Revisiting TIF

It's not working the way we were told it would.

by THOMAS HELLER

Lisa Barnum, graphic design

Research published previously in this journal found Indiana's tax-increment finance (TIF) mechanism worked in a curious way, one at variance with its central concept.[1]

That concept, the "hold-harmless" assurance, maintains that local government bodies will not lose any of their existing tax base when a TIF is established. At the same time, they are unable to share in any new, incremental tax revenue produced by subsequent private investment within the TIF area.

The article found the hold-harmless assurance to be hollow. The convoluted mathematics of TIF under Indiana law disguised substantial erosion of local government's pre-TIF tax base. This is the same base that is "frozen," if you believe the downtown Indianapolis law firms that market TIFs to local governments across the state.

That erosion translates into budgetary challenges and higher property-tax rates for cities, counties, schools, townships and libraries as it eats away at their pre-TIF tax base.

Meanwhile, through a series of opaque steps, the TIF mechanism harvests for itself what its math erodes from others, burdening local taxpayers with making up for the tax base and revenue lost by county and city government, schools and libraries. TIF, as practiced in Indiana, is a "heads I win, tails you lose" situation.

A False Aura of Success

This follow-on paper identifies two factors that together reveal as hollow the claims of TIF success. They expose as false that: a) TIF never erodes the pre-TIF tax base for local taxing jurisdictions; and b) it is an essential tool to stimulate economic development and attract new business investment.

A sobering example of how TIF has not worked as we were told it would is the experience of Bartholomew County since 2005. That was when the City of Columbus formed a Redevelopment Commission to establish and oversee the city's three TIFs. The subsequent history illustrates how TIF, twisted and torqued from its central principle, has functioned as a money-harvesting device for an appointed board that is largely independent of elected local government bodies.

Since its TIF district was established, the Woodside Industrial Park in Columbus has seen little new business investment. Yet, that TIF produces over $2.5 million annually for redevelopment coffers.

The "success" of the Woodside TIF lies in redirecting money eroded from the pre-TIF tax base, money that had benefited the county, the city, the schools, library and township. Woodside's tax base eroded by two-thirds since its TIF was created.

The earlier article found that in the first seven years of the three Columbus TIF districts, the supposedly frozen pre-TIF tax base declined by 43 percent. The Woodside TIF showed the greatest decline.

This erosion from tax base of the three TIFs has directly benefited the TIF incremental Assessed Value (AV), the "captured increment." That now is a pot holding $220 million in AV and producing $6 million revenue annually, money exclusively for the local redevelopment commission.

Meanwhile, local property tax rates increased by 28 percent. The county's tax rate alone rose 39 percent.

Down to 'Bare Metal'

The reality of this erosion is obscured by the complexity of TIF's accounting. Although the earlier article found clear evidence that erosion was happening in TIF districts all across Indiana, the pathways by which the erosion of pre-TIF tax base was accomplished were not specifically tracked.

This effort takes that work a step further by going down to bare metal in order to pinpoint the specific ways that tax bases in Columbus and in all likelihood many other Indiana communities have been compromised.

While this research is informed by the experience of Columbus in the period since TIF districts were initiated there a decade ago, a caveat is called for: The data requirements of going to such depth are too great for one individual to conduct parallel examination of TIFs elsewhere.

So for those who may wish to unravel the convoluted and complex numbers game that TIF apparently has become in Indiana, this paper may offer a roadmap.

Let's start by stipulating the following three outcomes of TIF accounting in Indiana (whether intended or coincidental is beyond the scope of this research):

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1. *Unearned TIF income* is credited to local redevelopment commissions, providing them with a false signal of success.

2. *Local budgetary challenges* and higher property-tax rates become necessary to make up for a tax base eroded into TIF's "captured increment."

3. *A market* is created for hyped development schemes that rely on TIF financing, including TIF-backed debt.

Woodside Industrial Park

Now let's look in detail at one Columbus industrial park. Platted in the late 1970s, Woodside Industrial Park was developed in three waves during the 1980s and 1990s when Japanese firms and related automotive-industry supply firms located there. Approximately a quarter billion dollars of plant investment occurred there from 1989 through 2004. *(See Chart 1 on the following page.)*

But the park wasn't established as a TIF district until early 2005. And unfortunately, the Great Recession soon washed across the American economic landscape and construction of new facilities slowed markedly.

