

# TIFs: Harder than Before But Still Viable

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# Today's Topics

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- TIF Structuring Basics
- TIFs in Ohio
- TIF Financing Today
- The Revenue Dilemma/TIF Monitoring
- TIF Examples
  - Queen City Square Tower
  - One Neighborhood Condominium Project



# TIF Structuring Basics

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- TIF = Tax Increment Finance
- Using new “incremental” revenues to finance projects
- Revenue types
  - Property taxes - - most common
  - Sales taxes
  - Utility taxes
  - Earnings taxes



# TIF Structuring Basics

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- Project types
  - Public Infrastructure - - most common
  - Public buildings and structures
  - Commercial and office (e.g. Ohio Revised Code 5709.41)
- Infrastructure types
  - Parking lots and structures
  - Roads
  - Sewer/water systems or connections
  - Landscaping and lighting



# TIF Structuring Basics

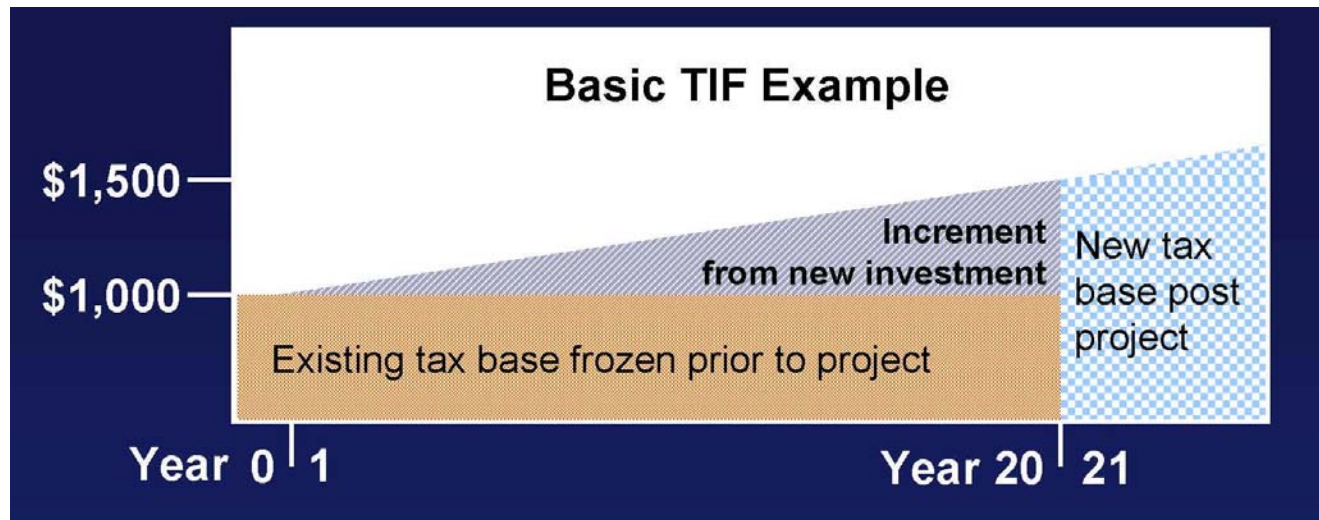
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- Public Buildings
  - Schools
  - Libraries
  - Service centers (fire, police)
  
- Commercial and Office
  - Public spaces
  - Environmental systems
  - Transportation aspects (e.g. elevators and escalators)
  - Even private spaces



# TIF Structuring Basics

- Allows local governments to invest in infrastructure and other improvements and pay for them by capturing the increase in property tax revenues generated by the enhancements (See the pre-2008 model below)



- Recent (2008-2010) financial modeling assumes no growth in the increment. It is assumed to be flat with no increase in property values. More coverage is required too.

