STATE-FACILITATED TAX INCREMENT FINANCING FOR BROWNFIELDS REDEVELOPMENT

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Northeast-Midwest Institute was recently asked by [Smart Growth America] to produce a policy piece on "State-Facilitated Tax Increment Financing for Brownfields Redevelopment." The following is an excerpt from the forthcoming SGA publication. NEMW also updated our more comprehensive paper on [Using Tax Increment Financing for Brownfields Redevelopment]

Numerous brownfields projects, including high profile large-scale projects like Atlantic Station in Atlanta, have used tax increment financing (TIF) as the primary public incentive to leverage private investment. However, using a private bond market TIF for a brownfields project can be difficult. Investors want to minimize risk and uncertainty – two factors that characterize every brownfields project. The brownfields–TIF mismatch might be further described as follows:

- TIF bonds, in most cases, can be sold only when the "vertical development" (the buildings, as opposed to site improvements) is 100 percent assured. This means that the funds may come into the project too late to assist with the upfront brownfields-related expenditures. This timing problem is particularly difficult for local governments that are acquiring and cleaning up brownfields without a committed end user.
- Cleanup expenditures are sometimes not eligible uses of TIF proceeds. This limitation sometimes has to do with statutory authority – many states restrict the use of TIF proceeds to public infrastructure. But even in states where this is not the case, cleanup of private property may be interpreted as "private activity," in which case the TIF bond becomes taxable, meaning the terms will be less favorable and the bond will be harder to sell.
- The tax increments often are less than they should be for brownfields sites because the base property tax value usually does not reflect the impact of the contamination on the market value.

These are not insurmountable problems – many brownfields projects work with TIFs that only assist with the infrastructure and only provide funding when vertical development is ready to proceed. However, brownfields development could get a real boost if states designed their TIF authority and financing programs in order to facilitate the brownfields-TIF connection. A number of states have done exactly that. State-facilitated TIF for brownfields can be thought of as a three-step process:

1. Enabling legislation may need to modified to allow brownfields and site preparation costs;
2. Enabling legislation can also be modified to escalate the benefits or improve the terms, in effect increasing the attractiveness of brownfields (or other priority redevelopment) investments;

3. State financing mechanisms can be created or modified to complement and supplement local TIF funds.

1. TIF Enabling Legislation – Get the Basics to Work for Brownfields

First, for states that currently restrict use of TIF proceeds to public infrastructure, consider modifications to TIF-enabling legislation to allow site assessment, remediation, and site preparation as eligible activities. In 2007, Kentucky modified its enabling legislation to include environmental remediation as an eligible use of TIF proceeds.

Second, states should outline a simplified pay-as-you-go mechanism for brownfields cleanups. This mechanism usually does not require any special legislation; rather it is simply a guide for applying TIF to brownfields cleanups. Under a pay-as-you-go option, the developer (or the locality) invests upfront funds in cleanup (site assessments and other site preparation activities could be added, as well) and is paid back later from a pre-determined portion of the tax increment. This approach avoids the costs of going to the bond market, and tends to work well for sites where brownfields-related costs represent a major part of the project gap, as apposed to sites that have larger infrastructure needs and bond market borrowing is necessary.

2. Escalate Benefits for Brownfields and Other Priority Redevelopment Activities

States should consider ways of escalating TIF benefits for brownfields and other priority redevelopment projects. This is where a number of states stand out in modifying their statutes to, in effect, make brownfield investments more attractive.

Minnesota – Adjusting the TIF base for cleanup costs. Hazardous Substance Subdistricts permit the frozen tax value - or "base" value - in a subdistrict to be written down by the cost of cleanup, thus increasing the increment and potentially bringing greater subsidy levels into a deal.

Minnesota – Longer terms for priority redevelopment projects. Minnesota also provides another way to give preference to priority redevelopment activities: it varies the term of the TIF from 8 to 25 years with the 25-year terms reserved for projects that are addressing blight or producing low and moderate income housing. (See this chart.)

Wisconsin – more eligible activities and "0" base for publicly owned sites. In 1997, Wisconsin created the Environmental Remediation TIF (ER-TIF) program that represents a new twist on previous Wisconsin TIF authority, which was already one of the more permissive enabling statutes. Both ER-TID and traditional TIFs can be used for brownfields. The ER-TID has been tailored to brownfield projects in a several key ways:

- Acquisition and cancellation of delinquent property taxes are included as allowable expenses; remediation and demolition are also eligible under *both* TIF authorities;
- If the site is publicly owned, the base value may be calculated as zero; and
- ER-TIF projects are exempt from the value limitations that restrict a community's ability to use TIF for other projects.

New Jersey – Exceptions to Debt Limitations.. In 2002, New Jersey updated its TIF statute, giving a distinct advantage to state-designated "Redevelopment Areas" by allowing Redevelopment Area TIF districts to create debt that is not subject to the same debt limitations as other local bond issuances. Redevelopment Area bonds, rather than counting against municipal debt limitations, are allowed to use alternate sources of security, such as Payment in Lieu of Taxes and special assessment districts.

