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The ABCs of TIF

A Basic Examination of Tax Increment Financing (“TIF”) from the Perspective of Both Lawyers and Underwriters

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In this outline, we provide details concerning Ohio TIF and comparisons to other States. Attached to this outline is a table summarizing important aspects of TIF law (or comparable laws) in thirteen states – California, Colorado, Georgia, Florida, Illinois, Indiana, Michigan, Missouri, New Jersey, New York, Ohio, Pennsylvania and Texas. We hope this method of analysis will provide the attendee with enough details concerning one state to spot issues and ideas on a micro level and enough generalities concerning other states to understand different ways of addressing TIF issues on a macro level.

I. TIF Overview

A. What is TIF?

Ohio

1. TIF is a tool that can be used by Ohio political subdivisions (municipal corporations, counties and townships) and private companies to fund infrastructure and site improvements.
2. One fundamental part of a TIF is the TIF real property tax exemption. The entire value of the real property that is subject to a TIF cannot be exempted. TIF exemptions are limited to the increase in the assessed

value of real property. This increase in assessed value is defined as an “improvement” under the TIF statutes.

3. In general, taxpayers make service payments in lieu of tax (“service payments”) at the same time, and in the same amount and the same manner as real property taxes. These service payments are then used to service debt for infrastructure or site improvements or to reimburse a developer or political subdivision for the construction of infrastructure or site improvements. There are certain types of TIFs that can serve as true tax exemptions. These TIFs will be discussed in greater detail later in this outline.

B. What TIF Is Not

Ohio

1. TIF is not a loan or immediate cash infusion into a project. TIF can be used to service project debt or to reimburse a developer or political subdivision for the construction of infrastructure or site improvements.

C. Who can use TIFs?

Ohio

1. Ohio cities, villages, townships and counties have the statutory authority to establish TIFs by passing an ordinance or resolution. The specific process for creating a TIF will be discussed later in this outline.
2. Although a TIF must be established by a political subdivision, private companies can also benefit greatly from TIFs, which can provide a source of funding to support infrastructure and site improvements that are needed in connection with a construction or expansion project. Private companies must work closely with political subdivision officials to benefit from a TIF.

D. Why use TIFs?

Ohio

1. TIFs can provide a consistent revenue stream for infrastructure and site improvements costs for up to 30 years. In some instances, cooperation from the affected local school district is necessary (as discussed in greater detail later in this outline).
2. The property owners are not negatively affected by the TIF. The property owners that are subject to a TIF make service payments in the same

amount and at the same time and in the same manner as the real property taxes that would be due on the increase in the assessed value of the property had that increase not been exempted pursuant to the TIF. It is not surprising, therefore, that it is not necessary to obtain consent from property owners to establish a TIF.

3. TIFs are valuable. Although each situation is different, most TIFs can generate at least \$1 million in revenues for each \$10 million in “improvement.”

II. Types of TIFs

Ohio

- A. TIFs can generally be categorized by the types of improvements for which TIF funding is being sought. Some TIFs can only be used to fund public infrastructure improvements, while others can be used creatively to provide assistance with project costs, including private improvements, or even to provide funding for public services.
- B. Public Infrastructure Improvements Only (and housing projects, if applicable)
 1. Some TIFs can only be used to fund public infrastructure improvements, or, in some situations, housing projects.
 - a. “Public infrastructure improvements” are specifically defined and generally include work typically deemed public improvements. Interestingly, the definition also includes “land acquisition, including acquisition in aid of industry, commerce, distribution, or research” and “demolition on private property when determined to be necessary for economic development purposes.”
 - b. These TIFs can be further categorized into TIFs that can be used to exempt nonresidential improvements only and those that can also be used to exempt residential improvements.
 2. Traditional TIFs (Exemption of Nonresidential Improvements Only)
 - a. A political subdivision can pass an ordinance or resolution declaring the “improvement” to certain parcels to be a public purpose, and exempting the improvement to those parcels from real property tax for a particular period of time. These TIFs are referred to in this outline as “traditional TIFs.”
 - b. Traditional TIFs can generally be used to exempt only nonresidential improvements. However, if the affected parcels are

located in a blighted area of an “impacted city”, traditional TIFs can be used by municipal corporations to exempt both residential and nonresidential improvements.

- c. Without approval from the affected city, local or exempted village school district, TIF exemptions can be for up to 75% and for a period of up to 10 years. However, with school district approval or, in the case of municipal corporations, with either school district approval or a school district “hold harmless” provision (see below), TIF exemptions can be for up to 100% and for a period of up to 30 years. As a result, it is generally best to cooperate with the affected school district to maximize potential TIF benefits.
 - i. All political subdivisions have the power to enter into compensation agreements with affected school districts whereby the political subdivision agrees to reimburse the school district for some portion of its lost revenue as a result of the TIF. In connection with such agreements, school districts typically agree to approve a 100% exemption for up to 30 years. Private companies can also execute compensation agreements with school districts and other political subdivisions.
 - ii. In addition, municipal corporations can create TIFs that hold the affected school district harmless by paying to the school district the amount of real property taxes that the school district otherwise would have received had the TIF not been created. In such cases, the TIF exemption can be 100% for up to 30 years. This arrangement is generally made in the TIF legislation, and it is not necessary for the political subdivision to enter into a separate compensation agreement with the school district.
 - d. All affected school districts and joint vocational school districts must receive formal notice of the proposed TIF.
 - e. The political subdivision can specify directly in the TIF legislation when the tax exemption will begin. Although each project is different, in general, it is best to have the TIF exemption begin in the first tax year in which an increase in the assessed value of the TIF’d property appears on the tax list and duplicate of real and public utility property.
3. Incentive District TIFs (Exemption of Both Commercial and Residential Improvements)

- a. A political subdivision may also pass an ordinance or resolution creating one or more incentive districts, and declaring the “improvement” to property within those incentive districts to be a public purpose and exempt from real property taxes for a specific period of time. These TIFs are referred to in this outline as “incentive district TIFs.”
- b. The exemption percentage and duration limits for traditional TIF also apply to incentive district TIFs. In addition, the same school district notice and approval requirements apply to incentive district TIFs.
- c. One of the major advantages to using incentive district TIFs is that residential improvements are exempted under an incentive district TIF. Another major advantage is that all “improvement” within the district – which area need not be limited to a project site – is captured, thereby increasing the potential TIF revenues.
- d. Another advantage to using incentive district TIFs is that these TIFs can be used to fund housing projects in addition to public infrastructure improvements, provided a project within the district will also include commercial/industrial improvements. In this way, incentive district TIFs can be used to fund some project costs, if the project involves the construction of residential improvements.
- e. Similar to traditional TIFs, the political subdivision can specify directly in the TIF legislation when the tax exemption will begin.
- f. In the past, there were significant advantages to using incentive district TIFs rather than traditional TIFs for most projects. However, recent legislative developments have made incentive district TIFs significantly less valuable.

C. Assistance with Project Costs and Other Costs

- 1. There are also certain TIFs that can be used to fund other project costs that would not be considered public infrastructure improvements (or housing projects, in the case of incentive district TIFs). These TIFs can only be established by municipal corporations.
- 2. Urban Redevelopment TIFs under R.C. Section 5709.41
 - a. An urban redevelopment TIF is a special type of TIF that is established by a municipal corporation to fund urban redevelopment.

