Tax Incremental Financing (TIF)

TIF is a partnership between a municipality and its overlapping taxing jurisdictions used to pay costs associated with stimulating economic development. The additional (incremental) taxes generated by the economic development that takes place are then used to repay those costs. TIF is commonly used to address challenging development sites, public infrastructure needs or lack of economic activity in an area. There are several types of tax incremental finance districts (TIDs) that municipalities can create depending on the type of development expected to occur and the characteristics of the area:

- Industrial
- Mixed Use
- Blighted Area
- In Need of Rehabilitation of Conservation
- Environmental Remediation

A TID may remain open for a term of either 20- or 27-years dependent upon the type of district created.

TIF Premise

The premise of TIF is that "but for" the creation of a TID the desired development:

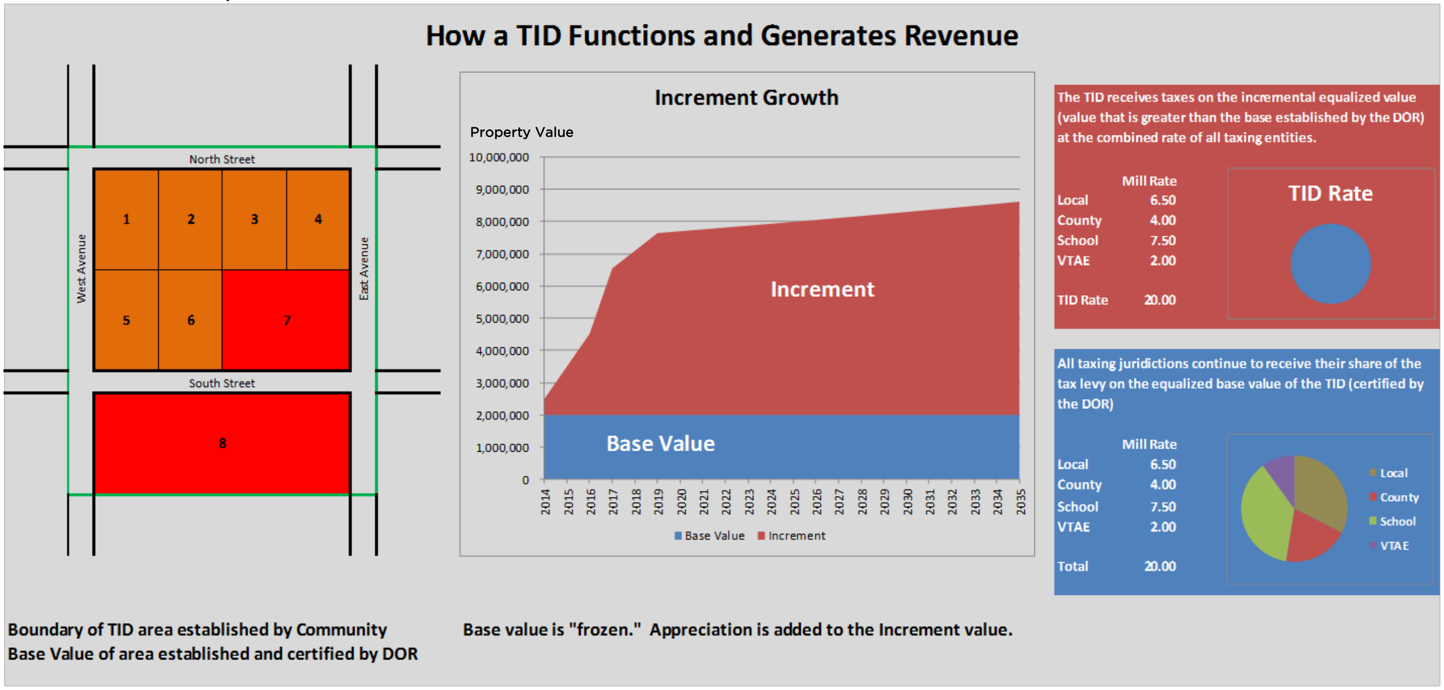
- may not occur at all.
- may not occur in the same time frame.
- may not achieve with the same value.
- may not provide the same amenities.
- may not result in the same level of job creation.

