

Understanding Tax Increment Finance: The Legal Basics

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Two Types of Economic Development Tools

Developer's taxes are abated:

- Renaissance Zones, MEGA, PA 198, PA 328

Developer's taxes are paid and captured:

- TIF: Use the future taxes from the development to pay for up-front development costs

With local government budgets under enormous stress, abating taxes is problematic. TIF is politically attractive.

TIF Statutes in Michigan

- **Downtown Development Authority Act (DDAs), 1975 PA 197**
- **Tax Increment Finance Authority Act (TIFAs), 1980 PA 450**
- **Local Development Financing Act (LDFAs, SmartZones), 1986 PA 281**
- **Brownfield Redevelopment Financing Act (BRAs), 1996 PA 381**

TIF Statutes in Michigan

- Historical Neighborhood TIFA Act, 2004 PA 530
- Corridor Improvement Authority Act (CIAs), 2005 PA 280
- Neighborhood Improvement Authority Act (NIAs), 2007 PA 61
- Water Resource Improvement Tax Increment Finance Authority Act (WRITIFAs), 2008 PA 94

What is a TIF entity's legal status?

- Statutes authorize creation by “municipalities,” generally cities, townships and villages (some exceptions)
- Separate legal entity
- Board members appointed by municipality governing body
- Included in municipality's budget

What is a TIF entity's legal status?

- Nature of the relationship
 - Parent municipality's power to say no
- TIF entity board's mission differs from legislative body's mission – can result in friction

TIF concept: Dedicate part of property tax revenues to improvements

- improvements bring growth
- more taxes for all
- “but for” development theory



Core Concept: “Captured Value”

- Initial Assessed Value (a/k/a Base Value) of property is set in the first year of Plan
 - Tax Day v. Final Equalization Day
- Each subsequent year: Current Assessed Value
- $\text{Current Assessed Value} - \text{Initial Assessed Value} = \text{Captured Value}$
- Captured Value is the *tax base*
 - Some statutes permit “sharing” of the CV, i.e., returning the tax base to the taxing entity
- $\text{Tax Increment Revenues (TIR)} = \text{Captured Value} \times \text{Applicable Millage Rates}$



“Captured Value” On What Property?

- Evolution of concept from “area” to “parcel”
 - Driver: reaction to revenue diversion
- DDA, TIFA: Development Area
 - Determine CV on the basis of aggregate difference between IAV and CAV
- LDFA: “Eligible property”
 - Collect TIR from development parcel (except sometimes)
- BRA: Eligible property (parcels)
- CIA: Back to “area,” but Plan opt-out

The Development Plan and TIF Plan

- Crucial legal document: Establishes legal basis to collect and spend TIR
- Procedural requirements complex
 - Varies by statute, but generally published notice, public hearing, opportunity for other taxing units to have input, 60-day “hold” period
 - Sometimes “opt-out,” sometimes not
- Differing degree of developer involvement
 - DDA, CIA Plans v. BRA Plan
- Anomalies abound
 - DDA: If 100+ residents: DA Citizens Council

Typical Procedure to Approve Plan

- Development Plan and TIF Plan drafted as single document
- TIF Entity adopts resolution approving combined Plan, sends to Municipality governing body for further proceedings
- TIF Entity notifies other taxing units of Plan fiscal implications
- Municipality governing body adopts resolution calling public hearing on Plan
- Publish notice of hearing, often twice – the first publication must be at least 20 days before hearing
- Post and mail notice of hearing (older statutes, e.g. DDA)
 - Certified mail to other taxing units
- Plan adopted by Municipality – resolution or ordinance
- Date of adoption of Plan is crucial to determination of IAV
 - Adopting a Plan by May 1 sets IAV at valuation as of *second* prior December 31; adopting a Plan on or after June 1 (approx) sets IAV at *immediately* prior December 31
 - Does it make a difference? Depends.

Limited Capture of School Taxes

- Since 1994, definition of “tax increment revenues” excludes revenues captured from the levy by the State, K-12 school districts and intermediate school districts.
- State can approve school capture on limited basis (BRAs)



Amending the Plan

- The TIF Plan should be amended with the Development Plan and should include updates to:
 - Maximum amount of bonded indebtedness to be incurred
 - Duration of the program
 - Estimated captured assessed value and tax increment revenues for the duration of the program
 - Estimated impact of the TIF Plan on taxing jurisdictions subject to capture in the Development Area
- Same procedures as initial Plan approval

Issuing TIF Bonds

- Each TIF statute contemplates pledging TIR as security for debt
- Market approaches TIF debt with caution – considered speculative
- TIF bonds generally not marketable without credit support
 - Parent municipality guaranty
 - Private credit enhancer (e.g., LC bank if available)
 - Sometimes developer guaranty if very strong
 - Combinations
- “Private use” issues for IRS present structuring challenges

What Can We Spend Money On?



- TIF statutes generally provide for spending money on capital improvements – bricks and mortar
- TIF bond proceeds generally limited to bricks and mortar
- Maintenance problematic
- Marketing and intangibles problematic, but some statutory relief, esp. DDA

Layering the Tools

City of Dearborn – 2009 Redevelopment of former Montgomery Wards site

- TIF capture: City of Dearborn BRA and East Dearborn DDA
- Developer tax credits: Brownfield MBT
- MEGA approval of school tax capture
- City of Dearborn BRA issues \$9.8MM tax-exempt and \$1MM taxable redevelopment bonds for parking structure
- Developer special assessment guaranty for additional credit support
- \$9.8MM bond issue designated “Recovery Zone Facilities Bonds” under ARRA
- ARRA designation received from Wayne County



The Legal Outlook for TIF

- Evolution of statutes driven by increasing tension over revenue “diversion”
 - 1975 language re not “circumvent existing property tax limitations”
 - Parcel limitations, school tax limitations, opt-out concept added in 1980s-1990s
 - Treasury “audit” late 1990s-early 2000s
- The “DDA Wars” with counties, municipal parents
- March 2010: Wayne County Prosecutor announces “review” of TIF capture and expenditures

Presenter: Michael McGee

Michael McGee, a Principal at Miller, Canfield, Paddock and Stone, P.L.C., has worked with Michigan communities since 1985. During this period he has helped create, expand, contract, and even dissolve dozens of tax increment authorities. Mike has worked on development/tax increment plans and has been bond counsel for over 75 tax increment bond issues. He also was bond counsel on the largest municipal bond issue in Michigan history, the \$1 billion bond issue for the McNamara Terminal at Detroit Metro Airport. He can be reached at (313) 496-7599 or mcgee@millercanfield.com