- b. In an urban redevelopment TIF, a municipal corporation may legislatively declare the increase in assessed value of a parcel of property to be a public purpose and exempt from real property tax if:
 - i. The municipal corporation held title to the property prior to the legislation; and
 - ii. The property is leased or conveyed to another person either before or after adoption of the legislation.
- c. Urban redevelopment TIFs are similar to traditional TIFs established by municipalities in several respects.
 - i. The exemption limits are the same, with the maximum exemption limited to 100% and the exemption period limited to 30 years.
 - ii. The same school board notice and approval provisions apply to urban redevelopment TIFs.
- d. However, there are several significant differences between traditional and incentive district TIFs and urban redevelopment TIFs.
 - i. Most significantly, in an urban redevelopment TIF, the municipal corporation may choose not to require owners of affected property to make service payments. Thus, an urban redevelopment TIF can function as a true tax exemption.
 - ii. In addition, service payments collected pursuant to an urban redevelopment TIF can be used “for such purposes as are authorized in the resolution or ordinance establishing the fund.” This appears to give municipalities **wide latitude in determining how those service payments are used, including using the service payments to fund private site improvements (within the scope of constitutional constraints) and including using the service payments to fund costs of public services (e.g, safety services).**
- e. Used creatively, urban redevelopment TIFs can be used to fund project costs that would not be considered to be public infrastructure improvements. The use of an urban redevelopment

TIF to fund site improvements is described in a case study appearing later in this outline.

3. R.C. Chapter 725 Urban Renewal Debt Retirement TIFs

- a. A municipal corporation may enter into a Development Agreement with private developers in an “urban renewal area” whereby the developers agree to perform urban renewal projects to rehabilitate property in the area in accordance with an adopted Urban Renewal Plan. An “urban renewal area” is a blighted area or a slum area of a municipal corporation, as defined in the chapter.
- b. The Development Agreement must include a requirement that the developer make the required improvements and that the owners and future owners of the property make all required service payments and use the property in a manner that is consistent with the Urban Renewal Plan.
- c. Urban renewal debt retirement TIF exemptions can be for up to 75%, or up to 100% with school district approval, which is obtained in the same way that school district approval is obtained for traditional and incentive district TIFs. The exemption begins on the date of the execution of the Development Agreement, and may last for up to 30 years or more, depending upon the time needed to retire certain debt.
- d. Public expenditures under an urban renewal debt retirement TIF are funded by a single issuance or series of bonds, or by state loans. The general process of funding improvements using TIF is discussed in detail later in this outline.
- e. R.C. Chapter 725 allows TIF funds to be used to fund any “urban renewal project,” which is defined generally to allow for assistance with project costs. However, these project costs are funded by the bond or loan proceeds rather than directly by service payments because service payments must be used to pay debt service on the bonds or loans.

4. R.C. Chapter 1728 Community Urban Redevelopment Corporation (“CURC”) TIFs

- a. A CURC may be formed for the purpose of performing projects in blighted areas of municipal corporations in accordance with a written Community Development Plan. This type of TIF is similar in many ways to urban renewal debt retirement TIFs.

- b. CURC TIF exemptions are generally only available in blighted areas of “impacted cities.”¹ If the municipal corporation does not meet the definition of an “impacted city,” the project must involve the sale or lease of all or a portion of the TIF’d property by the municipal corporation to the CURC.
- c. A written Community Development Plan must be adopted by the municipal corporation to establish this type of TIF. In addition, the municipal corporation must enter into a Financial Agreement with the CURC requiring the completion of the project by the CURC. The CURC generally finances improvements under the terms of the Financial Agreement.
- d. CURC TIF exemptions can be for up to 75%, or up to 100% with school district approval, which is obtained in the same way that school district approval is obtained for traditional and incentive district TIFs. The exemption begins on the date of the execution of the Financial Agreement, and may last for up to 20 years.
- e. The amount of service payments made pursuant to a CURC TIF is very flexible.
 - i. At a minimum, service payments and tax payments (for non-exempt portions) must equal the total taxes assessed on all real property in the area affected by the project in the calendar year immediately preceding the acquisition of the property by the city or the CURC (i.e., taxes prior to redevelopment).
 - ii. If the Financial Agreement is made with an impacted city, then the maximum amount of the service payments is the real estate taxes that would have been charged had the property not been exempted (along with the pre-redevelopment minimum).
 - iii. If the city has not been designated an impacted city, the service payments cannot be less than 7½% of the annual gross revenues from the Project (or 2% of the total project cost when revenues cannot be estimated). This amount is still subject to the overall pre-redevelopment minimum.
- f. The use of the service payments paid pursuant to a CURC TIF is also very flexible, and like urban redevelopment TIFs and unlike

¹ “Impacted city” is defined at R.C. Section 1728.01(C).

urban renewal debt retirement TIFs, CURC TIFs can provide property owners with a true exemption (in part) because the statutes allow for flexible use of the TIF service payments in an amount less than would have been paid as taxes.

III. Recent Developments

Ohio

- A. Since June 2004, the Ohio General Assembly has enacted three significant sets of amendments to Ohio TIF laws and to school funding laws as school funding laws apply to TIF'd property. For the most part, the amendments have had a prospective effect only, and there have been “grandfathering” provisions that have allowed practitioners to get TIF deals done under previously existing TIF laws where those previously existing TIF laws were more favorable.
- B. Key Amendments to Incentive District TIFs
1. Exemption Limits for Certain Political Subdivisions (the 25% test) Added – Any political subdivision with a population greater than 25,000 cannot create an incentive district if the sum of the taxable value of real property in the proposed district for the preceding tax year and the taxable value of all real property in the municipal corporation that would have been taxable in the preceding year were it not for the fact that the property was in an existing incentive district and therefore exempt from taxation exceeds 25% of the taxable value of real property in the municipal corporation for the preceding tax year.
 2. Project Requirement Added – Incentive district TIF laws did not historically require a specific project to be located within the incentive district. Now, however, incentive district legislation must specify a project or projects within the incentive district that place additional demand on the public infrastructure improvements to be made under the TIF.
 3. New Notice and Approval Requirement Added – Other political subdivisions – not just the school district – now have notice and approval rights in certain circumstances. If the proposed exemption exceeds 75% or 10 years, the legislative authority of the political subdivision creating the TIF must send a notice to a specified political subdivision that encompasses the incentive district at least 45 business days prior to the passage of the TIF legislation.² If a political subdivision that is entitled to

² R.C. Sections 5709.40 and 5709.73 require cities and townships establishing incentive districts to send the notice to the board of county commissioners of any county that encompasses the incentive district. R.C. Section 5709.78

receive notice objects to the exemption within 30 days of receiving the notice, the legislative authority may do either of the following: (1) negotiate a compensation agreement with the county or township that encompasses the incentive district (not to exceed the property taxes forgone pursuant to the TIF); or (2) proceed with the incentive district as planned and in the TIF legislation provide to that county or township compensation in the eleventh and subsequent years of the exemption period equal in value to not more than 50% of the taxes that would be payable to the political subdivision or, if the political subdivision's objection includes an objection to an exemption percentage in excess of 75%, compensation equal in value to not more than 50% of the taxes that would be payable to the political subdivision, on the portion of the improvement in excess of 75%, were that portion to be subject to taxation.

4. Levy Exceptions Added – The law now requires a portion of collected service payments to be distributed to certain taxing authorities to the extent that those service payments relate to certain tax levies, resulting in less service payment revenue to the political subdivision creating the TIF. This exception applies to specifically-designated levies, which are generally related to health, human services and public welfare, that are approved on or after January 1, 2006. This exception also applies to any renewal levy with an increase and any replacement levy passed on or after January 1, 2006, to the extent that the renewal or replacement levy exceeds the effective tax rate of the levy renewed or replaced.