Nonetheless, the Woodside industrial TIF district from its formation displayed an impressive rise in "Captured Increment" and corresponding TIF revenues. In fact, the industrial park now produces about $2.5 million annually for deposit into the redevelopment commission account.

Understand that this does not owe to any success in attracting significant new industrial investment. There were only $21 million in construction permits issued to a sample of 20 parcels in Woodside since the advent of its TIF. *(See Chart 1 on the following page.)* This sample covers 87 percent of the Woodside TIF's taxable property.

All of which begs a question: Given Woodside's inability to replicate its success in the 1980s and 1990s in attracting new industrial development, how is it possible that its TIF can produce millions of dollars annually for the Columbus Redevelopment Commission?

The answer lies with a "but for." That is jargon trotted out by economic-development champions whenever they advocate forming a TIF — as in *"but for* this proposed TIF, there is no prospect for market-based investment that could bring new jobs, new income and higher property values."

Ironically, the "but for" associated with the Woodside TIF is that the TIF district would not be able to pump millions a year into redevelopment bank accounts *but for* the existence of two curiosities in TIF accounting — secrets, if you will.

The first relates to the expiration of property-tax abatements granted to attract investment prior to creation of the TIF. The second relates to "contested assessments" claimed in the TIF's annual filings with the state Department of Local Government Finance (DLGF).

A Wrecking Ball for Local Government

When they were drawn in 2005, the boundaries of three TIFs in Columbus, Indiana, encompassed nearly one-sixth (16 percent) of the city's gross tax base and a tenth (10 percent) of the county's tax base. Although these TIFs were adopted with the assurance that these TIFs would harvest their property taxes only from the value of new development that happens within their boundaries, little new development followed. Yet magically these TIFs produce a quite handsome revenue stream ($6 million annually) for redevelopment bank accounts, whose uncommitted cash balance now exceeds $12 million.

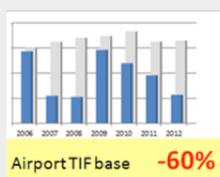
How did these TIFs make a silk purse out of a sow's ear? The answer lies in the convoluted, curious math of TIF. This follow-on to an earlier paper ("Indiana's Wobbly TIF Law," *Indiana Policy Review*, Summer 2013) reveals that TIF's bounteous annual revenue comes mostly from eroding pre-TIF tax base — something proponents assured would not happen. In just their first seven years, the base assessed valuation of these three TIFs in Columbus was eroded by almost half (see charts below). The erosion shifted it instead to benefit the TIF.

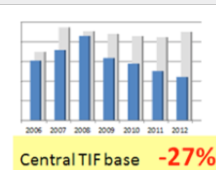
This paper finds base erosion is a key source of TIF "success" and produces substantial money for local redevelopment bank accounts. The erosion traces more to middlemen fudging the numbers than to any magical ability of TIFs to stimulate economic performance. This paper's findings amplify Kessler's political economy insight that public initiatives designed to benefit only a few attract intense interest by those few – and are fiercely defended by those few. Meanwhile, initiatives assured to have no downside lull the public into somnolescent if not eager acceptance.

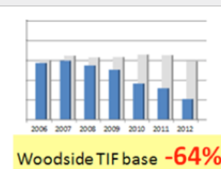
TIFs neatly fit both categories: they bestow gain upon a few at the same time they're marketed as benign. The behind-the-scenes mechanics of TIF reveal a surprisingly powerful ability to manufacture money without much visible economic development. But TIF's money-making power relies upon sleight-of-hand similar to a Three-Card Monty game on the street corner.

TIF's "no cost" assurance is hollow. Local budgetary challenges and higher taxes unavoidably result. So, too, developer interests obtain an out-sized influence on local elections. Candidates wishing to appear responsive to their community's perceived shortcomings quickly fall in line, embracing the "visions" those interests bring to local media.

