TAX INCREMENT FINANCING

WSACA FINANCE CONFERENCE

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INTRODUCTIONS

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PRESENTATION OVERVIEW

- Legislative History, Concerns, and Action
- Comparison to LIFT – Bothell Case Study
- Overview of Tax Increment Financing as enacted (HB 1189)
- Example Scenario of Tax Increment Financing
- Implementation Do's and Don'ts
- Question & Answer

LEGISLATIVE HISTORY, CONCERNS, ACTION

Previous efforts to authorize tax increment financing struck down by voters and the courts

- Washington State Constitution requires state property tax to be allocated to the common school fund.
- Legislature approved the Community Development Refinancing Act in 1982
  - Overturned for three reasons: 1) gifting of public funds and 2) uniform property tax rate 3) reduced funding to schools

Since then, the Legislature authorized several versions of "TIF lite" that utilized a credit against the state sales tax.

- Fell out of favor because these programs rely on investments from the state general fund
- Key legislators indicated TIF is a "handout to developers"

2021 Legislature approved HB 1189, authorizing tax increment financing.

- Constitutional, carefully crafted: school levy exempted, uniform property tax levies, funds used for public benefit

LIFT: BOTHELL CASE STUDY

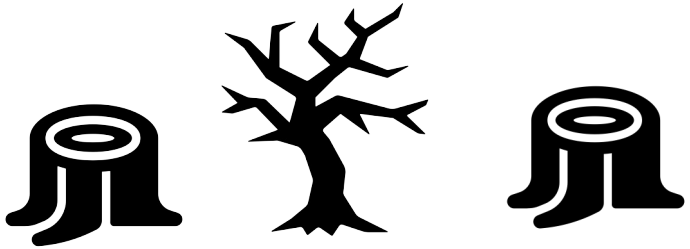
- Bothell's Downtown Revitalization: $150M of public infrastructure (included $48M of Facility Cost)
- LIFT (A.K.A.TIF lite) Enacted in 2006/Expires in 2044. Intent: Public Infrastructure Investment will attract private development. 9 Jurisdictions have been selected to receive excess tax revenue from State up to $1M per year for 25 years.
- Bothell received full amount of $1M per year (sales tax credit) to support some of its infrastructure investment in downtown.
- Economic Analysis in 2005 projected $650M of private investment over 25 year period within RDA as result of City's plan. Following first infrastructure projects and resulting private development, Bothell generated over $300M in additional private investment in first few years in RDA.
- Key early money critical to early success that allowed City to raise additional funds in support of it's infrastructure needs.

TIF FINANCING

Growth pays for Growth: Tax increment financing (TIF) is a method of allocating a portion of property taxes to finance public improvements in designated areas.

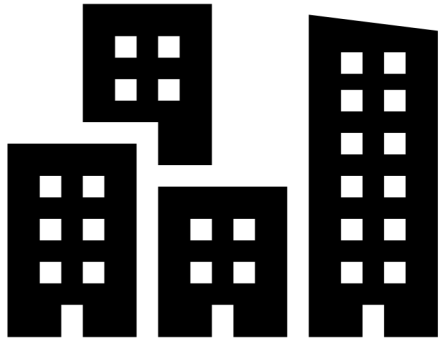
Parcel A: Undeveloped Site

Assessed valuation of $6 million
x 4.75 levy rate per $1,000 AV
= $28,500 in local property taxes paid



Parcel B: Developed Site

Assessed valuation of $121 million
x 4.75 levy rate per $1,000 AV
= $574,750 in local property taxes paid