D. Key Amendments to Traditional TIFs

1. Direct Relationship between TIF'd Property and Infrastructure Relaxed -- Two of the most burdensome and unclear requirements for traditional TIFs were effectively eliminated by H.B. 66. First, the requirement that the percentage exempted from tax not exceed the “estimated percentage of the incremental demand placed on the public infrastructure improvements that is directly attributable to the exempted improvement” was removed. Second, the requirement that the public infrastructure improvements “directly benefit” the TIF'd parcels was modified by removing the requirement that a specific project place “direct, additional demand” on the public infrastructure.
2. Flexibility Added Concerning Commencement of TIF Exemptions – From 2001 through mid-2005, TIF exemptions have commenced with the tax year in which an improvement first appears on the tax list and duplicate of real and public utility property and that begins after the effective date of the ordinance or resolution approving the exemption. As previously

requires counties establishing incentive districts to send the notice to the board of township trustees of any township that encompasses the incentive district.

discussed in this outline, TIF law now allows the commencement date of the TIF exemption to be specified in the ordinance or resolution.

E. Critical TIF-Related Changes to School Funding Law

1. School funding law in Ohio is very complex. In general, all public and joint vocational school districts in Ohio receive annual State assistance, which is determined by calculating the total amount of money that a school district needs to educate all of its students, and subtracting from that total the amount of property tax revenue that the State estimates can be raised by the school district.
2. Prior to recent amendments, political subdivisions and school districts often took advantage of an opportunity to compensate school districts for TIF (and other) exemptions without having those compensation payments affect the amount of State funding that the school district received. Prior to the law changes:
 - a. In general, the addition of taxable property within the school district would result in the school district receiving less in State funding because the State assumed that the school district could raise property tax revenue on that new property.
 - b. However, if the property was exempt, it would not result in the school district receiving less in State funding. As a result, many political subdivisions agreed to compensate school districts by making side payments pursuant to compensation agreements.
 - c. This arrangement was very advantageous for school districts. They would receive compensation payments to make up for “lost” taxes. At the same time, the school districts avoided being penalized because the property was exempt, and did not count against the districts for State funding purposes.
3. Recent amendments attempt to limit this type of opportunity for school districts. Beginning in 2007, school districts will generally receive less in State funding if the school districts receive payments pursuant to compensation agreements that were executed in connection with exemptions granted on or after January 1, 2006 under incentive district TIFs, enterprise zone (“EZ”) exemptions, community reinvestment area (“CRA”) exemptions, urban renewal debt retirement TIFs, CURC TIFs, qualified railroad company exemptions and environmental remediation exemptions. Both political subdivisions and private companies that wish to use TIF should be aware of this change in the law because of the importance of cooperating with local and joint vocational school districts in passing TIF legislation.

IV. Case Study

Ohio

A. Assumptions

1. All TIFs in this case study were established after January 1, 2006.
2. The TIFs in this case study are all municipal corporation TIFs.

B. Problem – A client approaches about using TIF to help fund project costs associated with a major downtown expansion project. The client would like to use the TIF funds to help pay for a new office building. The client would also like to improve the highways and other infrastructure around its downtown campus to make it better accessible to its customers and employees. The neighborhood around its campus includes a significant proportion of residential improvement. The expected cost of these improvements is as follows:

1. Remodeling of existing building – Approximately \$4 million.
2. Construction of a new attached building – Approximately \$40 million.

C. Solution – The client's needs can be addressed using both a 30 year, 100% municipal incentive district (R.C. Section 5709.40) TIF and a 30 year, 100% urban redevelopment (R.C. Section 5709.41) TIF coupled with a 10 year, 75% EZ exemption. These TIFs could be structured as follows:

1. R.C. Section 5709.40 Incentive District TIF
 - a. This incentive district would encompass the parcels immediately surrounding the client's property (but none of the client's property is included) and the TIF proceeds would be used to make necessary infrastructure improvements.
 - b. This TIF would be structured as a school district hold-harmless municipal TIF, meaning that the TIF legislation would specify that the affected school district would be paid the amount it would otherwise have received had the property been fully taxable. This structure allows the school district to be compensated without triggering any adverse school funding consequences under the H.B. 66 changes because there is no agreement with the school district.
 - c. Assuming that the true value of the TIF'd property increases by \$20 million because of small projects and appreciation of property,

and a tax rate of 6%, this TIF could be worth over \$4 million over 30 years on a non-net present value basis (after making payments to the school district estimated as approximately 65% of the total service payments and payments to the county estimated as approximately 2-3% of the total service payments). These TIF proceeds could be used to improve the infrastructure around the client's office building.

- d. It should be noted that because this TIF is an incentive district TIF, it would be necessary for a "project" to be constructed within the incentive district, and the municipal corporation would need to adhere to the new notice and approval requirements imposed by recent amendments. See discussion of these new requirements earlier in this outline.

2. R.C. Section 5709.41 TIF and EZ Exemption

- a. This urban redevelopment TIF would include the parcels comprising the client's existing downtown campus.
- b. The TIF proceeds would be used to help fund the cost of constructing the client's new office building. This would be accomplished by including language in the TIF legislation that would allow the client (or a developer hired by the client) to be reimbursed from the TIF service payments for certain costs associated with the construction of the office building that were paid by the client (or the developer). Alternatively, the city could issue bonds, with debt service to be funded by TIF service payments, and provide bonds proceeds to the client by grant or loan.
- c. This TIF could also be structured as a school district hold-harmless TIF.
- d. This TIF would be coupled with a 10 year, 75% EZ exemption that would take precedence over the TIF for a period of 10 years. The net effect of this arrangement is that the TIF exemption would only effectively be 25% (without considering the payments to the school district) for 10 years, but would then be 100% for the remaining 20 years.
- e. Assuming that the assessed value of the TIF'd property increases by \$40 million and a 6% tax rate, this TIF could be worth over \$6 million over 30 years on a non-net present value basis (after making payments to the school district estimated as approximately 65% of the total service payments). In addition, the client would

also be receiving a 75% EZ exemption for 10 years, which could be worth an additional \$6 million on a non-net present value basis.

3. Other Considerations – Although not directly addressed in this case study, if a significant number of new jobs are created as a result of this expansion project, the municipal corporation could be required by statute to share income tax revenue associated with these new employees with the affected local school district, unless that requirement is waived by a school district agreement. This revenue sharing process is discussed in greater detail later in this outline.

V. Practical TIF Structuring Issues

A. Constitutional Issues

Ohio

1. Because TIF funds are considered to be public funds, Ohio’s Constitution places several limitations on their use. Although several of these constitutional issues are described below, it is not possible to fully explain these issues in this outline. These issues require specific attention when structuring any TIF.
2. Article VIII, Section 6 of the Ohio Constitution (“Section 6”) generally prohibits a political subdivision from raising money for, or loaning its credit to or in aid of, private enterprises.
 - a. The purpose behind this provision has been described as “to prohibit private interests from tapping into public funds at the taxpayers’ expense.”
 - b. Courts have construed Section 6 to prohibit a city from funding the construction of public infrastructure improvements to support a housing development through the issuance of city bonds and notes. However, when the political subdivision is being fully (or nearly fully) reimbursed by a developer, courts have held that Section 6 was not violated.
3. Article VIII, Section 13 of the Ohio Constitution (“Section 13”) provides a significant exception to Section 6.
 - a. Section 13 allows a political subdivision to raise money for or loan its credit to private enterprises, provided that such financial involvement is (among other permitted purposes not relevant to the project) to create or preserve jobs and employment opportunities in relation to industry, commerce, distribution and research. The

Ohio Supreme Court has interpreted the meaning of “commerce” and “industry” in Section 13 broadly.

- b. Section 13 precludes the pledge of tax monies as security for the bonds. As a result, a political subdivision generally may not raise money for or lend its credit to private enterprises by issuing bonds that are secured by a pledge of the full faith and credit of a political subdivision (general obligation bonds) or by a specific tax levy. Revenue bonds, however, may be issued.
- c. Similar authority for support of housing projects is provided in Article VIII, Section 16.