TIF instead should be understood as a bank created by local government, a bank susceptible to manipulation by an eco-devo infrastructure of well-heeled legal professionals and favor-seeking developers. Because it is controlled by a political body and its money is insulated from market forces, it's not surprising that TIF's lending standard is as suspect as its economic performance. By the stream of revenue they capture, TIFs appear to be successful. But that financial performance disguises unremarkable underlying economic performance. And because a TIF stealthily drains away so much tax base, its downstream effects on both taxpayers and local government finances are significant, lasting and oh so very real. *—tah*



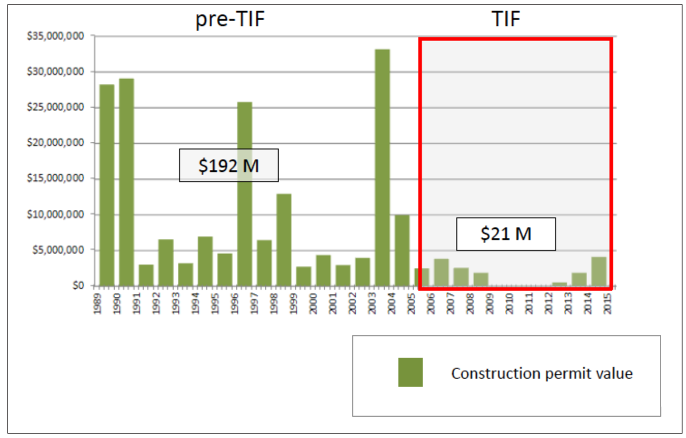




The promoters of tax-increment financing claim a tax base that they do nothing to earn or produce. They send a false signal misdirecting local economic-development strategy.

Secret No. 1: Capture of Previously Granted Abatements

Chart 1: Development Activity (Woodside Industrial Park, 1989-present)



Either through confusion or intent, the math of Indiana's TIF mechanism enables the Woodside TIF district to capture — when existing property-tax abatements rollback into taxable status — the increase in taxable assessed value of facilities constructed in years prior to formation of the TIF. This is referred to here as "reach-back" because those abatements a) preceded creation of the TIF and b) were not granted by its redevelopment commission.

This lassoed $32 million in added AV for the Woodside TIF. That represents tax base that arguably should belong to local taxing districts who surrender, with each abatement granted, several years of property-tax receipts.

Reach-back produces $500,000 additional revenue annually for the local redevelopment commission account. It is likely this same reach-back phenomenon is at work in TIFs elsewhere in Indiana.

What is the statutory authority behind reach-back accounting? Prior to 2013, the interplay between abatements and TIF had not been clearly addressed in state statute. But when concerns arose in late 2012 about substantial TIF base erosion, the DLGF approached the Legislature and, with other parties, sought to explicitly codify this "existing practice." The 2013 Legislature accommodated the DLGF request.[2]

In the case of Woodside, the TIF now receives two-thirds of the property taxes paid from an industrial park developed prior to the formation of the TIF. (This reach-back feature may set our state's TIF mechanism apart from any other with tax-increment financing.)

The Columbus Redevelopment Commission is the sole beneficiary of the return of abated property to the local tax rolls. Thus, Woodside's TIF receives credit for business investments made well before the TIF was formed — investments made in no small part because of generous property-tax abatements offered by local communities.

To summarize, the promoters of tax-increment financing lay claim to a tax base that they do nothing to earn or produce. This sends a false signal misdirecting local economic-development strategy.

Secret No. 2: Exploitive "Contested Assessments"

There is another curiosity in TIF accounting that also drains tax base from local taxing jurisdictions. It is called "contested assessments."*

For the Woodside TIF, a total of $66 million in "contested assessments" were entered in the TIF's annual filings to the DLGF, an amount representing about half the TIF's initial base AV. *(See Chart 2 on following page.)*

The math in the DLGF annual filing works to flow this $66 million of "contested assessments" directly out of the base and into the increment, pumping an extra $1.7 million annually into the Columbus redevelopment bank account.

These "contested assessments," because of their scale, played a pernicious role in pumping ever more of Woodside TIF's base AV — and thus annual property taxes — away from local taxing districts and to the favor of the redevelopment commission.