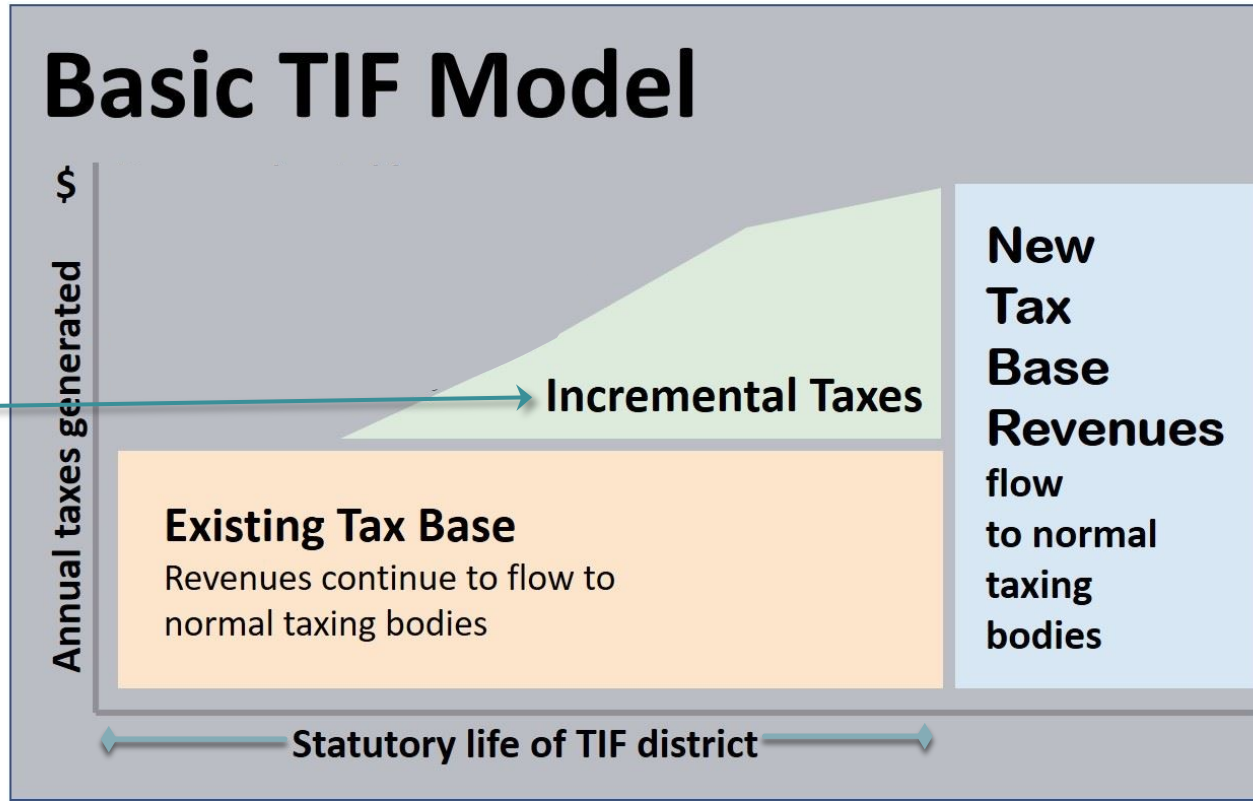


TIF FINANCING

Generally, TIF captures property taxes generated from the increased assessed valuation on the site that results from private development following infrastructure investment.

Revenues from **REGULAR** property taxes assessed against the **Increment Value** only, are captured:

- ✓ To pay "**public improvement costs**"
- ✓ To **repay bonds** issued for "public improvements"



OVERVIEW OF HB 1189: TAX INCREMENT FINANCING

- Available to cities, counties and ports
- Designed for a specific project/site where there is certainty that the infrastructure will result in development (not "build infrastructure, development will follow")
- **"But for" test:** private development would not otherwise occur within the reasonably foreseeable future but for an investment in infrastructure

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING

Eligible Infrastructure improvements owned by a local government within or outside of and serving the increment area that include:

- Street and road construction;
- Water and sewer system construction and improvements;
- Sidewalks and other non-motorized transportation improvements and streetlights;
- Parking, terminal, and dock facilities;
- Park and ride facilities or other transit facilities;
- Park and community facilities and recreational areas;
- Stormwater and drainage management systems;
- Electric, broadband, or rail service;
- Mitigation of brownfields; **or**

Eligible expenditures for any of the following purposes:

- Purchasing, rehabilitating, retrofitting for energy efficiency, and constructing housing for the purpose of creating or preserving long-term affordable housing;
- Purchasing, rehabilitating, retrofitting for energy efficiency, and constructing child care facilities serving children and youth that are low-income, homeless, or in foster care; Providing maintenance and security for the public improvements; or
- Historic preservation activities authorized under RCW 35.21.395.