B. Issuance of Debt and Associated Issues

Ohio

1. Issuance of Bonds or Notes

- a. Political subdivisions will often issue bonds or notes to fund infrastructure or site improvements that are made pursuant to a TIF or land acquisition needed for a project. In these situations, the proceeds of those bonds or notes are used to make the public infrastructure or site improvements or land acquisition, and the TIF service payments are used to pay the debt service on the bonds or notes.
- b. **General Obligation vs. Revenue Bonds**
 - i. General obligation bonds are supported by the full faith and credit of the political subdivision. When a political subdivision issues general obligation bonds, it effectively pledges its credit, and the bonds must be fully repaid, even if other funds must be used or taxes must be levied to do so. Generally, the payment of any general obligation bonds has priority over the payment of operating expenses of the political subdivision or any outstanding revenue bonds of the political subdivision. As discussed above, Section 13 restricts the issuance of general obligation bonds to raise money for private development.
 - ii. Revenue bonds are supported by specific streams of revenue rather than by the political subdivision’s full faith and credit. Because the stream of revenue can be uncertain, revenue bonds are generally riskier and therefore

carry higher interest rates than general obligation bonds. Revenue bonds are often used for TIF projects.

2. Credit Enhancements

- a. Because many of the bonds or notes that are issued to support TIF projects – if not general obligation bonds – are relatively risky in nature, investors will typically require some sort of credit enhancement to remove some of the risk from their investment. Although credit enhancements increase the cost of the financing to the property owner; they often lower the interest cost of the financing. Some of the most common credit enhancements in connection with TIFs are discussed below.
- b. Letters of Credit – in general, a letter of credit is an agreement between a letter of credit purchaser (e.g., a developer or private company) and a financial institution whereby the financial institution agrees to make the debt service payments in the event that the primary revenue stream (e.g., TIF service payments) is not sufficient and/or certain other events of default by the letter of credit purchaser occur. This arrangement protects the investor by providing the investor with a more secure, secondary source for debt service payments.
- c. Minimum Service Payments – property owners and/or developers often enter into agreements (usually guaranty agreements) whereby the property owners/developers agree to make a minimum amount of service payments regardless of the actual amount of taxes that are exempted as a result of the TIF. This arrangement ensures investors that a minimum amount of service payments will be paid to support debt service on the bonds or notes.
- d. Mortgages and Pledge Agreements – investors can request a mortgage on the TIF'd property (or other property) to secure their investment in bonds or notes. Investors can also request that the property owner/developer pledge other assets to secure their investment in bonds or notes.
- e. Special Assessments – property owners may agree to pay special assessments to the extent necessary to support debt service above and beyond the amount of the service payments that are paid into the TIF. This arrangement protects investors by ensuring that there will be sufficient money in the TIF fund to pay the debt service on the bonds or notes.

- f. Bond Insurance – the property owner may determine to purchase bond insurance from a qualified insurer. Under such an arrangement, the bond insurer agrees to pay debt service upon a payment default by the property owner. The capital markets views this type of credit enhancement as the most secure. However, it is usually the most expensive form of credit enhancement.

C. Developer Financing

Ohio

In lieu of the political subdivision issuing bonds or notes to fund TIF projects, a developer may agree to construct the public infrastructure or site improvements and later be reimbursed from the TIF fund. (This is probably not feasible under a Chapter 725 TIF.)

VI. Potential Pitfalls

Ohio

A. Exemption Priority Rules

- 1. In general, the priority of a TIF exemption depends on which party files the TIF exemption application (DTE Form 24).
 - a. If DTE Form 24 is filed by the property owner or the political subdivision with the owner's consent, the TIF exemption takes precedence over any later granted exemption (i.e., CRA exemptions, EZ exemptions) unless the political subdivision consents in writing to the later exemption.
 - b. If DTE Form 24 is filed by the political subdivision without the property owner's consent, the TIF exemption is automatically subordinated to an exemption granted under any other section of the Ohio Revised Code.
- 2. Political subdivisions and private companies should be aware of these general priority rules when establishing and using TIF. There are situations where it may be advantageous to subordinate the TIF exemption to other exemptions, such as ones in which a property owner wants the benefit of an EZ or CRA exemption. In other cases, however, it is most advantageous for the property owner to file DTE Form 24 to maximize the potential benefit of a TIF.

B. Marketability of TIF'd Property

1. As noted above, investors often require some form of credit enhancement prior to purchasing bonds or notes that will be used to finance public infrastructure or site improvements. These credit enhancements may be structured as an encumbrance on the property, which may decrease the value of the property to some prospective purchasers.
2. However, the benefits of TIF generally outweigh the burdens that these credit enhancements place on the TIF'd property. The value of the service payments over the life of a TIF can usually overcome any devaluation resulting from these credit enhancements.

C. Income Tax Revenue Sharing

1. As noted above, one potential pitfall for municipal corporations in creating TIF is the municipal income tax revenue sharing requirement in R.C. Section 5709.82.
2. If a TIF project will generate annual payroll from “new employees” of \$1,000,000 or more, the municipal corporation is required to negotiate to share a portion of the income tax revenue from these new employees with the affected city, local or exempted village school district. Municipal income tax sharing is not required if the municipal corporation has agreed in the TIF legislation to hold the school district harmless as to real property tax receipts from the project.
3. For applicable projects, if the school district and the municipal corporation fail to negotiate a mutually acceptable compensation agreement within six months of the passage of the TIF legislation, the municipal corporation must annually pay the school district an amount equal to 50% of the difference between (i) the amount of taxes levied and collected by the municipal corporation on the incomes of “new employees” and (ii) the amount of any “infrastructure costs” incurred by the municipal corporation in that calendar year, capped at the amount that the school district would have received had the project property not been exempt. For purposes of this computation, the amount of infrastructure costs cannot exceed 35% of the amount of those taxes unless the school board approves an amount in excess of that percentage.
 - a. “Infrastructure costs” are defined to include “costs incurred by a municipal corporation to in a calendar year to acquire, construct, reconstruct, improve, plan, or equip real or tangible personal property that directly benefits or will directly benefit the exempted property.”
 - b. “New employee” is defined to include:

- i. Construction employees who work to construct the real property subject to the TIF exemption (this was settled by a recent Ohio Supreme Court case); and
 - ii. Employees who are first employed at the site of the exempted property and who, within the two previous years, have not been subject, prior to being employed at that site, to the municipal corporation's income tax derived from employment for the person's current employer.
4. Municipal income tax revenue sharing pursuant to R.C. Section 5709.82 is an important consideration for any municipal corporation that intends to establish TIF. One easy way to avoid this confusing process is to agree in the TIF legislation to hold the school district harmless for any real property tax revenue lost as a result of the TIF exemption; or negotiate a city/school district compensation agreement that includes a waiver of income tax sharing.

TAX INCREMENTAL FINANCING IN OTHER STATES

The beginning of this outline provides details concerning Ohio TIF. At this point, we would like to offer general information about TIF schemes in other states. For purposes of the discussions below, the other states being compared are California, Colorado, Florida, Georgia, Illinois, Indiana, Michigan, Missouri, New Jersey, New York, Pennsylvania, and Texas.

Implementation of TIF

In Colorado, Michigan, and New Jersey, only municipalities have the authority to implement TIF, whereas California, Georgia, Florida, Indiana, New York, Pennsylvania, and Texas give authority to municipalities and counties to implement TIF. The state of Illinois provides that municipalities (cities, villages and incorporated towns) and townships that are located in the unincorporated portion of a county with 3 million or more residents (if the county has adopted an ordinance that approved the township's redevelopment plan) can implement TIF.

