

Labor Education Program White Paper | December, 2011

Tax Increment Financing and Chicago Public Schools: A New Approach to Comprehending a Complex Relationship

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I. INTRODUCTION

For the past three decades, tax increment financing (TIF) has been the primary public financing tool used by the City of Chicago to spur local economic development. During this time period, TIF advocates and opponents alike have attempted to understand TIF's impact on taxing jurisdictions that overlap TIF district boundaries. Interested parties have raised important questions. How much, if any, has the price of this economic growth been paid for by local schools and other taxing districts? How has the use of TIF in Chicago impacted taxpayers on the whole, both locally and throughout the state?

The modern-day debate in Chicago has focused on TIF's impact on schools and is shaped by two competing arguments: TIF districts "take" money away from Chicago Public Schools and contrarily, TIF has had no or limited financial impact on the school district. Opponents claim that in 2009, TIF diverted approximately \$250 million away from Chicago schools. This reproach of TIF resonates with much of the public given the current budget crises confronting the school district and the City of Chicago. Schools in Illinois are highly dependent on the collection of property taxes for revenue generation, and Chicago schools face a \$700 million budget shortfall for the 2011-2012 school year.

The local controversy over TIF stems from both the undemocratic nature of the processes that govern its usage as well as from the perceived negative fiscal impact it has on taxing bodies that overlap TIF boundaries. Readers interested in learning more about the issues surrounding TIF governance should consult the reform proposals presented by Mayor Emmanuel and his TIF Task Force, which include recommendations for improving TIF accountability and transparency.¹ While this paper addresses the latter issue, it principally seeks to navigate the competing arguments that describe TIF's impact on Chicago's largest taxing body, Chicago Public School District 299 (CPS).

1 TIF Reform Panel, "Findings and Recommendations for Reforming the Use of Tax Increment Financing in Chicago: Creating Greater Efficiency, Transparency and Accountability." August 23, 2011.

A central dynamic that we explore is the distinction between TIF's impact on CPS' available tax base and its annual revenue. A number of often conflicting variables come into play when trying to fully understand these two issues. While some of these variables are known and relatively simple to quantify, others are abstract and extremely challenging to measure. An example of a known and calculable variable that affects TIF's relationship with CPS revenue is the use of intergovernmental agreements to transfer TIF funds for capital improvements within the school district. An extremely difficult variable to explain is the question of whether property development in TIF districts would have occurred in the absence of TIF. The "but for" question – would development have occurred "but for" TIF - is central to the debate of TIF efficacy, but calculation of the counterfactual is limited by assumptions.

In placing these conflicting interpretations side by side, this "white" paper attempts to create an alternative narrative that is developed from an honest and informed discussion of the complexities surrounding this topic. We examine the arguments on each side of the debate and the relevant issues that influence these questions. Our ultimate goal is for interested and affected parties to better understand the multifaceted relationship TIF holds with CPS so that sustainable solutions for financing school budgets can be constructively discussed.

In this spirit, after a brief presentation of the mechanics and expansion of TIF, the fourth section will address the variables that account for contrasting narratives for TIF impacts on school funding. Section five follows with a brief presentation of a short list of ways in which other municipalities and states that employ TIF are able to counteract some of the perceived negative impacts TIF causes for overlapping taxing jurisdictions. This list of "best practices" outlines some policy fixes that could inform the public debate on how to reform TIF usage in Chicago. The paper closes with three recommendations for analyzing the interaction between use of TIF and local school financing.

II. TIF MECHANICS

Tax Increment Financing, or TIF, is an economic development tool used by cities to economically revitalize blighted areas by attracting new investment that will increase property values.² A municipality can use TIF to generate money for economic development in a specific geographic area, known as a TIF district. TIF districts enable a city to reinvest all “new” property tax revenue growth in the area in which they were generated. The tool is intended to spur development or redevelopment activity that would not have occurred “but for” the public incentives offered. In Illinois, the use of TIF funds is restricted to three purposes: (1) to remediate blight; (2) to prevent an area from deteriorating into a blighted situation; or (3) to foster industrial development.