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING, CONT.

- City, county, or port adopts an ordinance designating increment area, and identifying the public improvements to be financed, and whether bonds will be issued. Limitations:
  - No more than <u>two</u> active increment areas per sponsoring jurisdiction and they may not overlap
  - Increment areas may not total more than $200 million in assessed valuation, or more than 20% of the total assessed valuation of the sponsoring jurisdiction, whichever is less.
  - Cannot add additional public improvements or change the boundary of the increment area once adopted.
  - Must include a deadline by when construction of public improvements will begin.
  - The local government may only receive TIF revenues for the period of time necessary to pay the costs of the public improvements.
  - If the local government finances the public improvements, the increment area must be retired no more than 25 years after the adoption of the ordinance designating the increment area.

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING, CONT.

- Must prepare project analysis. Highlights:
  - A description of the expected private development within the increment area, including a comparison of scenarios with and without proposed public improvements.
  - An assessment of any impacts and necessary mitigation to address impacts on the following:
    - Affordable and low-income housing
    - Local business community
    - Local school districts
    - Local fire service
      - If 20% of the assessed valuation of fire district is within the increment level or there is an increase in level of service to increment area, must negotiate a mitigation plan.

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING, CONT.

Required Outreach:

- Hold two public briefings exclusively on the project
- Submit a project analysis to the state treasurer for review
- Publish notice in public newspaper
- Notice to county treasurer, county assessor, and governing body of each taxing district where the increment area is located

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING, CONT.

- Ordinance is adopted, effective June 2022. Increment funds distributed as early as calendar year 2023, likely later
- Each taxing district will collect levy + 1% + new construction + TIF growth
  - TIF growth = district's previous year's levy rate X growth in assessed valuation in increment area*
    - *TIF Growth excludes "new construction" in the IA – no "double dipping"!*
- New construction from within the increment area is added to each taxing district's levy when constructed.
- Applies to local property taxes <u>only</u>
- Limited to the amount needed to fund the public improvements outlined in ordinance
- Additional revenues not needed to repay bonds or pay other costs of the public improvements are then allocated back to the taxing districts in proportion to their regular tax levy rates.
  - Cannot be allocated back to the taxing districts if it would impair bond covenants. May want to think about appropriate length of financing, assumptions being made, etc.

IMPACT ON TAXING DISTRICT

- **When a TIF District is Created in the Taxing District:** Taxing district collects its budgeted amount (above) PLUS the levy rate applied to the increased assessed valuation in the TIF district (TIF growth). HB 1189 authorizes the taxing district to collect more money than they would otherwise be able to under law. The additional money they collect is remitted to the sponsoring jurisdiction to pay for infrastructure.
  - One of the reasons that the <u>but for</u> test is important is that IF the development would have occurred WITHOUT TIF, then using TIF is taking away potential future revenues from the taxing district.
  - New construction from within the increment area is added to the jurisdiction's overall levy.
  - The way the increased assessed valuation is calculated is compared to the base year; if the property's assessed valuation has increased significantly due to inflation, then there is an impact on the taxing district. Focus on <u>underdeveloped sites</u> and <u>construction starts within 5 years.</u>
- **Is the levy rate itself impacted?** The levy (including the TIF growth) is divided by the assessed valuation of the jurisdiction (including the increase in AV within the TIF area), that then determines the levy rate applied in and out of the increment area. The levy rate does not substantially increase/decrease because it is included on both ends of the equation.
- **When the levy amount is calculated the following year, TIF is not included (it does not carry over).**

OVERVIEW OF HB 1189: TAX INCREMENT FINANCING, CONT.

- Taxpayer Impacts:
  - The levy rate in the increment area and outside the increment area remain the same
  - Minimal impacts on taxpayers outside the taxing district.
- Developer Tax Impacts:
  - Pays the same levy rate as any other taxpayer.
  - Pays more (amount) because the assessed valuation of the site is increasing.