# TIF in Ohio (as an example)

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- ❑ TIF usually put in place by legislation of Township Trustees or Municipal Council
- ❑ Provides an exemption from property taxes that would be generated from the increased value of a development project – the exemption applies only to the tax increment generated from the increased in value
- ❑ Existing property taxes continue to be paid to the respective governmental entities
- ❑ The owner of the property is required to make “service payments in lieu of taxes” (commonly called service payments or PILOTs) with respect to the exempted real property taxes



# TIF in Ohio

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- ❑ PILOT payments can reimburse the developer for infrastructure cost, under a Developer Construction Agreement
- ❑ PILOT payments can be used as security for new bonds
- ❑ Can be revenue bonds or GO bonds, with PILOT payments assigned to the issuer of the bonds
- ❑ The PILOT payments are then used to pay debt service on the bonds, together with any other revenue sources



# TIF Bonds in Ohio

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- ❑ In Ohio, it is common for a Port Authority to serve as the issuer of TIF and/or Special Assessment Revenue Bonds
- ❑ Port Authorities can finance governmental, housing and economic development facilities
- ❑ Five Port Authorities have economic development lending programs called “Bond Funds” that match fund loans, which can be underwritten based on TIF and special assessment revenues and other special district charges

# TIF Bonds in Ohio

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- ❑ School districts often receive all or a portion of the tax revenue they would otherwise have received out of the PILOT payments (Negotiated if the TIF is longer than 10 years or greater than a 75% exemption)
- ❑ TIF bonds may be issued on a taxable or tax exempt basis depending on Bond Counsel's analysis of use of proceeds, ownership of infrastructure, preferential rights and structure of the security for the bonds
- ❑ Revenue Bonds are typically non-recourse to the Port Authority and the municipality and do not count against the municipality's general obligation bond cap
- ❑ TIF bonds were frequently backed by security in addition to PILOT payments, including: minimum service payments by the developer and/or a special assessment (More to come)



# TIF Financing Today

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- ❑ Need additional credit/security sources, unless it is a TIF of a mature (built, operating and stabilized) development
- ❑ “No growth” increment projections may be required; and higher coverages (e.g. 125% and up)
- ❑ Consider “flipping” the old model, using TIF/ PILOTs as a backup revenue source, with other security as the primary source



# TIF Financing Today

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- Consider other tax relief
  - e.g. sales tax exemption on building components (see below)
  - e.g. income tax abatement or sales tax abatement (if possible)
  
- Consider public/private partnerships
  - Is there a potential private owner of infrastructure or quasi-public facilities?
  - Some REITs may like this structure; will lease facility back to political subdivision which can pay rent to REIT



# TIF Financing Today

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- Consider special legislative relief
  - e.g. isolated sales tax TIFs in Ohio (although not the rule)
  - e.g. isolated additional property tax exemptions



# TIF Financing Today

- Other credit/security sources examples
  - Minimum PILOT payments by Developer
  - Non-tax revenue pledge by municipality
  - Limited pledge of municipal/governmental credit, subject to annual appropriation
  - Federal programs (e.g. HUD 108 loans)
  - EB-5 (U.S. Citizenship and Immigration Services) investment program
    - e.g. Cleveland International Fund [\$500,000 minimum investment by foreign nationals aggregated as one source]
  - DOE alternative energy loan guarantee program (\$100 billion available)
  - Special assessments - common backup



# TIF Financing Today

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- Special assessment backup structure
  - Prior to 2008, Letters of Credit and municipal bond insurance were used - - now no such market resources exist
  - Levy special assessment in full project and bond amount
  - Reduce next annual assessment if full or partial projected PILOT payment made

# TIF Financing Today

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- Special assessment lien has first priority and not dependent on “increment”, i.e., not dependent on completion of vertical improvements
- Need careful underwriting, i.e., what is the existing real estate worth today and “how low” could it go?