In 2010 alone, a $36,576,800 figure** was entered as "contested assessments" for

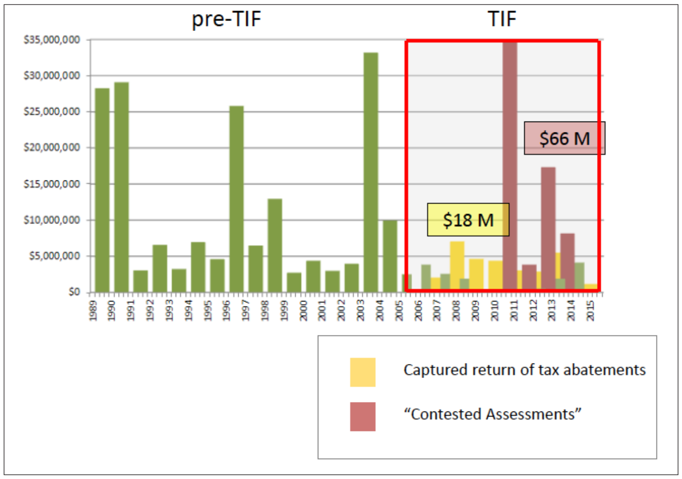
** I employ air quotes around "contested assessments" because I cannot rule out the possibility that these figures were simply paper entries like phony deductions claimed on a tax return. I was unable to obtain any substantiation for this category entered for four straight years into the annual TIF neutralization form filed with the DLGF. Nor was I able to discern subsequent assessment changes in the Woodside TIF district's properties consistent with such large "contested assessment" figures.*

***This is not the largest amount of "contested assessments" found by the author. The Greencastle Economic Development Area's TIF showed a $52.6-million "contested assessments" figure in its 2012 filing.*

the properties within the Woodside TIF. (The Bartholomew County assessor assures me he has no knowledge of this beyond what I've informed him was uncovered in the DLGF filing.)

Whereas abatement reach-back was codified into statutory language in 2013, "contested assessments" remain in legal limbo, existing without clear statutory authority. But the DLGF's recently revised TIF filing form still retains a line for this very adjustment, enabling continued use of what is an accounting trick or worse.

Chart 2: Woodside Abatement Capture and "Contested Assessments"



To summarize, these two secrets generate $2.2 million in additional revenue annually for the Columbus local redevelopment bank account, almost 90 percent of Woodside's total TIF contribution. In turn, affected local taxing jurisdictions suffered the loss of several tens of millions of AV from their tax bases. This is a permanent loss; TIF math does not allow it to be restored.

A Million Here, a Million There . . .

The power of the two accounting devices to pump unearned money into local TIF redevelopment accounts is astonishing. Table 1 presents the before-and-after picture of nine years of the Woodside TIF for that 20-parcel sample.

While the taxable value of real property for these parcels increased by only $8.7 million, their base AV suffered a whopping $74-million decline. That decline traces principally to "contested assessments" totaling $66 million.

These "contested assessments" swapped out huge amounts of base AV and pumped it into the TIF mechanism. The captured increment of this TIF sample has skyrocketed to $82.9 million in nine short years. There is no indication in the county's property-tax records that the claimed "contested assessments" did anything except enrich the TIF's bank account.

The Woodside example provides an illustration of the unreported but nonetheless real effect of these two TIF accounting secrets. One industrial parcel, developed in the late 1980s and with no building permits issued since 1994, shows 44 percent of its annual tax bill paid into the TIF's coffers. And that's on the low end; its neighbors on average pay 65 percent to TIF, and a handful of them pay over 90 percent.

What did TIF produce to earn this money? The answer is a single $10-million parking garage more than seven miles away in the renovated downtown district of Columbus — a garage that serves a half dozen new downtown restaurants, their evening diners and "perhaps one day" theater goers.

The TIF-financed garage also serves Cummins, Inc., a Fortune 200 company long headquartered in Columbus. The company, with a need to recruit and retain a talented young workforce — talent that otherwise could be lost to bigger, hipper cities — also benefits from the city's more vibrant downtown scene.

But truth be told, the downtown's rejuvenation is only part of a sleight-of-hand that creates the illusion of TIF economic-development success. For it is a stretch to claim that a $10-million parking garage can attract over $220 million in development that in turn produces $6 million annually in TIF revenue.