DEBT ISSUANCE AND HB 1189 TAX INCREMENT FINANCING

- **General Obligation Bonds** *(this is the primary method of leveraging the tax allocation revenues)*
  - WILL create an "indebtedness" that counts against Issuer's debt capacity (% of Assessed Value *as of the date issued*)
    - There is no State backstop and no guarantee that there will be any increase in the increment value!
      - Issuer must repay the debt, regardless of whether tax increment revenues are generated within the Increment Area
      - Issuer's full faith and credit and general revenues will be on the hook
      - Important to understand the financial impact if the private development in the area does not occur

  - **What about Revenue Bonds?** *(Authorized...But not expected to be widely used.)*
    - **NOT "tax allocation revenue bonds" -** Must be payable solely from the revenue generated by the public facility
    - **Only** available to finance public improvements that consist of a "**revenue-generating public facility**" that:
      - is located in the increment area, and
      - the local government is otherwise authorized to operate.

DEBT ISSUANCE AND HB 1189 TAX INCREMENT FINANCING

- **Local Government Policy Considerations**
  - **What level of risk can the Local Government tolerate?**
    - What happens if the private development does not materialize? How good are the projections provided by the promoters?
  - **What level of debt service can be supported?**
    - Will need good modeling of expected TIF tax allocation revenues (and other revenues that you intend to use for repayment of debt) to determine the shape and structure of the debt
      - What are realistic projections about tax allocation revenues & increment value? What level is supportable?
      - Level vs. increasing over time? What is the "cost" for pushing out debt service?
  - **Over what time period?**
    - Keep the repayment period short? vs. When will sufficient tax revenues be generated?
    - Conservative structuring – Remember that these will most likely be general obligations!
      - Make sure your projections about TIF tax allocation revenues are realistic and not excessively rosy
      - Consider building in a buffer – Structure bonds to be retired *earlier* than maximum duration of TIF district
      - Consider other flexible call provisions to allow early call as revenues permit?

DEBT ISSUANCE AND HB 1189 TAX INCREMENT FINANCING

- **Considerations for working with project promoters**
  - Do you (and they) have a clear understanding of project risk? And risk to the local government if the project does not materialize?
    - Do you have a clear picture of their other sources of funding and the risks related to those funds?
  - What types of forecasts and projections do you have/need?
    - Who will prepare? (Are the project promoters the only ones providing these projections? Does the City have its own internal projections? What about outside consultants?)
- **Timing considerations**
  - Maximum life of Increment Area = 25 years
    - Apportionment begins in calendar year AFTER passage of the ordinance creating the increment area – then clock begins to tick!
    - Can apply to pay some costs as you go, as long as they are "direct costs of public improvements" until you are ready to issue debt, but cannot go more than the 25 years; good idea to get your debt issuance lined up as early as possible in coordination with timing of passing the formation ordinance
  - And finally….Make sure your Bond Counsel is involved in the early stages of planning the TIF project.

PROJECT ANALYSIS REVIEW BY OFFICE OF THE STATE TREASURER

- **Sponsoring jurisdiction must:**
  - Submit a Project Analysis to the Office of the State Treasurer (OST) for review
  - Provide such additional information as may be requested by OST
    - If providing projections, be prepared to describe assumptions and methodology that went into those projections
  - Consider any comments that OST may provide
- **OST must:**
  - Complete the review within 90 days of receipt of the project analysis and may consult with other agencies and outside experts as necessary.
  - Upon completing their review, promptly provide to the sponsoring jurisdiction any comments regarding suggested revisions or enhancements to the project analysis based on the statutory requirements.

