MUNICIPAL TAX INCREMENT FINANCING (TIF)

This has been prepared by NMDC with the goal of familiarizing the reader with how TIF works. ***This NOT intended to replace program regulations or state statute governing Tax Increment Financing.*** *For more information, you may wish to contact Tina Mullin at DECD, a legal firm experienced with Tax Increment Financing, or for general guidance, Alain Ouellette of Northern Maine Development Commission.*

Municipal Economic Development

A municipality may choose to support local economic development projects – from infrastructure improvements to business expansions and relocations - by providing financial assistance through the use of the new property taxes generated from the investments, i.e. the tax "increment."

Program Summary

TIF is strictly a local economic development tool that permits a municipality to use all, or a portion, of the new property taxes that result from an investment project within a designated district, to assist in that project's financing. The municipality has the option of issuing bonds, which are retired using the tax increment, or paying the tax increment directly to the investing business to help pay project costs.

TIF districts may be designated for a period up to 30 years. Bonds may be issued under this program for up to 20 years. The designation of a TIF district requires a public hearing and the majority vote of the municipal legislative body.

Program Example

A business expects to invest $500,000 in buildings and site improvements on vacant land presently valued at $100,000, and construct a $400,000 manufacturing center. The municipality's property tax mil rate is $20 per $1,000 of valuation, so the business will have a tax obligation of $20,000 per year once the investments are recorded on the tax rolls. Of this tax obligation, $18,000 is incremental, and therefore eligible for TIF.

Scenario 1: Credit Enhancement Agreement. The municipality agrees to "capture" 75% of the incremental tax revenues for a period of fifteen years and return them to the business to assist in financing the new building. The business would receive $13,500 in the first year of TIF, though subsequent payments might be adjusted for equipment depreciation, real estate appreciation, and future capital investments. All things being equal, however, the business would receive approximately $202,500 over the life of the TIF district.

Scenario 2: Municipal Bond Financing. The business needs a road and utilities installed for $150,000. The municipality agrees to pay this cost, issuing a 20-year TIF bond in the amount of $150,000. Annual debt service on the bond will be $12,338, which the municipality will "capture" out of the incremental taxes.

More Information

The remaining pages of this "information" section provide a more thorough discussion of the TIF program.

How to Apply

Please fully address each part of the attached application which includes a cover sheet and "application requirements." Submit completed applications to the Department of Economic and Community Development, 59 State House Station, Augusta, ME 04333-0059. All applications will be reviewed by the Department on a timely basis, and in the order they are received. Applicants will be notified of their acceptance or rejection in writing. If you have any questions, need assistance or require additional information, please contact Tina Mullins of DECD at 624-9816.

Tax Increment Financing

"TIF" is a **local** economic development financing program that uses all, or part, of the tax revenues generated from new capital investments, i.e. tax "increment," to reduce bond debt issued for the project, or pay the investing company directly for project costs incurred;

A "shelter" against adverse adjustments to state subsidies and county taxes based on total valuation; and

A powerful, flexible economic development tool for municipalities to support job creation, capital investment and a broadening of the local tax base.

TIF Revenue Uses

Capital costs, including:

- construction or improvement of public works, new buildings or structures and fixtures;
- demolition, repair or remodeling of existing buildings, structures and fixtures;
- acquisition of equipment; and site work.

Financing costs, including:

- all interest paid to holders of evidences of indebtedness (notes, bonds, etc.) issued to pay for project costs (either municipal or corporate); and

- any premiums to be paid for early redemption of obligations.

- Deficits incurred by a municipality from making real or personal property within a development district available to the developer at a cost below that of the municipality (e.g. rent subsidies and sale of assets at a price below acquisition cost).

- Professional services, including, but not limited to, architects, engineers, planners, and attorneys.

- Administrative expenses, including those incurred by municipal employees in connection with the development program.

- Relocation costs.

- Organizational costs, including environmental and other impact studies and public information processes.

- Certain infrastructure associated with the project, whether or not physically located in the development district, including:
    - sewer and water handling and treatment plants;
    - road construction or improvement;
    - utility installation;
    - environmental protection devices and facilities; and sewer, storm sewer, and water lines.