Use of TIF Funds

Of the states compared, Colorado, Florida, and Missouri limit the use of TIF funds solely to the costs of public infrastructure projects such as highways, roads, streets, bridges, sewer, traffic control systems and devices, water systems, curbing, sidewalks and other public improvements. In contrast, the states of Indiana, California, Illinois, Michigan, New Jersey, New York, Pennsylvania, Texas, and Georgia allow the use of TIF funds in public and private improvements. California, Colorado, Georgia, Indiana, New Jersey, and New York specifically authorize the use of TIF funds to pay debt service on bonds, principal and interest on loans, or advances or indebtedness related to a TIF project.

Blight Finding

All the states referenced above, except for New Jersey, require a finding of blight, as defined by statute, within the proposed TIF project area. Most of these states require an explicit finding of blight. However, Georgia, Indiana, Michigan, and Texas are not clear as to whether a specific finding of blight is necessary for the use of TIF funds. Nevertheless, those states do consider the following:

- whether the area has a need for redevelopment or an economic development area (Indiana);
- whether the potential redevelopment project is in a brownfield development area (Michigan);
- whether the area suffers from substantially arrested or impaired growth, whether the area poses a threat to the public health, safety, morals or welfare in its present condition, or whether the area is located in a federally assisted new community or within a reinvestment zone (Texas); and
- whether the area is deteriorating, dilapidated, or is the location of a predominant number of slum areas which show general signs of disrepair (Georgia).

Written Agreement/Plan

All states, except New Jersey, require a written agreement or redevelopment plan for the use of TIF funds. Usually the agreement or plan will include a general description of the program or project, estimated costs, sources and uses, etc. Agreements or plans may include some of the following specifications:

- Description
- Estimated costs
- Sources and uses of funds
- Project to be constructed
- Public improvements
- Infrastructure
- Community redevelopment plan
- Urban renewal plan undertaken by an urban renewal authority
- Tax incremental plan
- Development and redevelopment
- Project plan
- Financing plan

In New Jersey, although a written agreement is not required to implement TIF, the statute does authorize the municipality's authorizing agency to enter into contracts as may be necessary, convenient or incidental to the execution of the plans and the exercise of the agency's powers. Other states, such as Georgia, Missouri, and Indiana, give similar powers to contract for leases, mortgages, construction, and other agreements necessary to the redevelopment plan. New York gives property owners authority to enter into agreements with the municipality or county to

participate in the redevelopment of the project area. Colorado statutes provide the opportunity for the urban renewal authority to enter into an agreement with the subject county to share the responsibility for constructing an urban renewal project or to share TIF revenues.

Exemption/Redirection and Scope

Generally, states follow the same general scheme for implementing TIF. The exemption (or payment in lieu of taxes) is equal to 100% of the increase in the value of real property over a base amount for a period of 20 - 30 years. This amount is deposited into a fund created for the sole purpose of carrying out the TIF. The fund is terminated after the debt is paid, the project costs have been paid, or pursuant to the terms of the authorizing ordinances.

Many states have variations on aspects of this general scheme. For example, Indiana provides that real property acquired by a redevelopment district is 100% exempt from taxation while owned by the district. Florida only requires use of 95% of the difference between (i) the amounts of ad valorem taxes, exclusive of the debt service millage, levied in a community redevelopment area, and (ii) the amount of the ad valorem taxes prior to the establishment of the TIF. Illinois is also a bit particular in that it requires 100% of the ad valorem taxes levied on the increase in the current equalized assessed value of real property in a redevelopment project for either 23 or 35 years, depending on when the authorizing ordinance was passed, to be used. Missouri also mandates that 50% of “new state revenues” generated as a result of the TIF must be deposited into a special account.

Impact on School Districts

School districts in California, unlike most states, are not affected by TIF because the California school district funding formula offsets any gain or loss in property tax revenue (i.e., the school funding level is maintained regardless of the amount of property taxes collected or not collected). Other states’ TIF statutes specifically address the impact on affected school districts, because the implementation of TIF may reduce the funds available to school districts, depending on how the state funds its schools. Michigan provides for the reimbursement of school districts by the state legislature should revenue be lost because the TIF impairs the affected school district’s ability to meet certain financial obligations. In Georgia, school districts that are not controlled directly by the TIF municipality or county must consent in writing to the inclusion of their millage in the TIF plan. Illinois deals with the issue by authorizing payment to an affected school district to compensate for an increase in enrollment due to the construction of housing units. These payments are generally equal to approximately 8% and 40% of the total property tax increment revenue produced by the housing units.

But For Test

All states discussed, with the exception of Florida, require satisfaction of the “But For Test.” Statutes require that prior to implementation of TIF, the governmental agency must state that but for the TIF, the subject area would remain blighted and underdeveloped. California, for example, requires the plan adopting the TIF to state that “[t]he elimination of blight and the redevelopment of the project area could not be reasonably expected to be accomplished by

private enterprise acting alone without the aid and assistance of the agency.” Georgia’s scheme also allows for the protection of natural or historical assets that may not be adequately preserved without the assistance of the TIF.

State Overviews

California (CAL. HEALTH & SAFETY CODE §33000 *et seq*)

TIF can be implemented by municipalities and counties for up to 30 years and such authority may be delegated to the redevelopment agency of the community. All taxes attributable to the increase of the assessed value of property comprising a redevelopment project must be paid into a special fund of the redevelopment agency. The resulting TIF funds can be used to pay the principal and interest of any loans, monies advanced to, or indebtedness incurred by a redevelopment agency to finance or refinance a public or private development project for commercial, industrial and residential use, as well as recreational and low-to-moderate income housing. The redevelopment agency must make a finding of blight before proceeding with the redevelopment program. A written redevelopment plan must be submitted to the city council or board of county commissioners; the plan must describe specific projects proposed by the redevelopment agency. California also requires satisfaction of the “but for test”: the redevelopment plan must find that the elimination of blight and the redevelopment of the project area could not be reasonably expected to be accomplished by private enterprise.

Colorado (COLO. REV. STAT. §31-25-101 *et seq*)

TIF can be implemented by municipalities for a period up to 25 years, with entities called “urban renewal authorities” tasked with overseeing the operation of “urban renewal projects.” Urban renewal projects include public commercial, residential, and industrial projects. The use of TIF in disaster areas is also a permissible use. All real property taxes on the increase in the assessed value of real property comprising an urban renewal project, and all or a portion of the new sales taxes, are placed into a special fund. The TIF proceeds may be used to make debt service payments on bonds or to make payments to any affected county in connection with an urban renewal project. The 25-year time period can be extended by the municipality with respect to the collection of increased sales taxes if bonds are in default or about to go into default. The urban renewal authority must make a finding of blight before proceeding with redevelopment plans. Colorado requires a written urban renewal plan for each urban renewal project that is undertaken by an urban renewal authority. An urban renewal authority may enter into an agreement with any county to share the responsibility for constructing an urban renewal project or to share TIF revenues. The plan must meet the “but for test” and must afford “maximum opportunity for redevelopment by private enterprise.”

Florida (FLA. STAT. §163.330 *et seq*)

Municipalities and counties can both implement TIF for a period up to 30 years (if created prior to 7/1/02) or 40 years (if created after 7/1/02). This is done by creating community redevelopment agencies to undertake redevelopment. A redevelopment trust fund is created and funded by an amount equal to 95% of the difference between (i) the amount of ad valorem taxes,

exclusive of debt service millage, levied in a community redevelopment area; and (ii) the amount of ad valorem taxes prior to the establishment of the TIF. The fund can be used to pay costs related to the construction of public streets, parks, playground, public portions of hotels and other related improvements for commercial, industrial, and residential redevelopment. The revitalization of coastal and tourist areas is also a permissible use. The county or municipality must pass a resolution making a legislative finding that one or more slum or blighted areas exist before the TIF can go forward. Florida also requires a written community redevelopment plan. Florida does not explicitly require a “but for” showing.