PROJECT ANALYSIS REVIEW BY OFFICE OF THE STATE TREASURER

- **What is in the Project Analysis?**
  - Statement of sponsoring jurisdiction's objectives for the designated increment area and any property intended to be acquired by the sponsoring jurisdiction
  - Boundaries and duration of the increment area
  - Description of the expected private development, including a comparison of scenarios with and without the proposed public improvements
  - Description of the public improvements, estimated public improvement costs, and the estimated amount of bonds or other obligations expected to be issued
  - Total certified assessed value of real property within the increment area and an estimate of the increment value and tax allocation revenues expected *[this is a required part of the project analysis and may require more formal projections to show the estimates over time]*
  - Estimate of the job creation reasonably expected to result from the public improvements and the private development
  - An assessment of any impacts and any necessary mitigation on the following:
    - Affordable and low-income housing
    - Local business community
    - Local school districts
    - Local fire service

DEVELOPMENT SCENARIO

- City X wants to create new mixed-use development based on adopted community vision/plan. New or replacement infrastructure is needed to support desired development. Current lease rates for commercial and residential development are close but are not currently sufficient to support new construction costs.

TIF ANALYSIS | DEVELOPMENT PRO FORMA

- City X prepares project analysis if desired development can occur with/without tax increment support. City X determines that a significant barrier to the proposed development is the cost of the infrastructure and without funds to pay for the infrastructure, the private sector would not be able to accomplish the City's envisioned development. The infrastructure cost is estimated at $10M.

BUT FOR TEST - EXAMPLE

Projects should demonstrate a need for a TIF area by satisfying at least one test within each category below:

Initial Tests

- ❑ **Lack of Growth and/or History of Development**
- ❑ **Unusual/Additional Development Expenses**

Secondary Tests

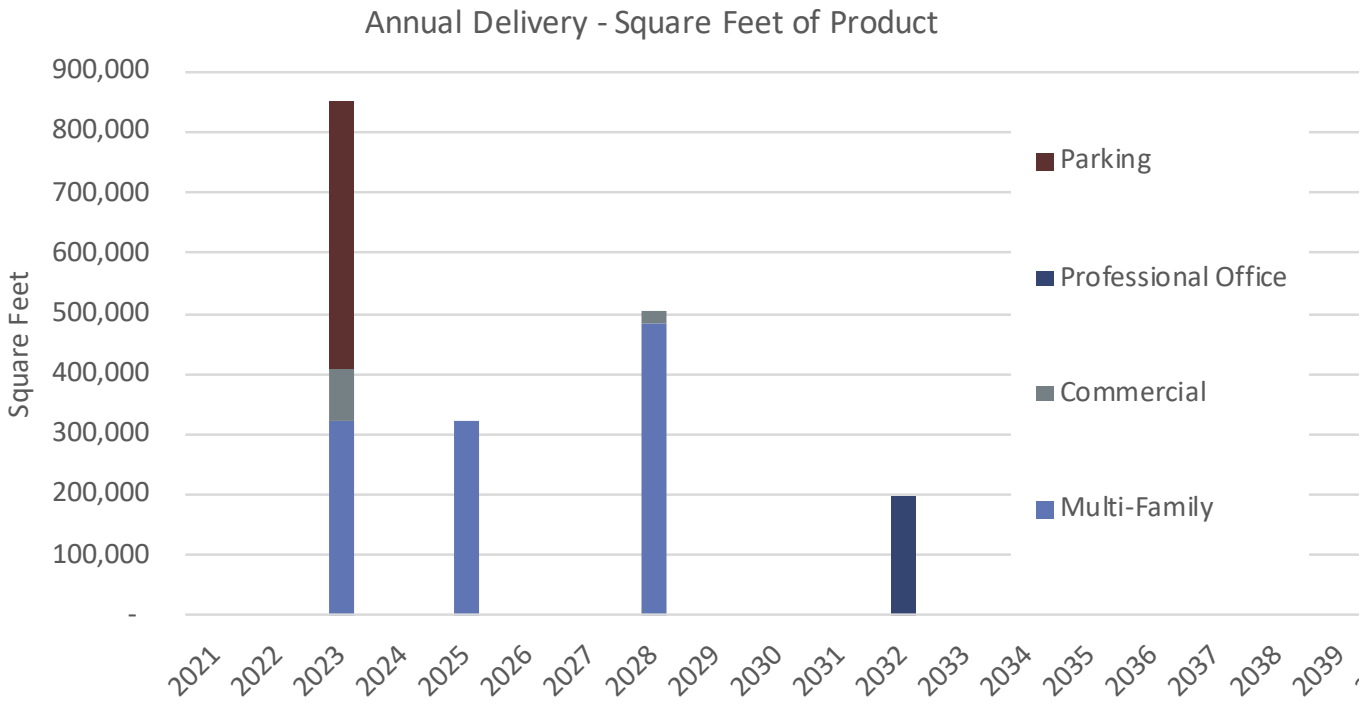
- ❑ **Market/Gap Analysis**
- ❑ **Developer Commitment**