# TIF Financing Today

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## □ Lien Enforcement Issues

- Probably need one or two year reserve fund
- Tax lien (TIF or special assessment) is leverage to get the attention of any holder of a commercial mortgage on the development
- Theory is that bank mortgage holder will pay the past due lien amounts to protect the status of the bigger commercial mortgage loan
- Need local official/tax assessor cooperation in state remedy enforcement procedures (e.g. potential foreclosure)



# THE REVENUE DILEMMA

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- ❑ The TIF financing is complete and...
- ❑ The public infrastructure improvements are in place.
- ❑ The debt service payment is due on the bonds or...
- ❑ The developer is requesting reimbursement.

**IS THERE ENOUGH MONEY  
IN THE TIF FUND?**



# THE REVENUE DILEMMA

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**IF THE  
ANSWER IS  
NO THERE  
ARE A FEW  
PLACES TO  
LOOK...**



# WHERE TO LOOK?

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## □ **Developer/Property Owner**

- Exemption application not filed
- Errors in exemption application – denied by State
- Delinquencies

## □ **Collection Agent**

- Timeliness in establishing TIF revenue collection system
- Errors in identifying TIF base and incremental value



# WHERE TO LOOK?

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## □ **Other Political Subdivisions**

- Statute may require distribution to assessing authority
- Revenues may be misdirected by Collection Agent
- Administrative or procedural errors may hold up payment

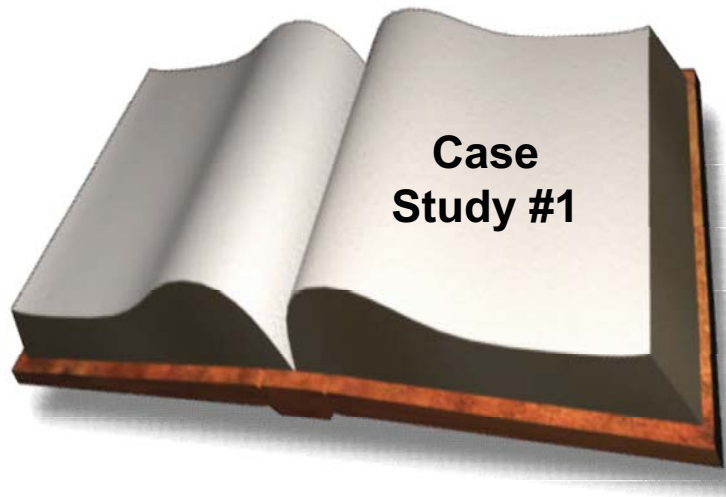
## □ **Bond Trustee**

- Unclear bond documents
- Flow of funds



# CASE STUDY

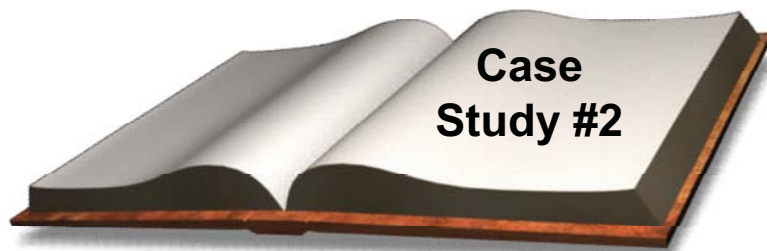
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- ❑ TIF legislation adopted in July 2003
- ❑ TIF Agreement states developer responsible for filing exemption application with State
- ❑ As of 2007 no TIF revenue collected
- ❑ Developer failed to file exemption application

# CASE STUDY

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- TIF legislation adopted in April 2005
- Exemption application filed by developer with State in August 2005
- As of 2007 no TIF revenue collected
- Exemption application denied by Department of Taxation due to “premature” filing

# TIF MONITORING

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- Prior to Creation
  - Analyze cash flows to verify developer's assumptions and determine project feasibility
  - Identify in the TIF agreement the party responsible for filing exemption application
  
- After the Creation
  - Confirm exemption applications are filed in a timely manner
  - Ensure proper records of TIF parcels are maintained and that PILOTs are distributed appropriately