Georgia (GA. CODE ANN. §36-44-1 *et seq*)

Georgia grants authority to municipalities and counties to establish TIF for commercial, industrial, and residential projects for a period of up to 30 years. Municipalities and counties can create “tax allocation districts” and deposit 100% of the “tax allocation increments” related to property taxes on the increase in the assessed value of property in the district, not including bond levies, into a special fund. The tax allocation increments can be used for debt service or for redevelopment costs, which include public and private improvements. School districts not directly controlled by the implementing municipality or county must consent to the inclusion of their millage in the tax allocation increment. If a municipality establishes TIF, the affected counties must consent to the inclusion of their millage in the tax allocation increment. The redevelopment area must be deteriorating, dilapidated, must contain a predominant number of slum areas, or must show other general signs of disrepair before the TIF can be implemented. Additionally, such plans may be used to protect natural or historical assets that would not be adequately preserved or protected without a redevelopment plan. The municipality or county must approve a written plan of redevelopment for the redevelopment area, which must satisfy the “but for test.”

Illinois (65 ILL. COMP. STAT. 5/11-74.4-1 *et seq*)

Municipalities and certain townships are able to establish TIF for a period of 23 or 35 years (depending on the date the TIF was established). The governmental entity implementing the TIF creates a special tax allocation fund in which 100% of the ad valorem taxes levied on the increase in the current equalized assessed value of real property in a redevelopment project area are deposited. The funds may be used for commercial, industrial, and residential redevelopment projects, broadly defined to encompass both public and private improvements. The funds may also be used to provide compensation payments to affected school districts. Payments to any affected school district may be made to compensate the school district for an increase in enrollment due to the construction of housing units through the redevelopment plan. A redevelopment area must be a blighted area, conservation area, or combination thereof. The municipality must prepare a written plan providing for the construction of a redevelopment project. Such a plan must include findings that the project satisfies the “but for test”: that the redevelopment project area would not reasonably be anticipated to be developed without the adoption of the redevelopment plan.

Indiana (IND. CODE §36-7-14-7 et seq)

Municipalities and counties are authorized to establish TIF for a period of up to 30 years and may delegate their powers to redevelopment commissions. One hundred percent of the increase in value of real property in a redevelopment district over a base amount is redirected to a special allocation fund. TIF funds can be used to reimburse local taxing units for the costs of “local public improvements,” to pay debt service on any redevelopment commission bonds, to reimburse public and private entities for certain training expenses, or to pay all or part of a “property tax replacement credit” to certain tax payers. The area in question must require redevelopment, but it is not clear if the redevelopment commission need make a specific finding of blight. The redevelopment commission must submit a resolution and supporting data to the plan commission of the affected municipality or county for approval. The redevelopment commission’s plan must satisfy the “but for test”; that is it must find that the conditions in the area at issue cannot be corrected by regulatory processes or the ordinary operations of private enterprise without resort to TIF. The creation of a redevelopment district must be of public utility. Further, the estimated economic benefits and costs incurred as measured by increased employment and anticipated growth of real property assessed values, and the impact on tax revenues must be disclosed to each affected taxing unit.

Michigan (MICH. COMP. LAWS §125.1801 et seq)

Only municipalities are authorized to implement TIF and the statute does not provide a durational time limit, but it must be long enough to retire any debt issued in the course of implementation. TIF funds may be used for commercial, industrial, residential, and infrastructure improvements. TIF funds can also be used to pay debt service on any redevelopment commission bonds, to reimburse public and private entities for certain training expenses, or to pay all or part of a “property replacement credit” to certain taxpayers. Up to 100% of the tax increment revenues associated with the “captured assessed value” of property in a development or redevelopment district may be paid to the redevelopment authority. If an affected school district’s ability to pay certain obligations is impaired because of the TIF, the state legislature reimburses the school district. The redevelopment authority need not make a finding of blight before proceeding, but elimination of blight can be an eligible activity in a brownfield redevelopment district. A written plan for redevelopment and a written tax increment plan are required. The plan must include a finding that the “but for test” is satisfied.

Missouri (MO. ANN. STAT. §99.800 et seq)

Both municipalities and counties can establish TIF for commercial and industrial projects for no longer than 23 years. Payments in lieu of taxes attributable to 100% of the increase in the current equalized assessed valuation of the taxable real property in the area is deposited into a “special allocation fund”. The monies in the fund are used to pay redevelopment costs and obligations for TIF infrastructure projects within an economic development area; TIF funds cannot be used to construct buildings. Fifty percent of certain “new state revenues” generated because of the TIF are also deposited into the special allocation fund. After incurred project costs have been paid, excess monies are distributed and the special allocation fund is dissolved. On the whole, the redevelopment area must be a blighted area or a conservation area, and must

be lacking in the requisite investment through private enterprise to spur sufficient development. A written redevelopment plan must be generated and should include a general description of the program, estimated costs, anticipated sources of funds, evidence of commitments to finance the costs, among many possible inclusions. The redevelopment plan must satisfy a “but for test,” finding that the redevelopment area has not been subject to growth and development through private investment, and would not be reasonably anticipated to develop such investment without the adoption of TIF.

New Jersey (N.J. STAT. ANN. §52:27D-459 *et seq*)

Municipalities can establish TIF, and no explicit time period is provided for in the statutes. One hundred percent of the “property tax increment” and the incremental value of several other taxes may be pledged to pay debt service or other project costs. Payments in lieu of taxes associated with the “property tax increment” are used to pay commercial and industrial project costs which may include the construction of public and private improvements, housing improvements and other structures located in a municipal economic development revitalization district. A written redevelopment plan is not required, but the municipality’s designated agent may enter into contracts and agreements with entities necessary to carry out the plan. The local finance board must determine that “but for test” has been satisfied by finding that the planned developments would not likely be accomplished by private enterprise without the creation of the TIF and the revenue allocation financing of the proposed project; however, no specific finding of blight needs to be made.

New York (N.Y. GEN. MUN. LAW §970-a *et seq*)

Municipalities and certain counties are authorized to establish TIF, but no explicit time period is provided by the statutes. The TIF is implemented pursuant to a redevelopment plan requiring 100% of the real property taxes associated with the increase in the assessed value of real property in the project area to be placed into a special fund. The TIF funds may be used for commercial, industrial, and residential projects, and may include private and public purposes. TIF funds are often used to make principal and interest payments on debt issued to finance the redevelopment project. Once the debt has been retired, all tax revenues in the project area must be paid to the respective taxing units. A written redevelopment plan must be submitted to the municipality or county for review and recommendation, and then approved by the appropriate legislative body. A finding of blight must be made, and the plan must also satisfy the “but for test” with a statement explaining why redevelopment of the project area would not go forward without the TIF.

Pennsylvania (53 PA. CONS. STAT. ANN. §6930.1 *et seq*)

Municipalities and counties can establish TIF through the creation of tax increment districts that may last for up to 20 years. The funds created by such districts can be used for commercial, industrial, and residential projects, including public works, new buildings, structures or fixtures. One hundred percent of the tax increments associated with a tax increment district are deposited into a special fund until project costs have been recovered. The municipality creating the tax increment district must produce a written plan for redevelopment;

the plan must include a finding of blight. The municipality or county must also adopt a resolution essentially finding the plan satisfies the “but for test” by stating that the area comprising the district as a whole has not been subject to adequate growth and development through investment by private enterprise or would not reasonably be anticipated to be adequately developed without the TIF.