A best practice to substantiate the "but for" test is to engage a qualified firm to undertake an independent review of a development project's sources, uses, and cash flows with and without TIF assistance to determine if TIF participation is warranted. An oversight body composed of representatives of each taxing jurisdiction called the Joint Review Board (JRB) must ultimately conclude that the "but for" standard has been met before a community can finalize creation of a TID.

How TIF Works

A TID may contain only whole parcels and all parcels must be contiguous. Once the boundary is defined, the current value of the real and personal property of the TID is totaled to establish the "base value". All taxing jurisdictions (school district, technical college, county and the municipality) continue to receive their proportional share of tax revenue on this base value.

When a TID's value increases above the base value due to new development or appreciation of existing values, this is called the "incremental value". The municipality retains all taxes generated from the incremental value to pay for projects within the TID. The other taxing jurisdictions agree to forego their proportional share of taxes on the new development until the TID closes and the increment value returns to the tax rolls benefitting all taxing jurisdictions. The inset graphs illustrate how this tax capture mechanism functions.



Types of TID Projects

TIF can be used to pay for infrastructure and other public improvements, financing costs, real property assembly costs, professional service costs, administrative costs, relocation costs, development incentives, environmental remediation, and certain types of projects outside of the TID's boundaries. The term during which costs may be incurred, referred to as the "expenditure period", ends five years before the maximum life of the TID. Provided that a commitment to a project is made prior to the end of the expenditure period, associated debt service, repayment of advances, and development incentives can be paid beyond the end of the expenditure period. Projects costs within a TID are detailed in a "Project Plan" that specifies what projects are eligible to be paid for by a TID.

TID Limitations & Amendments

To create a TID, or to add territory to an existing TID, a community must comply with the "12% test". This test specifies that the incremental value of any existing TID's, plus the base value of the new TID or that of the territory being added to an existing district, cannot exceed 12% of a community's total equalized value. If a community exceeds the 12% limitation, new TID's cannot be created nor can territory be added to an existing district. A community that is "TIF'd out" may be able to achieve compliance by closing or subtracting territory from an existing TID.

An existing TID can be amended to add or subtract territory up to four times during its life. A TID can also be amended to modify its list of project costs at any time during its expenditure period. Other types of amendments allow for sharing of excess revenue with another TID, extension of maximum life, and a reset of base value. A TID must meet certain requirements to qualify for these latter types of amendments.

TID Process

The general process municipalities must undertake to create or amend a TID is as follows:

1. Undertake a feasibility study and develop a Project Plan.
2. Convene an organizational meeting of the JRB.
3. Hold a public hearing before the Plan Commission, Community Development Authority or Redevelopment Authority.
4. Plan Commission, Community Development Authority or Redevelopment Authority approval of the TID Project Plan and provision of a recommendation as to the TID's boundaries.
5. Approval of the TID by the municipality's Governing Body.
6. JRB approval.
7. Submittal to the Department of Revenue for review and certification.

For planning purposes, it is recommended that a community allow for at least three months from the time development of a Project Plan begins to final approval by the JRB. The JRB meetings and the public hearing require publication of legal notices and certain other timing requirements must be followed that will impact when meetings can be scheduled.

TID Benefits & Risks

The primary benefit of a TID is it can be used to expand and diversify the tax base and accomplish economic development objectives in comprehensive plans. A TID is a partnership that allows economic development projects to be funded with assistance from other taxing jurisdictions, recognizing that all jurisdictions ultimately benefit from that development. However, if a TID underperforms the municipality bears the risk. Municipalities are still obligated to pay debt service costs if increment is insufficient and TIDs may require support from other funds to pay for project costs. Advances from other funds, if required, may never be repaid. Steps can be taken to mitigate risk by requiring developers to provide letters of credit, valuation guarantees or shortfall payments, or by levying special assessments against the development project. A common way of further mitigating risk is to provide TIF assistance on a "pay as you go" basis where the development must fund all costs up front and is repaid from the tax increments as they are received over time.