DEVELOPMENT PLAN

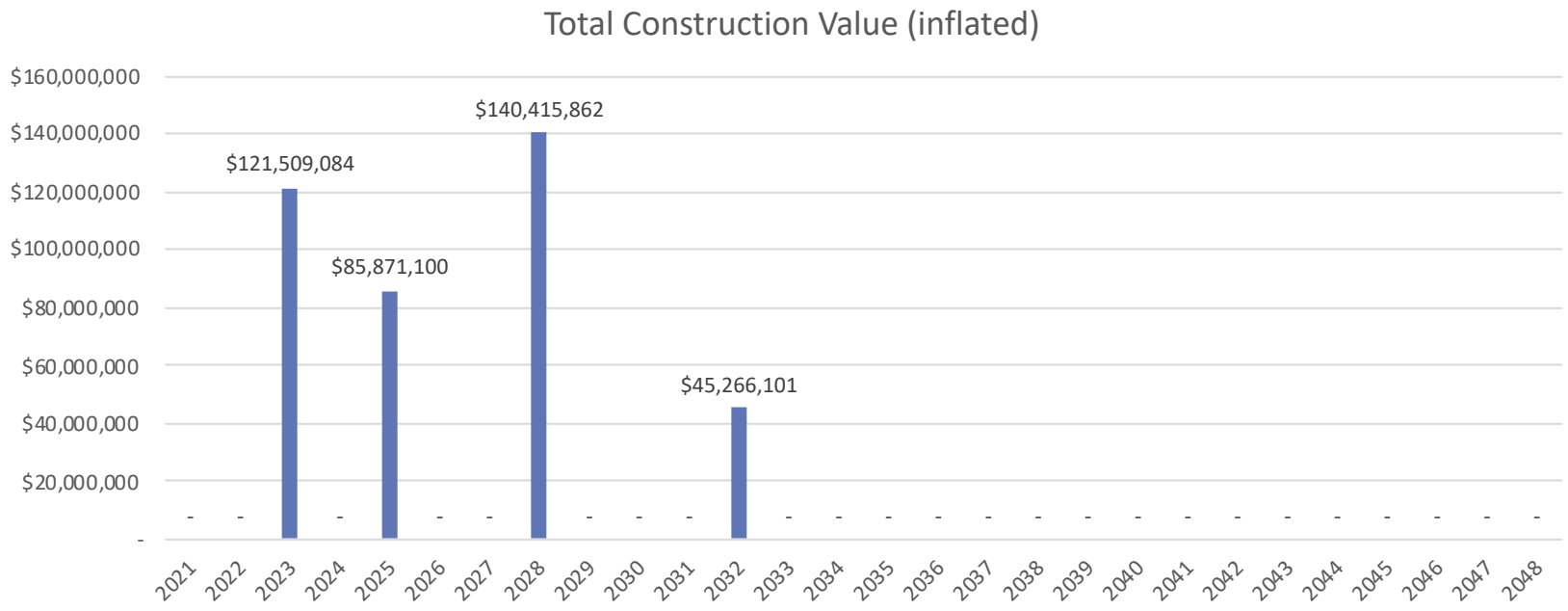
Construction timing

- 1st Phase
  - 2023: 400 units of multi-family (assumed to be podium with stick built over)
  - 2023: 1,500 parking spaces (assumes some blended structured and surface parking)
  - 2023: 85,000 sqft of retail space
  - 2025: 380 units of multi-family (assumed to be podium with stick built over)
- 2nd Phase
  - 2028: 600 units of multi-family (assumed to be podium with stick built over)
  - 2028: 20,000 sqft of retail space
- 3rd & Final Phase
  - 2032: 200,000 sqft of office/entertainment space