Texas (TEX. TAX CODE ANN. §311.001 *et seq*)

Municipalities and counties can establish TIF. No time limit is prescribed by the statutes. TIF funds may be used for commercial, industrial, and residential projects, including acquisition of blighted/undeveloped property, installation of public works, facilities or sites, or other public improvements. Each taxing unit contributes up to approximately 85% of the property taxes levied on the unit’s tax increment. This amount is generally equal to the property taxes levied on the increase in the assessed value of property in a reinvestment zone. A written financing plan for the zone must be adopted. A specific finding of blight is not required, but the plan must include a showing that the area suffers from substantially arrested or impaired growth, or that it is detrimental to the public health, safety, morals, or welfare in its present condition, among other possible findings. The governing body must also determine that the “but for test” has been satisfied, namely by attesting that redevelopment would not occur solely through private investment in the reasonably foreseeable future.

The ABCs of TIF

A Basic Examination of Tax Increment Financing (“TIF”) from the Perspective of Both Lawyers and Underwriters

PRESENTATION TO THE 2006 JOINT FALL CLE
MEETING OF THE ABA’S SECTION OF TAXATION

AND

THE ABA’S SECTION OF REAL PROPERTY,
PROBATE & TRUST LAW

The ABCs of TIF

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The ABCs of TIF

Our presentation provides details concerning Ohio TIF and comparisons to other select States. We hope this approach will provide you with enough details concerning one state to spot issues and ideas on a micro level and enough generalities concerning other states to understand different ways of addressing TIF issues on a macro level.

The ABCs of TIF

The States Compared are:

California

Colorado

Florida

Georgia

Illinois

Indiana

Michigan

Missouri

New Jersey

New York

Pennsylvania

Texas

The ABCs of TIF

TIF Overview

What is Tax Increment Financing?

TIF is a tool that can be used by political subdivisions to fund infrastructure and, in some cases, site improvements for private redevelopment.

The ABCs of TIF

TIF Overview

TIF relies upon the increase in real property taxes – the “increment” – resulting from improvements to real property.

The ABCs of TIF

TIF Overview

TIF Either:

1. Grants a tax exemption of the increased value in exchange for an obligation to make service payments in lieu of taxes (PILOTS);
or
2. Redirects the increased taxes to a special fund created by the local government

The ABCs of TIF

TIF Overview

The service payments are used to service debt for infrastructure or site improvements, or to reimburse a developer or political subdivision for the construction of infrastructure or site improvements.

The ABCs of TIF

TIF Overview

What TIF is NOT

TIF is not a loan or immediate cash infusion into a project. TIF is a stream of revenue to service project debt or to reimburse a developer or political subdivision for project costs.

The ABCs of TIF

TIF Overview

Who can use TIF?

Generally, the authority to establish TIF lies with the local government. Private companies must work closely with local government officials in order to benefit from TIF

The ABCs of TIF

TIF Overview

Who can use TIF?

Of the states compared:

- CO, MI & NJ authorize only municipalities to implement TIF;
- CA, GA, FL, IN, NY, PA & TX give the authority to municipalities and counties.

The ABCs of TIF

TIF Overview

Who can use TIF?

Of the states compared:

- IL – municipalities and townships; however, county must have approved township's redevelopment plan if in an unincorporated area of a county of three million or more

The ABCs of TIF

TIF Overview

Why use TIF?

- *TIFs can provide a consistent revenue stream for project costs for up to 30 years.*

Note: In Ohio and many other states, cooperation from other entities affected by the tax exemption or redirection, such as the local school district, may be necessary.

The ABCs of TIF

TIF Overview

Why use TIF?

- *Property owners don't see or feel any difference*
 - service payments are in the same amount and are paid at the same time and in the same manner as the real property taxes that would be due on the increase in the assessed value of the property

The ABCs of TIF

TIF Overview

Why use TIF?

- *TIFs are valuable*

Although each situation is different, most TIFs can generate at least \$1 million in revenues for each \$10 million in “improvement.”

The ABCs of TIF

TIF Overview

Interaction with School Districts

- Generally, states require that school districts either:
 - Retain a portion of the tax revenue
 - Are made whole; or
 - Participate in the PILOTS

The ABCs of TIF

TIF Overview

Interaction with School Districts – Ohio

- The affected school district must approve a TIF that exempts more than 75% of the new real property taxes or lasts longer than 10 years.

The ABCs of TIF

TIF Overview

Interaction with School Districts – Ohio

- Political subdivisions have the authority to enter into compensation agreements with the school district.
 - The local government can agree to compensate the school district for some or all of the lost revenue.

The ABCs of TIF

TIF Overview

Interaction with School Districts – Ohio

- Private companies can also enter into compensation agreements with school districts and political subdivisions.

In the alternative . . .

The ABCs of TIF

TIF Overview

Interaction with School Districts – Ohio

- The local government can create a “hold harmless” TIF that pays to the school district the amount it would have received but for the exemption.

The ABCs of TIF

TIF Overview

Interaction with School Districts – Ohio

- If the TIF keeps the school district whole:
 - The school district must get notice, but has no approval authority
 - The payments reduce the net value of the TIF to the project

The ABCs of TIF

TIF Overview

Interaction with schools – other states

- NY – school's taxes NOT INCLUDED in increment
- GA – authorizes “make whole” payments to school district
- MO – requires surplus to pass through to school district

The ABCs of TIF

TIF Overview

Interaction with schools – other states

- IL – if the project includes housing that adds to school enrollment, increased school district operating costs are allocated from the increment (up to 40%)
- GA – if the district is not controlled by the TIF entity, the school district must consent

The ABCs of TIF

TIF Overview

Interaction with schools – other states

- CA – schools insulated from the TIF by the state funding formula
- MI – schools reimbursed by the state if the TIF impairs its ability to meet certain funding obligations

The ABCs of TIF

TIF Overview

Blight

- All of the states compared, except NJ, require a finding of “blight”
- In some of these states, a specific blight finding is not required, but blighting influences are considered . . .

TIF Overview **The ABCs of TIF**

Blight

- IN – does the area have a need for redevelopment or is it an “economic development area”
- MI – is the project in a “brownfield development area”
- GA – is the area deteriorating, dilapidated, or is it the location of slum areas showing signs of disrepair

The ABCs of TIF

TIF Overview

Blight

- TX – does the area suffer from substantially arrested or impaired growth, does the area poses a threat to the public health, safety, morals or welfare, is the area located in a federally assisted new community or within a reinvestment zone

The ABCs of TIF

TIF Overview

The “But For” test

- All of the states compared, except FL, require a finding that, but for the TIF, the area will remain blighted and underdeveloped
- GA allows for the protection of natural and historic assets that may not be preserved without TIF assistance

The ABCs of TIF

Types of TIFs

TIFs are generally categorized by the use of the TIF proceeds:

- Public Infrastructure
- Assistance with Project Costs

The ABCs of TIF

Types of TIFs

Public Infrastructure includes the typical work, such as water & sewer lines and streets. In Ohio, this phrase also includes:

- “land acquisition, including acquisition in aid of industry, commerce, distribution, or research” and
- “demolition on private property when determined to be necessary for economic development purposes.”

The ABCs of TIF

Types of TIFs

Ohio also recognizes a subset of the public infrastructure TIF known as the Incentive District TIF

- An Ohio Incentive District TIF is subject to most of the same restrictions as other TIFs,

HOWEVER . . .

