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NJ's Version of Tax Increment Financing... RADs will Provide Municipalities with Another Tool to Encourage Redevelopment Projects

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An Introduction to RADs and TIFs. Faced with decreasing federal funds for redevelopment, New Jersey's local governments are continually searching for creative ways to attract new businesses, retain existing ones, and improve the overall economic climate of their communities. New Jersey's Revenue Allocation District Financing Act (the "Act") provides municipalities with an additional tool to encourage private development by using the incremental tax or other revenue generated by a development project to finance various related infrastructure and redevelopment costs. The Act states that Revenue Allocation Districts ("RAD") will "open new avenues of private investment ... and create favorable conditions for increases in economic activity, property values, employment opportunities and the provision of affordable housing." N.J.S.A 52:27D-460(d). RAD financings are New Jersey's version of tax increment financings, commonly referred to as TIFs. TIF financings involve the incurrence of debt which generally is repaid from the incremental property tax revenue generated by the financed project. TIFs first appeared in California in 1952. Today, every U.S. state, except Arizona, has enacted legislation authorizing TIFs. Although New Jersey has long had financing mechanisms in place to assist economic redevelopment, TIFs or RADs are a recent addition in New Jersey, with authorizing legislation having been approved in 2002. In February 2005, the rules and process (the "Rules") for approval of a municipality's RAD and financing plan were promulgated by the Department of Community Affairs' Local Finance Board (the "Board"). The Rules are significantly less burdensome than those first proposed in 2004 and, therefore, should make it easier for municipalities to undertake RAD financings.

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Current Examples of RAD Projects: Millville and Somerville. Millville in Cumberland County has gained approval of a RAD and plans to make infrastructure improvements including, water and sewer projects, housing rehabilitation and infrastructure improvements to a major retail shopping center. Millville has not yet issued bonds for this project. A private developer in Somerville is turning a strip mall into a new town center with apartments, restaurants, office space, retail, parking garage and recreation area with an indoor and outdoor pool. Somerville has begun the process for approval of RAD financing to pay for a new road, parking and other redevelopment project costs.

What is RAD financing and how can municipalities use this tool to finance redevelopment? RAD financing enables municipalities to promote private development by financing project costs of redevelopment, including street and utility infrastructure, land acquisition, construction of buildings, parking facilities and residential structures, and the payment of engineering and legal expenses and costs of bond issuance. Blighted or underutilized areas often cannot attract private capital or development. Private developers are deterred from investing in these areas due to the prohibitively high costs of repairing infrastructure and the uncertainty associated with underperforming economic conditions. Under the Act, certain redevelopment costs can be financed by a municipality through RADs if the Board determines among other things, that "the planned developments would not likely be accomplished by private enterprise without the creation of the District." N.J.S.A 52:27D-464(a).

The fundamental advantage of traditional RAD financing is that the municipality can finance redevelopment projects through the issuance of bonds, the debt service on which is paid solely by the increase in revenue realized from the redevelopment. Additionally, when the bonds have been paid off, the municipality will hopefully have a significant increase in tax revenue due to the broader tax base created by the economic revitalization of previously underutilized areas.

A municipality, by ordinance, must establish a "District," which is a defined area designated as a RAD. Once the municipality obtains Board approval in a multi-step process, it can issue bonds secured by tax increments and certain other amounts in the RAD to finance allowable project costs. The Act permits RAD bonds to be secured by "Eligible Revenues," which include the increased or "incremental" property taxes from the RAD due to the redevelopment's increase in the value of

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taxable property, payments in lieu of taxes ("PILOTS"), incremental revenues from payroll or wage taxes, incremental revenue from lease payments, parking taxes or revenue from parking facilities, and assessments permitted by law. While incremental property taxes are the most common source of security for TIF bonds, the Act's broad definition of "Eligible Revenues" provides a municipality with flexibility in designing its RAD financing plan. Municipalities will need to work closely with counsel and other professional advisors to determine, among other things, whether RAD bonds can be issued on a tax-exempt basis, and whether other financing options, such as general obligation bonds, which are a cheaper source of funds but may affect existing debt limits, make more sense.

The RAD Process. The Rules provide a three step process for Board approval of a RAD and RAD financing plan. 1) Application for approval to create RAD and Preliminary Revenue Allocation Plan: The local government ordinance establishing the District must contain a map designating the RAD and a certification that the total taxable property value in the RAD does not exceed 15% (20% if approved by the Board) of the total value of the taxable property assessed in the municipality. 2) Approval of Final Revenue Allocation Plan: Before pledging any revenues or issuing bonds, the municipality must adopt a final revenue allocation plan, which must detail changes from the preliminary plan and be approved by the Board. 3) Any bonds secured by Eligible Revenues from a RAD or otherwise guaranteed must receive Board approval prior to issuance. In addition to the preceding three steps, the Rules provide for an optional initial plan assessment which allows the municipality to work closely with the Board and other state agencies at the outset of the process to resolve issues and insure compliance with the various requirements of the Act and Rules.

Assuming Board approval is obtained, RAD financing creates a new source of funding at the local government level. While the RAD process is lengthy and complex, it is designed to assist municipalities in properly utilizing RAD financings and promoting development in accordance with the State's redevelopment and Smart Growth initiatives. Municipalities should work closely with the Board, legal counsel, engineers, financial advisors and other professionals once they commence consideration of a RAD project and financing. ■