- Payments made at the discretion of the local legislative body, and considered necessary or convenient to the implementation of project plans, or the creation of development districts. These must be economic development project costs and specified in the development program.

- Employee training, limited to 20% of total project costs, and designated as "training funds" in the development program.

- Other improvements, including:
    - development of new employment opportunities;
    - promoting public events;
    - advertising cultural, educational and commercial activities;
    - public safety;
    - and administrative and management support.

TIF Revenue <u>Prohibitions</u>

Project costs associated with buildings used predominantly for the general conduct of government, or for public recreational facilities.

How Municipal Development Works *Without* TIF

A municipality's total Equalized Assessed Value (as of April 1) is used to compute:

General Purpose Aid to Education (subsidy)
State Revenue Sharing (subsidy)
County Taxes (expense)

State subsidies change inversely to value; County taxes change directly.

As total value increases (through inflationary growth and increased investment), the municipality will realize a decrease in Education and Revenue Sharing subsidies, and an increase in County tax obligations.

Therefore new tax revenues resulting from a development project are reduced through loss of subsidies and increased county taxes.

How TIF *Helps* Municipal Development

TIF allows the municipality to "shelter" new value resulting from certain development projects from the computation of its State subsidies and County taxes.

The sheltering allows the municipality to retain all or a portion of those new tax revenues otherwise passed on to the County and State.

The municipality achieves the sheltering effect by designating a specific geographic area as a Municipal Development Tax Increment Financing District.

The designation "freezes" the value of taxable property within the district with respect to the State and County.

Criteria for District Designation

At least 25% of the District area must be:

- Blighted; or
- In need of rehabilitation, redevelopment, or conservation; or
- Suitable for industrial (commercial) sites.

Municipal legislative body designates the district, and must consider the effect of this action on other "interested parties."

DECD's Commissioner reviews and approves proposals based upon statutory compliance.

TIF Limitations

Geographic: no single district may exceed 2% of the total acreage of the municipality; the total of all districts may not exceed 5% of the total acreage of the municipality. The boundaries (area) of a designated district may be altered only through the statutory district adoption procedure.

Value: the total value (as of the April 1st preceding designation) of all taxable property within a district to be designated, plus the value of all existing TIF districts (at the time of their designation) cannot exceed 5% of the municipality's total equalized value as of the current property tax year.

Municipal Indebtedness: the total amount of municipal debt financed through TIF districts within any county may not exceed $50 million.

Term: Bonds may be issued for a maximum of 20 years (anticipation notes for three years). TIF districts may be designated for a maximum of 30 years.

Funding Mechanisms

Initially only one approach, i.e. ***bonding***, was used to fund TIF projects. A second mechanism, called a ***credit enhancement agreement***, is now very popular and widely utilized by municipalities. The two methods, and the particular payment account that each must have, is highlighted below:

The issuance by the municipality of General or Limited Obligation Bonds require TIF revenues to be placed in a ***Development Sinking Fund*** established to repay the debt created by the bond, and/or

Direct payment by the municipality, through a Credit Enhancement Agreement with the company, in which either fixed dollar amounts, or a percentage of TIF revenues, are placed in a ***Project Cost Account*** in order to pay authorized project costs.

One development project may be financed using both bonds and a credit enhancement agreement. Terms of financing vary. Declining percentage retention schedules are common.

Credit Enhancement Agreement

A mechanism to assist the development project by using all, or a percentage, of the tax revenues generated by the new investment to pay certain authorized project costs, including payments made directly to the company. CEA's are developed by a legal firm with particular expertise in their development.

Advantages of the Credit Enhancement Agreement

- Municipality automatically indemnified against risk of insufficient tax increment revenues to meet debt service requirements.
- $50 million county debt cap for TIF districts does not apply.
- Public approval often easier to obtain.
- Easily accounts for revaluations.
- Allows municipality to provide a direct cash subsidy to business(es) within the district for up to 30 years.
- Flexibility
- Percentage of tax revenues retained may vary over life of district.
- Can finance multiple project costs.
- Possible to "share" unanticipated additional tax revenues.
- Business may pursue best available financing in private sector.