The ABCs of TIF

Types of TIFs – Ohio Incentive District TIF

- *Portions of proceeds must sometimes be shared with other taxing units,*
- *Residential improvements can be exempt,*
and
- *Proceeds can be used to fund housing renovations.*

The ABCs of TIF

Types of TIFs – Other States

- *CO, FL & MO limit the use of TIF funds to public infrastructure*
- *CA, GA, IN, IL, MI, NJ, NY, PA & TX allow use of TIF funds for public and private improvements*

The ABCs of TIF

Types of TIFs

Ohio Urban Redevelopment TIF

- The local government declares the increase in assessed value to be a “public purpose” and exempt from real property taxes.
- This type of TIF differs from other Ohio TIFs in several important ways:

The ABCs of TIF

Types of TIFs

Ohio Urban Redevelopment TIF

- The local government must have held title to the property prior to passage of legislation authorizing the TIF,
- The property is leased or conveyed to another person either before or after adoption of the TIF legislation,

The ABCs of TIF

Types of TIFs

Ohio Urban Redevelopment TIF

- The local government has the option of requiring service payments in lieu of taxes,
 - Consequently, this type of Ohio TIF can act as a 30-year tax exemption.

And

The ABCs of TIF

Types of TIFs

Ohio Urban Redevelopment TIF

- TIF proceeds can be used “for such purposes as are authorized in the resolution establishing the fund.”
- The local government has wide latitude in determining how the TIF proceeds can be used, subject only to the Ohio Constitution

The ABCs of TIF

Types of TIFs

Ohio Urban Renewal Debt Retirement TIF

Key Differences

- Authority to issue bonds to fund project costs, and service payments are used to pay debt service on the bonds
- Projects are within an “urban renewal area”

The ABCs of TIF

Types of TIFs

Ohio Urban Renewal Debt Retirement TIF

- Must have a development agreement
 - Developer agrees to make certain improvements within the urban renewal area
 - Developer and all subsequent property owners agree to make required service payments

The ABCs of TIF

Types of TIFs – other states

- *Other states utilize other tax increments, in addition to real property taxes*
 - IL allows capture of increases in sales taxes
 - NY – A recent interpretation of PILOT includes what had been various local taxes in the increment
 - MO – utilizes an Economic Activity Tax

The ABCs of TIF

Recent Developments – Ohio

Incentive District TIFs

- 25% Test
- Must Specify a project
- Other political subdivisions have approval rights in certain circumstances
- Certain levies excluded

The ABCs of TIF

Recent Developments – Ohio

Traditional Infrastructure TIFs

- No longer requires a correlation between the percent exemption and percent increase in demand on infrastructure
- No longer required to show direct, additional demand on infrastructure being constructed or improved

The ABCs of TIF

Recent Developments – Ohio

Interaction with School Districts

- Ohio's school funding formula is very complex – schools are funded both by the state and by local property taxes
- Now, the state portion will be reduced by the amount of funds a school district receives pursuant to a compensation agreement for some TIFs

The ABCs of TIF

Case Study – Ohio

Project – Improvement and Expansion of a Downtown Campus

Client would like to improve its existing building (\$4MM), construct a new building (\$40MM), and improve the infrastructure around its downtown campus to enhance access and the surrounding area

The ABCs of TIF

Case Study – Ohio

TIF Solutions

- Incentive District TIF
 - applied to the area surrounding the client's property
 - funds redevelopment of public infrastructure
- Urban Redevelopment TIF
 - applied to the client's property
 - generates funds to assist with client's project costs

The ABCs of TIF

Case Study – Ohio, Easton

Project – 1200-acre mixed-use (office, retail, residential, recreation) development

TIF Solutions

- Project supported \$30,000,000 of TIF bonds in 1999, and was refinanced in 2004 for \$36,000,000

The ABCs of TIF

Case Study – Ohio, Easton

TIF Solutions

- School district kept whole
- Excess TIF proceeds captured to retire bonds early
 - The project was so successful that the increment was also used for infrastructure several miles away (this temporary provision of Ohio law has since expired)

The ABCs of TIF

Case Study – Ohio, Easton

Credit Characteristics

- Original LOC provided by the developer; revenue threshold achieved and LOC dropped with refinance
- early retirement provisions dropped upon refinance;
- credit ultimately attracted ‘AAA’ rated municipal bond insurance.

The ABCs of TIF

Case Study – GA, Atlantic Station (Atlanta)

Project – Redevelopment of 160-acre former Brownfield for residential, retail, office, entertainment, & hotel

TIF Solutions

- Utilizes increment from real property improvements and sales taxes
- Bonding capacity recently increased to \$500,000,000

The ABCs of TIF

Case Study – GA, Atlantic Station

Credit Characteristics

- Over \$150,000,000 in bonds outstanding
- Bonds not yet rated or offered in full public offering
- Bonds featured third-party credit enhancement

The ABCs of TIF

Case Study – CA, Centre City, San Diego

Project – 1400-acre redevelopment in urban center

TIF Solutions

- Implemented under CA Community Redevelopment Law
- Multiple bond issuances over time to fund public infrastructure, parking, and housing

The ABCs of TIF

Case Study – CA, Centre City, San Diego

Credit Characteristics

- TIF revenue is growing due to diversification of tax base within area – bonds marketed as if funding essential government projects.
- Redevelopment authority has previously issued eleven series of bonds totaling over \$300 million.

The ABCs of TIF

Case Study – IL, *Prairie Springs*

*Project – 512 detached, single-family units
and necessary public infrastructure*

TIF Solutions

- 80% of increment available to pay debt service – other 20% to schools, but all or part goes back to project if schools do not show net new students

The ABCs of TIF

Case Study – IL, *Prairie Springs*

TIF Solutions

- TIF bonds partially reimburse developer for eligible construction-period expenses

The ABCs of TIF

Case Study – IL, *Prairie Springs*

Credit Characteristics

- Bonds issued after first-phase public improvements completed
- Village limits developer reimbursements until both phases complete

The ABCs of TIF

Case Study – MO, Branson Hills

Project – Retail “power center” anchored by Home Depot, Target, and TJ Maxx

TIF Solutions

- Proceeds financed wide range of private costs – land acquisition, site preparation, and public improvements
- Captures real property and sales tax increment

The ABCs of TIF

Case Study – MO, Branson Hills

Credit Characteristics

- Major tenants, not developer, provided limited guarantees
- Bonds limited to institutional sale
- Bond proceeds insufficient – developer issued taxable, subordinate note repaid from excess TIF proceeds

The ABCs of TIF

Practical Structuring Issues – Ohio

Constitutional Issues

- Generally, a political subdivision is prohibited from lending its credit to or in aid of a private enterprise

However . . .

- Government can make loans, etc. to create and preserve job opportunities relating to industry, commerce, distribution, and research.

The ABCs of TIF

Practical Structuring Issues – Ohio

Issuance of debt

Local government can issue either:

- General obligation bonds, backed by the full faith and credit of the municipality OR
- Revenue bonds supported by a specific stream of revenue – the TIF service payments

The ABCs of TIF

Practical Structuring Issues – Ohio

Developer Financing

- Under most Ohio TIFs, the developer can agree to make the improvements and be reimbursed over time from the TIF service payments

The ABCs of TIF

Practical Structuring Issues

Credit Enhancements

- Local Government
- Letter of Credit
- Minimum Service Payments
- Mortgages
- Special Assessments

The ABCs of TIF

Practical Structuring Issues

All states, except NJ, require a written agreement and/or plan

- Agreements generally include a description of private and public improvements, a budget, etc.
- Some states (and municipalities) require an urban renewal plan or a community redevelopment plan

The ABCs of TIF

Potential Pitfalls – Ohio

Exemption Priority Rules

- Local government files for the exemption without the property owner's consent

OR

- Local government files with the property owner's consent or the property owner files

The ABCs of TIF

Potential Pitfalls – Ohio

Marketability of TIFed property

The credit enhancements noted above frequently encumber the TIFed property, which may decrease the value of the property in the eyes of some buyers.

The ABCs of TIF

Potential Pitfalls – Ohio

Income Tax Revenue Sharing

- if the TIF project will generate more than \$1MM in new employee payroll, and
- the TIF does not keep the school district whole,
 - the school district must share in the payroll taxes collected by the local government.