# TIF Financing Examples

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## Project Financing for Queen City Square Tower

“The tallest building in Cincinnati, Ohio”



# QSC Public/Private Partnership

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- Participants: Western & Southern Financial Group, City of Cincinnati, Port of Greater Cincinnati Development Authority (one of those Ohio Port Authorities)
  - **City**
    - Approved the TIF
    - Provided \$3.75 million in grants
  
  - **Port Authority**
    - Owns the project
    - Leases the project to master lessee
    - Issues TIF-backed and Lease-backed bonds
  
  - **W&SFG**
    - Develops and manages the project
    - Provides funding



# QCS – Project Financing

Project Budget	
Land	\$22,000,000
Design	10,000,000
Construction	270,000,000
Financing	23,000,000
Other Costs	<u>15,000,000</u>
Total Project Costs	\$340,000,000



# QCS – Project Financing

Project Financing	
Lease-backed Bonds	\$225,000,000
Tax Increment Financing (TIF) Bonds	54,000,000
City Funds	3,750,000
Western & Southern Financial Group	<u>57,250,000</u>
Total Financing	\$340,000,000



# QCS – Project Financing

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- TIF bonds privately placed as alternative to developer reimbursement
  - \$54,000,000 in TIF bonds secured by PILOTs
  - Combined with \$10,000,000 of prior 2004 TIF bonds that financed, in part, adjacent building
  - Bonds bought by developer
  - Bonds may be speculative today, but not as stabilization is reached
  - With coverage and time bonds can be resold at a premium or even securitized



# Additional “Revenue” Source - - Sales Tax Savings

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- Used in Ohio to provide sales tax exemption on the building materials for a new structure owned by a governmental unit; developers call this savings “new equity”
- Port Authority enters into agreement with W&SFG as developer to be construction agent. Completed facility then leased to a master lessee who makes lease payments sufficient to cover debt service on the bonds that financed the facility
- The general resources of the Port Authority are not pledged to debt repayment and bondholders have recourse only to the lease payments made by the lessee or any guarantor or to the asset leased or financed



# Lease Bond Financing

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- ❑ Lease bond financings are heavily credit dependent and are typically, but not exclusively, used by investment grade entities
- ❑ Typically a bank group buys the lease bonds
- ❑ May offer the user financial, federal tax and accounting advantages, attractive purchase options and other incentives (synthetic leases)



# Lease Bond Financing

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- Lease financings fall into two main categories:
  - **Capital Lease:**
    - Lease rentals are sufficient to pay debt service on the financing undertaken to pay costs of the project
    - The lease is treated as a debt obligation of the lessee
    - At the end of the lease term, and upon retirement of the related financing, the lessee has an option to purchase the project for a nominal amount
    - Depending upon the restrictions of the lender, the lessee might have the ability to purchase the project upon retirement of the related financing

# Lease Bond Financing

- Lease financings fall into two main categories (cont.):
  - **Operating Lease:**
    - The lease is structured as a true lease for tax and for accounting purposes (FASB 13)
    - Typical lease term of twenty years or less with a significant unamortized balloon amount
    - Upon expiration of the lease, the lessee has the option to:
      - (i) renew the lease at a then current fair market rental, or
      - (ii) purchase the project for an amount equal to the then fair market value of the project, or
      - (iii) surrender its rights under the lease and vacate the project without having to pay the balloon amount.
- Both of the lease forms utilize triple net leases

# TIF Financing Examples - - The One Neighborhood Condominium Project

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## Project Overview

- ❑ New residential neighborhood located in the central business district in Columbus, Ohio
- ❑ The development comprises approximately nine city blocks and more than 300 residential units upon full build-out



# TIF Financing Examples - - The One Neighborhood Condominium Project

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## **Project Overview**

- ❑ 47 units of the development have been completed. An additional 13 units are under construction
- ❑ 47 of the 60 units are closed or are in contract as of the bond financing