Again, in the case of the Woodside TIF, the vast majority of its money comes from "subsequent new development" that didn't really happen. Thanks to TIF accounting secrets, the success of a previous era is being claimed by this TIF. And even then, a turbo boost from "contested assessments" was thought necessary to make the TIF appear successful.

Conclusion

The "we'll-freeze-the-base-and-keep-only-what-we-produce" assurance appears to be commonly violated — at least as TIF has been practiced in Indiana. But the dark side of this financing system isn't confined to accounting trickery.

One industrial parcel developed in the late 1980s — with no building permits issued since 1994 — now pays 44 percent of its annual tax bill into the TIF district's coffers. And that's on the low end.

Analysis by the Ball State University Center for Business and Economic Research found virtually no beneficial result from tax-increment financing in terms of standard metrics of local economic performance, *e.g.,* added jobs, higher incomes, enlarged property-tax base.

Table 1: The "Before and After" Picture of Nine Years of the Woodside TIF

Reconciliation of components,
TIF accounting for 20 industrial properties
over nine years inside Woodside TIF district
($ in millions)

(properties represent 88% of TIF's total taxable AV)

	Total Taxable AV	TIF Assignment: Base	TIF Assignment: Captured Increment
Starting taxable AV (2005p2006)	118.7	118.7	0.0
Abatement adjustment:			
return, abated AV to taxable status	18.6	0.0	+18.6
Other adjustments , net:			63% erosion
1. addition of New development 2. reassessment* of existing development 3. loss of AV (demolition, change in tax status)	-9.9	-74.2	+64.3
Ending taxable AV (2014p2015)	127.4	44.5	82.9

* "contested assessments" totaled $66 million for allocation area in these years

data sources: DLGF annual TIF filings and Bartholomew County assessment records

Little or no connection exists between the public investment ("local public improvements" in statutory language) and the cornucopia of money TIF now bestows upon local redevelopment bodies and the passel of camp-followers they attract.

The $600 million a year in TIF revenues currently collected statewide implies that over $20 billion in new private, taxable development was created by strategic local public improvements (*e.g.,* the Columbus parking garage) undertaken by quasi-governmental redevelopment commissions.

But isn't it reasonable to expect that $20 billion in new private investment would make a detectable economic ripple? It hasn't.

Recent analysis by the Ball State University Center for Business and Economic Research found virtually no beneficial result from tax-increment financing in terms of standard metrics of local economic performance, *e.g.,* added jobs, higher incomes, enlarged property-tax base.[3]

The explanation may be that some large piece of that supposed follow-on economic development didn't really happen. That is, the supposed economic growth might be only borrowed from an earlier era, or it might be that the money pumped into tax-increment financing was an illusion created by "contested assessments."

In any case, the temptation to profit at the expense of others is strong. Joan Youngman of the Lincoln Institute astutely cautions that "a municipality may have an incentive to draw the boundaries of the TIF district as widely as possible, including development that may be unrelated to the TIF investment."[4] It is likely that not even a scholar like Youngman, however, could have foreseen how far afield TIF's temptation could go.

Was the public aware of these TIF secrets? Almost surely not, but a skeptic might ask whether the secrets indeed were known, albeit closely guarded, by the legal, eco-devo and architectural-engineering consultants who make up the cottage industry TIF has fostered in Indiana.

Twenty-two amendments to Indiana's TIF law since 1987 stand as testimony to the extraordinary influence this group has at the Statehouse. When it comes to economic development and TIF, justice and good government appear only hurdles to overcome.

Endnotes

1. Tom Heller. "Indiana's Wobbly TIF Law,." *Indiana Policy Review.* Summer 2013, pp. 2-7: http://www.pageturnpro.com/Indiana-Policy-Review-Foundation/52989-Fall-2013/index.html#1

2. HEA 1116; PL 218-2013, Sec. 16.

3. Michael Hicks, Dagney Faulk, Pam Guirin. "Some Economic Effects of Tax Increment Financing in Indiana." *Policy Brief.* Ball State University Center for Business and Economic Research, Jan. 28, 2015.

4. Joan Youngman,."TIF at a Turning Point." *State Tax Notes,* May 2, 2011.