Disadvantages of Credit Enhancement Agreement

- Tax-exempt municipal bond interest rate not available.
- Municipality's TIF participation may not be limited to a fixed amount.

Municipal Debt (Bonds)

A mechanism to fund development projects through the issuance of municipal general obligation bonds or limited obligation bonds.

Advantages of Municipal Debt

The municipal bond tax-exempt interest rate may significantly increase the total amount of financing available.

The municipality's support for the project is fixed with respect to amount and term...a "clean and simple" package.

Disadvantages of Municipal Debt

Risk exposure:

- Municipality remains liable for debt service on general obligation bonds if tax increment revenues are insufficient (shortfalls may be guaranteed by the developer).

- Voters are generally debt averse, so approval is often more difficult to obtain.

- $50 million cap on total TIF debt per county could be a factor, especially in Southern Maine.

- Revaluations can negatively affect tax increment revenues available for debt service, requiring an amendment to the original approval.

CHECKLIST: Preparing a Tax Increment Financing Plan and Application

Development Program ... a statement of means and objectives...

Designation Process

- Notification of public hearing in newspaper of general circulation ten days prior to the public hearing.

- Public hearing.
- Majority vote of town legislative body.
- Application to DECD.
- DECD commissioner approves.

Application Components

- Cover Sheet.
- Development Program.
- Calculations of tax shifts.
- Evidence of public hearing notice.
- Record of district designation by municipal legislative body.
- District area and value certifications.
- Map and description of district.
- The Development Project to be financed.
- Financial Plan...a statement of costs and sources of revenue required to accomplish the development program to include:
    - Cost estimates for the program.
    - Indebtedness to be incurred.
    - Sources of anticipated revenues.
    - Estimates of Captured Assessed Values (CAV).
    - CAV and resulting tax increment revenues to be applied to the program each year.
    - Estimated impact of district on all taxing jurisdictions in which district is located.
    - List of public facilities to be constructed (if any).
    - Uses of private property within district.

- Plans for relocation of persons displaced by development activities.
- Proposed traffic improvements.
- Environmental controls to be applied.
- Proposed operation of the district after capital improvements are complete.

Duration of district (not to exceed 30 years).

Program Policy Notes

Municipal TIF Policies. TIF projects often catch municipalities by surprise. It is never too early to be learning how this powerful and increasingly popular program works, or to begin developing a *local policy* for its use, both as a proactive development tool, and in response to proposals from existing businesses. Creation of a clear policy document initially requires TIF “education” for the municipality. Then it takes public deliberation. The eventual document articulates the will and values of the community. It acts as a benchmark for the evaluation of projects requesting public investment, and when done well, can serve as a negotiating tool for the municipality. A number of municipalities have prepared, or are in the process of preparing, TIF policies.

Project Costs. DECD will look to legislative findings in considering project costs, like “creation and retention of jobs” and “broadening of the tax base,” that are not clearly addressed in statute. Project costs should, wherever possible, be contained within the TIF district, even if this means extending the district, e.g. to include surrounding roads. Any project costs not actually within the district must be clearly related to it (physically or operationally), or constitute a bona fide economic development purpose.

New Reporting Requirements. The new statute requires employers who are applicants for specified economic development incentives (TIF being one of seven) to disclose the public purpose and project uses supported by the economic development incentive, and the employer’s goals for the number, type and wage levels of jobs that will be created or retained. Additionally, recipients of more than $10,000 per year must file an annual report containing more detailed information about the amount of economic development assistance received and the employment creation or retention experience of the employer.

Early Contact with DECD. Tax Increment Financing continues to be one of the most powerful and flexible programs in support of economic development available in the State of Maine. It is clearly a local initiative, however, and DECD's oversight role is intended to ensure statutory compliance. DECD staff welcomes early project involvement in order to provide timely assistance so that a TIF proposal is approvable upon receipt at the Commissioner's Office.

Laws and Rules

30-A M.R.S.A. §§5251-5261: Municipal Development Districts

36 M.R.S.A. §§208 and 305: Equalization of Property Tax Assessments

5 M.R.S.A. §13070-J: Return on Public Investment from Economic Development Incentives

19-100 CMR ch. 1: Municipal Tax Increment Financing Rule