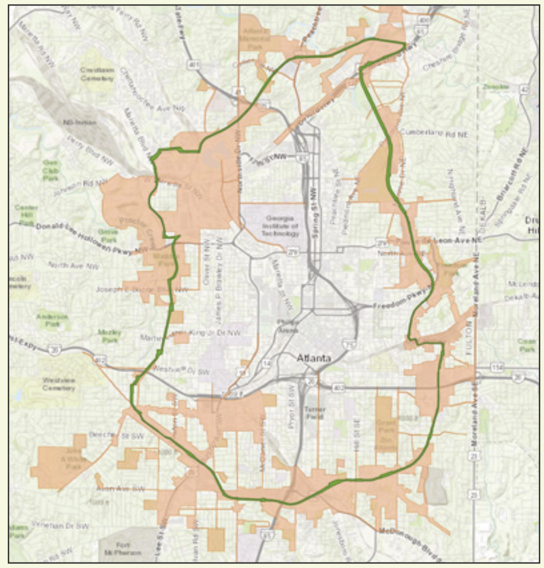
Transparency is an ongoing challenge, and state and city monitoring of TIF use is very uneven. Once a municipality establishes a TIF district and begins to receive revenues and make expenditures, it can account for them separately—and sometimes obscurely—compared to other governmental funds. Some states, such as Illinois, require annual reports on each TIF district and provide state-level data about TIF use. Others, such as Maine, simply verify that proposals for local TIF districts meet statutory requirements but do not then track or monitor active districts.

That lack of transparency makes it difficult to rigorously evaluate TIF. Though there is evidence that TIF works in certain cases, existing research suggests that most TIF uses do not accomplish the goal of promoting economic development. TIF may also bring a variety of unintended effects, such as diminished or reallocated school revenues and increased budget volatility, especially during unstable economic cycles.

TIF often fails in both obvious and subtle ways. For instance, TIF can fail if planned developments simply do not materialize, and even a successful TIF project may also impose negative externalities—like traffic, crime, or noise pollution—that lower the value of nearby houses or businesses. State statutes and regulations generally require specific criteria that must be documented prior to the establishment of a TIF district, but these criteria are generally vague enough that almost any project with strong political support can satisfy the requirements. In particular, inconsistencies persist around two key questions: (1) What constitutes "blight" in need of redevelopment? and (2) Would economic growth have occurred without ("but for") the TIF?

Figure 2

Map of Atlanta BeltLine Tax Allocation District



Atlanta BeltLine Corridor

Atlanta BeltLine Tax Allocation District (TAD)

Source: Atlanta BeltLine, Inc. (2018).

TIF Is Not Additional Land Value Capture

Land value capture is a policy approach that enables communities to recover and reinvest land value increases that result from public investment and other government actions. Since well-functioning property tax systems base obligations on the market value of real estate, the property tax can be an important form of land value capture.[1]

Because TIF diverts revenue from real estate appreciation that may in part be due to public investment, some observers may erroneously believe that TIF is a land value capture tool separate from the property tax. In fact, it is more properly a device that "transfers" value to, rather than "captures" value from, the private sector.

Case Studies

CHICAGO, ILLINOIS

The Windy City employs TIF more than any other big city in the United States, with 149 districts; in 2015 alone, Chicago TIFs collected about $461 million in property tax revenues.[2] The use of those revenues remains controversial, however; though much information has been made public, transparency remains inconsistent. Because of how TIF spending functions, districts can persist for decades without being subject to ordinary democratic controls. Critics called one former mayor's use of TIF dollars a "shadow budget," which could be allocated with minimal oversight from the elected city council or the general public. A task force convened in 2011 generated a number of transparency measures, including an open data portal, but many of its recommendations have yet to be acted upon—and Chicago's evolving TIF use remains controversial.

STATE OF CALIFORNIA

California was the first state to make extensive use of tax increment financing—and recently became the first state to reverse course and drastically reduce its use of TIF. In 2008, California had over 400 TIF districts with more than $10 billion in annual revenue, but enabling legislation prevented school districts and other overlying governments from opting out, which resulted in ongoing scrambles (often at the state level) to fill resulting budgetary gaps. Eventually, 2010 state legislation essentially ended local governments' ability to create TIF districts; subsequent legislation permitted TIF, but on a much more limited basis. Current state requirements for TIF use include affordable housing mandates, the requirement that overlying governments opt in, and extensive public input and approval.

ST. LOUIS, MISSOURI

Facing severe fiscal, economic, and competitive challenges, St. Louis has approximately 100 TIF projects, mostly retail-oriented development, which had by early 2016 diverted $2 billion of public tax dollars to developers. With so many TIF districts, mixed results are unsurprising. Some, like the Cortex Redevelopment Plan, one of the largest TIF-supported undertakings in the area, generated even more outside funding and jobs than expected.[3] By contrast, 20 projects were terminated before completion, and another 16 ultimately failed to get approval; studies suggest this was because the retail-oriented projects would displace rather than create jobs. Others may have failed by depending too much on TIF financing, rather than on community partnerships that would help ensure long-term success.

