## *Tax Increment Financing*

Tax increment financing (TIF) is a method of encouraging the redevelopment of rundown areas or brownfield sites through strategic investments in infrastructure – with the infrastructure investments financed by the increases in property taxes resulting from the improvements in properties in the areas.

The theory behind TIF is that underdeveloped or blighted areas can be improved by investments in infrastructure which will (at least) pay their way by stimulating private investments and improvements in the local area. If successful, the effect of the infrastructure investments on the local area will result in higher property tax revenues as a result of:

- New private investments in the area – which will result in a new stream of property tax revenue; and,

- Higher property taxes from existing properties in the area – as a result of increased property valuations which flow from the enhanced desirability of the area because of the TIF investments.

TIF is unlike local improvement charges, which some municipalities have used to finance the installation of infrastructure in particular areas. With local improvement charges, the cost of the infrastructure is spread over a period of years, and paid off (with interest) by the owners of properties in the area, through a special assessment on top of their normal property taxes. With TIF, property owners do not pay a higher tax *rate* than other properties in the municipality, however, it is expected that their property taxes will rise faster than taxes in other areas – due to higher rates of increase in property valuations as the area improves.

In the U.S., TIF is used in many states. The process involved in initiating a TIF varies from state to state but typically includes a number of steps:

- Identification of an area in need of improvements and enhanced infrastructure – and expectation that provision of these will result in new private investment and an improvement in the area. This can occur either through a top-down process whereby the local municipality or other authority launches the scheme, or through a bottom-up process whereby local property owners petition for such designation. In general, there are specific criteria for an area to be selected for improvement – for example, in San Antonio, an area must meet one or more of the following criteria to be considered for TIF:

  "The area's present condition must substantially impair the city's growth, retard the provision of housing, or constitute an economic or social liability to the public health, safety, morals, or welfare. Furthermore, this condition must exist because of the presence of one or more of the following conditions: a substantial number of substandard or deteriorating structures, inadequate sidewalks or street layout, faulty lot layouts, unsanitary or unsafe conditions, a tax or special assessment delinquency that exceeds the fair market value of the land, defective or unusual conditions of title, or conditions that endanger life or property by fire or other cause." [City of San Antonio website]

- Assessment of the types of investments necessary to improve the area – these can include traditional infrastructure investments such as roads, water and sewer works, as well as a wide variety of expenditures for things like planning, management, promotion, security, parks and recreation facilities, historic preservation, etc.

- Determination of the base level of property taxes in the area, and the likely increases in property taxes which will result from the improvements and infrastructure investments. Typically, the TIF establishes the base amount of property taxes generated in the area and allocates (all or a portion of) increases in property taxes to fund the planned works until they are fully paid-for (with interest) or for some specified period. If more than one jurisdiction is involved in collecting property-based taxes (e.g. school boards, other levels of municipal governments, or other local authorities), agreements must be reached on whether they will participate in the scheme – to the extent that other jurisdictions do not participate, the expected revenues generated will be less and the scheme may not be self-financing.

- Cost-benefit analysis – for TIF to be self-financing, the costs associated with the investments required must be able to be financed (with interest) through the expected increases in property taxes. Typically, TIF schemes are financed through a municipal bond which must be repaid over time – if tax revenues from the area do not increase as planned, the municipality will be responsible for making up any shortfall. Therefore, it is important that municipalities ensure that the assumptions and projections behind the establishment of a TIF are realistic.

Provincial enabling legislation is required before municipalities can use tax increment financing in Canada. Some municipalities are looking at the potential; however, no province has passed the necessary legislation at this point.

If successful, TIFs can be a win-win for municipalities and the local area: the area is redeveloped so local property owners benefit; not only is there is no cost to the municipality associated with the necessary investments but, over the long-term, after the TIF loan is repaid, the municipality benefits through higher tax revenues from the area.

However, in structuring a tax increment financing arrangement, it is extremely important that the necessary due diligence be undertaken. If, for example, the expected increases in property taxes resulting from the new investment do not occur, the repayment of the bond will still be required – to be funded, most likely, by taxpayers in the municipality as a whole.