# The One Neighborhood Condominium Project

## Project Financing Summary of Terms

<b>New Community Authority</b>	A New Community Authority has been established under Ohio law to facilitate the development of the One Neighborhood project. This is a new special financing district. The New Community Authority has levied a community development charge to generate revenues sufficient to fund bond debt service for the project (the Charge)
<b>The Bonds</b>	One Neighborhood New Community Authority Revenue Bonds, Series 2010 will fund, in part, Phase I project costs relating to the development of the One Neighborhood Condominium project
<b>Description of the Transaction</b>	The New Community Authority expects to issue the Bonds, described in greater detail below, to fund certain of the project costs. The transaction structure contemplates the purchase of the Bonds by the Columbus – Franklin County Finance Authority (the Finance Authority) which will then sell its Development Revenue Bonds (Central Ohio Regional Bond Fund) Series 2010A



# The One Neighborhood Condominium Project

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## Project Financing Summary of Terms (cont.)

<b>Description of the Finance Authority Common Bond Fund</b>	The Finance Authority Bond Fund, as previously described, is an economic development loan program with a common security interest in several Reserve Funds and the revenue designated to repay the various issues.
<b>Par Amount of the Bonds</b>	\$2,750,000
<b>Security and Sources of Payment for Financing Arrangements</b>	Proceeds of the Charge levied by the New Community Authority, representing a lien on real estate like a special assessment, will be deposited with the trustee for the New Community Authority Bonds. The New Community Authority agrees to levy the Charge at a rate of 25 mills



# The One Neighborhood Condominium Project

## Project Financing Summary of Terms (cont.)

<b>TIF</b>	<p>The City of Columbus approved legislation in September 2009 exempting the property from ad valorem property taxes and establishing PILOTs to be paid and assigned to the New Community Authority pursuant to a Tax Increment Financing and Cooperative Agreement between the City, the Developer, and the New Community Authority in conjunction with the issuance of the New Community Authority Bonds</p> <p>Together the Charge and the PILOTs constitute revenues as defined by financing documents (Revenues). Bondholders receive a first priority security interest lien in the Revenues</p> <p>A Primary Reserve Fund equal to the least of 10% of the par of the bonds will be funded. A Supplemental Reserve Fund equal to the difference between \$500,000 and the amount of the Primary Reserve Fund will additionally secure obligations related to the New Community Authority Bonds. The Supplemental Reserve Fund is subject to release upon meeting certain performance conditions</p> <p>The Developer and its principal individual owners will guaranty the bond payment obligations of the New Community Authority</p>
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# The One Neighborhood Condominium Project

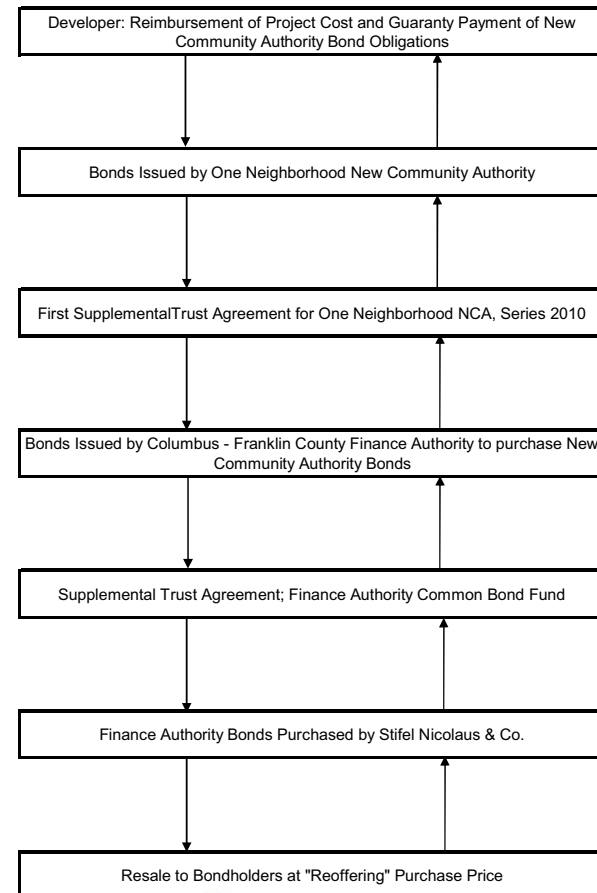
## Project Financing Summary of Terms (cont.)