In Illinois, a TIF district is authorized for a period of up to twenty-three years, with the possibility of renewal for an additional twelve years.³ At the time of designation of a TIF district, the then-current Equalized Assessed Value (EAV) of all property is measured by the Cook County Assessor’s Office and established as a baseline, which is often referred to as the “frozen” EAV.⁴ During a TIF district’s duration, no tax revenue created from increases in property values are allocated to overlapping taxing bodies such as Cook County, Chicago Public Schools, or the Chicago Park District. These jurisdictions are however able to continue to collect taxes on the base level of EAV within TIF districts during its 23-year lifespan. Tax revenues from the growth in EAV over the baseline amount, also known as the “increment,” are used to fund redevelopment costs within the TIF district boundaries. Funds can also be transferred (i.e., “ported”) from a TIF district to be invested in an adjoining area. After dissolution of a TIF district, the increment is added to the tax base and is made accessible to all overlapping taxing bodies.

² Illinois Tax Increment Allocation Financing Act of 1977, 65 ILCS 5/11-74.4

³ The lifespan of a TIF district typically lasts over 20 years.

⁴ Equalized Assessed Value or EAV is the assessed value of a property multiplied by the state-certified equalization factor, resulting in the value from which the tax rate is calculated after deducting homestead exemptions, if applicable. Tax bills are calculated by multiplying the EAV by the tax rate.