3. Create or Modify State Financing Mechanisms to Complement and Supplement Local TIF Funds

State loans (for pre-TIF upfront costs) and guarantees (to remove risk) can go a long way toward helping localities make TIF work for brownfield sites. Better still is the state committing some state tax revenues to the deal.

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Michigan - Brownfield Redevelopment Authorities and TIF-complementary financing programs. Michigan allows local units of government to establish a TIF district and capture the property tax increments to provide reimbursement for the costs of the eligible cleanup and site preparation activities. Local Brownfield Redevelopment Authorities (BRAs, the entities that govern the TIF plans) also may establish a Local Site Remediation Revolving Fund from surplus captured taxes in order to cover cleanup and site preparation at other designated properties in the BRA's jurisdiction.

Recognizing the mismatch between how the bond market works and how brownfields projects work, Michigan created three alternative financing programs, including Brownfields Redevelopment Grants (BRG) and two loan programs - Brownfields Redevelopment Loans (BRL - for cleanup) and Revitalization Revolving Loans (RRL - for demolition and site preparation). The two loan programs are designed to work with TIFs, as they feature flexible repayment terms, such as no payments due for the first five years and two percent interest rates. These terms are an ideal match with front-loaded, long-lead-time brownfields projects.

Connecticut - Converting the locality's TIF to an upfront grant for the developer and guaranteeing repayment. Connecticut's Brownfields Redevelopment Authority – Connecticut BRA - offers financing for brownfields remediation through its parent organization, the Connecticut Development Authority (CDA). CBRA deals are three-party transactions between CBRA, the developer, and the municipality, through the following steps:

1. The municipality pledges a portion of future incremental tax revenues towards the cost of the remediation of a specified site;
2. CBRA converts the city's pledge of future incremental revenues into an upfront cash grant to the developer; and
3. The pledged tax revenues repay the CBRA grant over a period of years. CBRA takes the risk for non-performance, in effect guaranteeing repayment.

The grant proceeds can be used for expenses directly related to demolition, as well as remediation, which includes asbestos and lead paint cleanup. The project can be located in any municipality (169) in Connecticut. CBRA acts as the conduit for the pledged monies, thereby taking the risk away from the municipality.

Pennsylvania - Tax Increment Financing Guarantee Program. Pennsylvania's TIF Guarantee Program is designed to assist local TIFs that qualify under a strict definition of blight removal. The state's guarantee, up to $5 million per project, can serve as an important credit enhancement that can make the difference between a feasible and an infeasible project. TIF proceeds may be used for infrastructure and environmental remediation costs. The state gives priority to brownfields sites as one of several program criteria. The program is funded to provide $100 million total in guarantees.

Kentucky and Mississippi - bringing state tax revenues to a deal. Most TIF projects work with local property taxes as the revenue stream, but for some projects that is not enough to cover a financing gap. If the state places a high priority on a particular public objective (job creation in distressed areas, for example), it can structure the TIF statute to offer an option of bringing certain state revenues into the mix if the project meets those criteria.

Kentucky's 2007 modification to the TIF statute potentially brings a host of state revenues (state real property taxes, sales taxes, individual and corporate income taxes, and limited liability entity taxes) into the mix if the project: 1) meets three of seven findings related to economic distress and blight; 2) exceeds $20 million investment; and 3) involves mixing uses with no more than 20 percent retail.

Mississippi designed a TIF vehicle to facilitate a single project: a 540-acre former chemical plant on the Mississippi River in Vicksburg, Mississippi. Under an agreement adopted under special legislation by the Mississippi state legislature, all state taxes (sales, income, and franchise taxes) will be rebated to the developer for ten years with a ceiling of 2½ times cleanup costs. With this financing in place, developer Silvertip Properties is proceeding with an $8 million cleanup, which is paving the way for a planned resort and casino. (See this article for more information)

State-facilitated Tax Increment Financing as a State Brownfields Strategy

From the state's point of view, gearing brownfields incentives to TIF has numerous advantages over the more common practice of doling out of direct grants and loans:

1. ***More money into deals*** **-** TIF financing, with a potential to capture taxes for as long as 30 years, can put more dollars into a deal than is typical of cash-strapped loan and grant programs. The result is that more sites and tougher sites can be redeveloped.
2. ***The perfect marriage of state and local commitment*** **-** State funds can be viewed as leveraging local funds, as well as private investment. The state's investment goes further – is more productive - under this arrangement. The state-supported TIF framework has automatic controls because localities are going to scrutinize a deal that involves foregoing taxes for many years.
3. ***Greater use of loans and guarantees/less use of grants*** **-** State funds can be mostly (or even exclusively) loans and guarantees rather than grants. Once a loan program is capitalized it will revolve and self-generate.
4. ***More proactive action by local government*** **-** The availability of state TIF-linked loan funds under favorable terms allows local governments to proactively acquire, cleanup, and redevelop mothballed and other difficult sites that have failed to attract private investment.