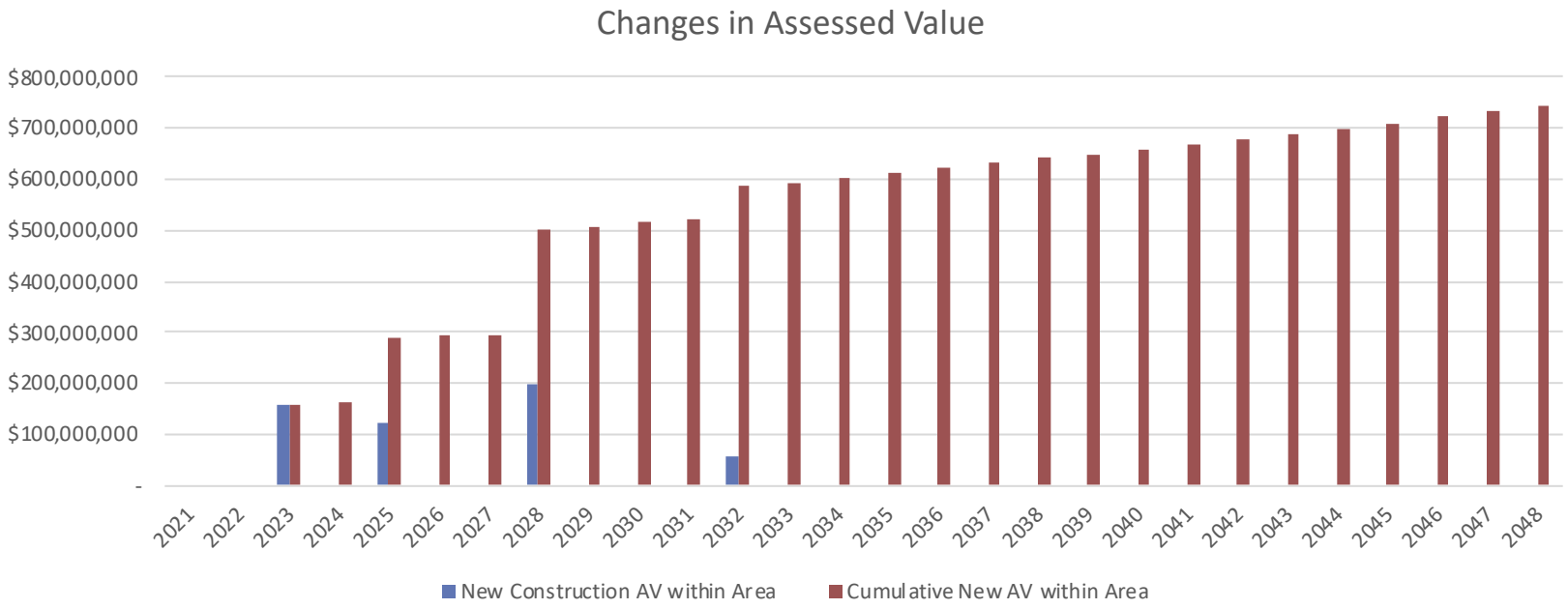
DEVELOPMENT SCHEDULE



CONSTRUCTION VALUE | DEVELOPMENT PLAN ($393M)



CHANGES IN ASSESSED VALUATION



EXAMPLE: TIF REVENUES WITHIN INCREMENT AREA: $121M OF INCREASED AV IN 2024

City of X	.9139
Y County	.9849
Fire District	.9518
Transit	.1971
Port	.1732
Library District	.4362
PUD	.1002