ATLANTA BELTLINE TAX ALLOCATION DISTRICT ATLANTA, GEORGIA

Launched in 2006, the Atlanta BeltLine Tax Allocation District (TAD, Georgia's name for a TIF district) was an ambitious plan to fund a new transit system linking multiple Atlanta neighborhoods along old rail corridors surrounding the city (figure 2). Projected for completion by 2030 at a total cost of up to $4.8 billion, the BeltLine has thus far generated mixed results, delivering trail and transit real estate on time but lagging on transit, streetscape, and affordable housing construction. Overall, however, the project maintains both popular and judicial support—and it has continued to evolve in light of community concerns about delays, gentrification, racial inequities, and government spending.

JEFFERSON COUNTY, MONTANA

A small but relatively wealthy county in southwestern Montana, Jefferson County depends economically on agriculture, forestry, and mining. When the Golden Sunlight Mine, a longstanding community presence and major employer, projected that it would shut down, the county proposed developing a TIF-funded business park to cushion the economic transition away from mining and attract high-tech companies and jobs. By early 2017, three years after the groundbreaking, the new Sunlight Business Park had three newly built units, including office and warehouse space, and a small number of new jobs. Development remains slow, but thanks to the mine operator's commitment to ensuring the county's economic stability, including its partnership in the TIF district, the project remains poised for success.

Recommendations

TRACK AND MONITOR TIF USE

Consistent monitoring would help states better evaluate the use of TIF and support state legislators in understanding whether and how TIF actually works. Virtually all states monitor property tax assessment processes and could easily track TIF districts as well. Wisconsin, which already requires regular reporting on TIF, provides a particularly strong example, as it requires detailed delineation of expenditures and "porting," the movement of TIF funds from one district to another.[4]

ALLOW OPT-OUTS

States should allow counties, school districts, and other overlying local governments to opt out of TIF, which can deprive them of significant and needed revenue. Recent legislation in Chicago may provide a model.[5]

REVIEW "BUT FOR" EFFICACY

States should require conclusive evidence that development would not occur "but for" the TIF. An effective "but for" requirement can prevent abuse of TIF, especially when other policies might be more appropriate, so state legislators should review and revise their states' rules to ensure they place effective, realistic limits on local governments' use of this tool. California's recent revisions of TIF rules might provide useful guidance.[6]

ENABLE MORE TRANSPARENCY

Local governments should provide extensive, easily accessible information about TIF use, revenues, and expenditures, and they should document progress toward clearly articulated goals. TIF spending is fundamentally different from other government spending; districts are often not subject to ordinary democratic controls, thus meriting much more reporting and transparency. Furthermore, municipal legislators should be able to make evidence-based adjustments to TIF districts, such as limiting durations or dissolving those that do not meet the jurisdiction's objectives.

CONDUCT COMPARATIVE RESEARCH

Researchers should study, document, and explain the mixed outcomes of TIF and expand knowledge about the types of TIF expenditures that best promote economic development. To date, academic studies of TIF document mixed outcomes but do not clearly identify factors that explain variations in outcomes of TIF use in various geographic areas.

Below: Morgan Station in Chicago, funded almost fully through TIF, accelerated the redevelopment of the area. Photo: Steven Vance/ Flickr CC BY-NC-SA 2.0.

This policy brief is based on the Policy Focus Report by David Merriman, *Improving Tax Increment Financing (TIF) for Economic Development* (Cambridge, MA: Lincoln Institute of Land Policy, 2018).

1 See www.lincolninst.edu/key-issues/value-capture-property-tax.

2 Office of the Cook County Clerk. 2016. "TIF District Summary: City of Chicago Only 2014 to 2015 Revenue Comparison." https://www.cookcountyclerk.com/sites/default/files/pdfs/ChicagoTIFTotalsSummary2015.pdf.

3 Barker, Jacob, and Tim Bryant. 2016. "New $170 Million Cortex Development to Add Hotel, Apartments, Parking Garage." *St. Louis Post-Dispatch*, October 16.

4 Wisconsin Department of Revenue. 2017b. Tax Incremental Financing (TIF). Information. https://www.revenue.wi.gov/Pages/SLF/tif.aspx.

5 Vance, Steven. 2016. "Transit TIF Districts Pass State House and Senate, Would Fund CTA Projects." Streets Blog Chicago. June 30. http://chi.streetsblog.org/2016/06/30/transit-tif-districts-pass-state-house-and-senate-would-fund-major-cta-projects.

6 Torres, Paco. 2016. "AB 2492 (Alejo): Cleanup for CRIA Implementation (AB 2)." www.caled.org/wp-content/uploads/2014/12/AB-2492-CRIA-Cleanup-Fact-Sheet-Final.pdf.

LINCOLN INSTITUTE OF LAND POLICY

113 Brattle Street, Cambridge, MA 02138-3400, USA | help@lincolninst.edu **lincolninst.edu** January 2019

P (617) 661-3016 or (800) 526-3873 **F** (617) 661-7235 or (800) 526-3944