<b>Use of Proceed</b>	<p>The proceeds of the bonds are expected to fund a portion of the public infrastructure costs as estimated below:</p> <table><tr><td>Landscaping, Trees and Shrubs, Fencing, Irrigation</td><td>\$ 400,000</td></tr><tr><td>Utility Relocations: Sanitary, Gas, Electric</td><td>1,000,000</td></tr><tr><td>Public Infrastructure, Right-of-Way, Inspection, Fees</td><td><u>670,000</u></td></tr><tr><td>Total</td><td>\$ 2,070,000</td></tr></table>	Landscaping, Trees and Shrubs, Fencing, Irrigation	\$ 400,000	Utility Relocations: Sanitary, Gas, Electric	1,000,000	Public Infrastructure, Right-of-Way, Inspection, Fees	<u>670,000</u>	Total	\$ 2,070,000
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# The One Neighborhood Condominium Project

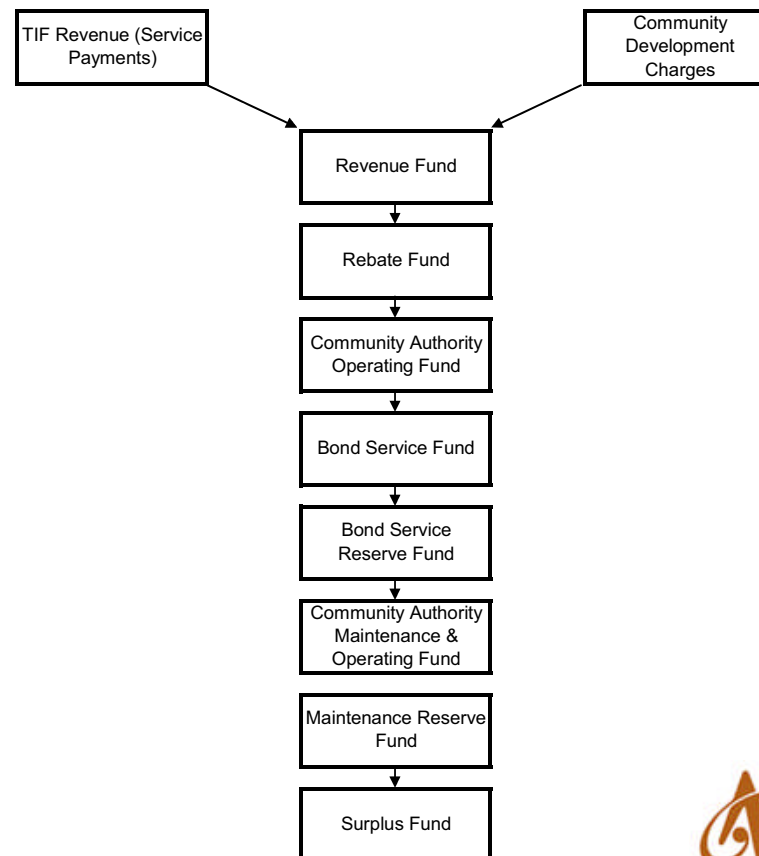
## Project Financing Flow of Funds

One Neighborhood New Community Authority Revenue Bonds/ Columbus – Franklin County Finance Authority Development Revenue Bonds, Series 2010



# The One Neighborhood Condominium Project

## Series 2010 Bonds Proposed Flow of Funds



# Questions?

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