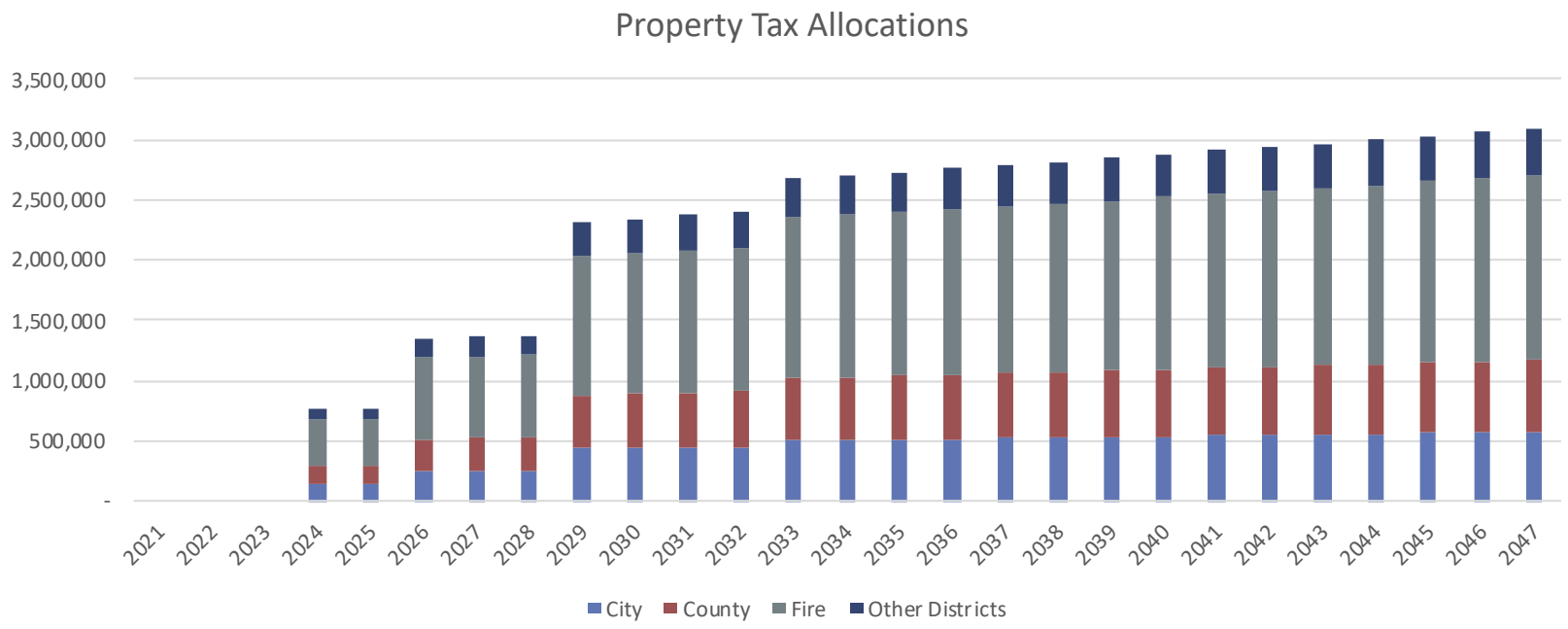
EXCLUDE voter-approved school district levies

EXCLUDE state property tax levy

Total 4.75 Levy Rate
X
$121 million
÷
$1000

$574,750

ALL DEVELOPMENT PHASES OVER 25 YEARS



TOTAL PROPERTY TAX ALLOCATIONS | 25 YR PRESENT VALUE

Tax Entity	TIF Revenues
City of X	$ 7,400,000.00
Y County	$ 7,570,000.00
Fire District	$ 19,630,000.00
Transit	$ 1,730,000.00
Port	$ 1,520,000.00
Library District	$ 380,000.00
PUD	$ 880,000.00
TOTAL	$ 39,110,000.00

ADDITIONAL TAX REVENUES

- Sales Tax
- Utility Tax
- Other

IMPLEMENTATION DO'S AND DON'T'S

- Carefully examine projected TIF's revenues; you will be responsible for any debt issued regardless of development success.
- Follow the letter and spirit of the law.
- Make realistic projections about ability to attract private development with TIF.
- Recognize that future criticism is likely to suggest that private development could have occurred without TIF and back up your findings with market data. How we manage future TIF projects will likely shape future legislation; positive and negative.
- Identify early any possible impacts to affordable housing, business community, schools, fire and work to mitigate.
- Early outreach to special purpose districts, community outreach, etc. beyond what statute requires
- TIF will likely not be the answer to all your infrastructure needs of a project but can create an important revenue stream.

QUESTIONS?

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