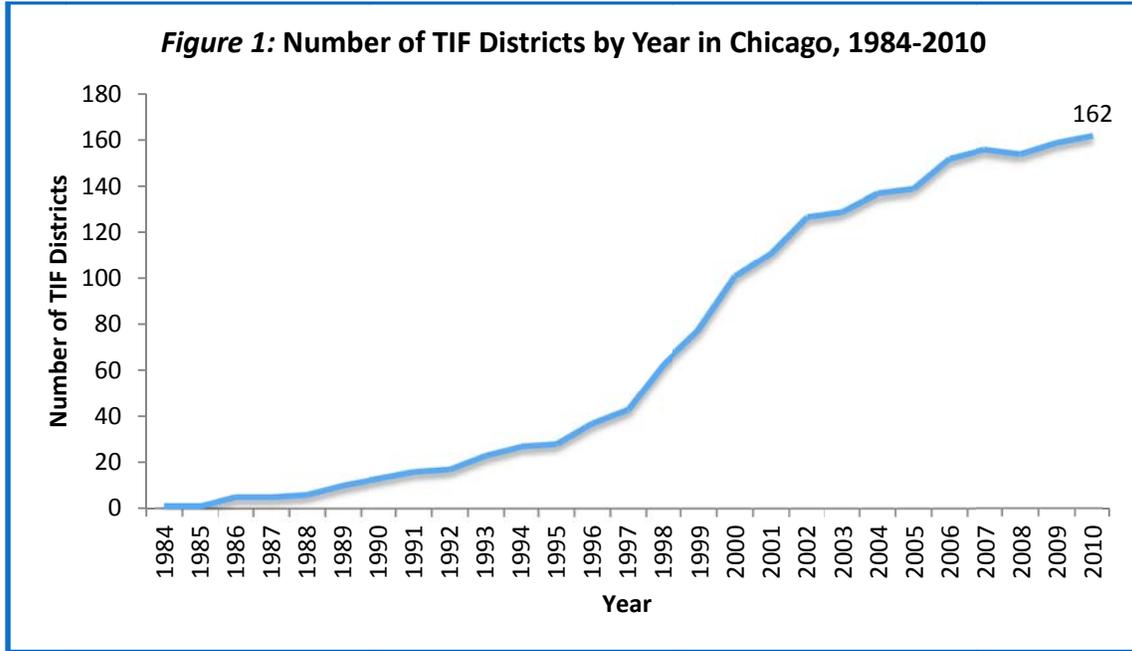
III. TIF EXPANSION

In the second half of the 20th century, many cities throughout the United States suffered losses of manufacturing jobs and corresponding declines in population. Decreased local tax bases were accompanied by reduced federal funding for urban renewal. This combination forced cities to look for more creative ways to finance redevelopment projects (Weber, Bhatta, & Merriman, 2003). The first wave of economic development practices employed by local governments were designed specifically to attract new businesses and included tools such as subsidized loans or direct payments to firms for relocation expenses, tax reductions, subsidies applied to the cost of plant facilities or utilities, and costly industrial recruitment programs. A second wave of strategies shifted focus to firm retention and expansion and made use of indirect forms of corporate assistance like increasing investment capital, developing business incubators, and providing technical assistance for business growth or expansion. Development tools used with second wave programs have historically included revolving loan funds, below-market loans, and enterprise zones.

Cities adopting second wave strategies have been characterized by a strong investment and entrepreneurial approach (Clarke & Gaile, 1992), and have increasingly embraced policies that focus on “sustained, strategic alliances with private businesses” (Weber, 2003). Entrepreneurial programs include tools such as equity participation in redevelopment projects, venture capital funds, and use of TIF. Such strategies “endow local governments with a tremendous amount of city-shaping capacity” (Weber, 2003), with TIF serving as “one of the most powerful tools that municipal governments have for fostering and facilitating market-driven urban renewal” (Jolin, Legenza, & McDermott, 1998).

California first used TIF in 1952, though real momentum for TIF usage nationally did not arise until the mid-1980s. Over time, TIF’s original use as a tool in blight reduction has shifted towards its use for general economic development purposes (Byrne, 2009). TIF is now authorized in 49 states and the District of Columbia and is one of the most widely used local government programs for financing economic development in the United States. Former Chicago Mayor Richard M. Daley proclaimed TIF “the only game in town” and his city’s “only tool” for promoting economic development (Nolan & Berlin, 2002). As can be seen in *Figure 1*, TIF usage in Chicago expanded considerably in the late 1990s

and early 2000s. At the current time, approximately 10% of Chicago’s EAV base is located in TIF districts, and TIF districts cover roughly 30% of the city’s area (TIF Reform Panel, 2011).



Source: City of Chicago, Department of Housing and Economic Development

IV. DUELING NARRATIVES

Two competing narratives have arisen to complicate the understanding of how TIF affects the level of school funding in Chicago. The question both narratives claim to answer is “Does TIF take money away from schools or does TIF have no or only limited fiscal impact on CPS?” Each perspective relies on examining (1) the growth in TIF usage in Chicago (2), the way in which tax extensions are calculated (3), and how CPS compensates for revenue shortfalls with other funding sources.⁵ A substantial portion of CPS’ annual budget is derived from property tax collection, and TIF is funded through growth in property tax values in areas subject to CPS tax extensions. TIF critics summarily claim that these tax revenues are being diverted from schools to subsidize private development.⁶ Proponents dismiss claims of lost revenue due to TIF by arguing that schools compensate losses through other funding mechanisms such as state aid and question whether CPS would have received additional revenue without TIF.

The following sections explore the different ways in which TIF impacts CPS funding by separately discussing the erosion of the city tax base and the erosion of available revenues. If we conceptualize this debate by placing the two narratives of TIF impact as extremes on either end of a linear spectrum, we can see the ways in which each of the relevant variables shift the effect in one direction or another. As we introduce new variables, we will discuss how they add to the argument that TIF “takes” money away from the schools or mitigate TIF’s overall fiscal impact.

⁵ A tax extension is both: 1) the process in which the county clerk determines the tax rate needed to raise the revenue (levy) certified by each taxing district in the county; and 2) the actual dollar amount billed to property owners in a taxing district.

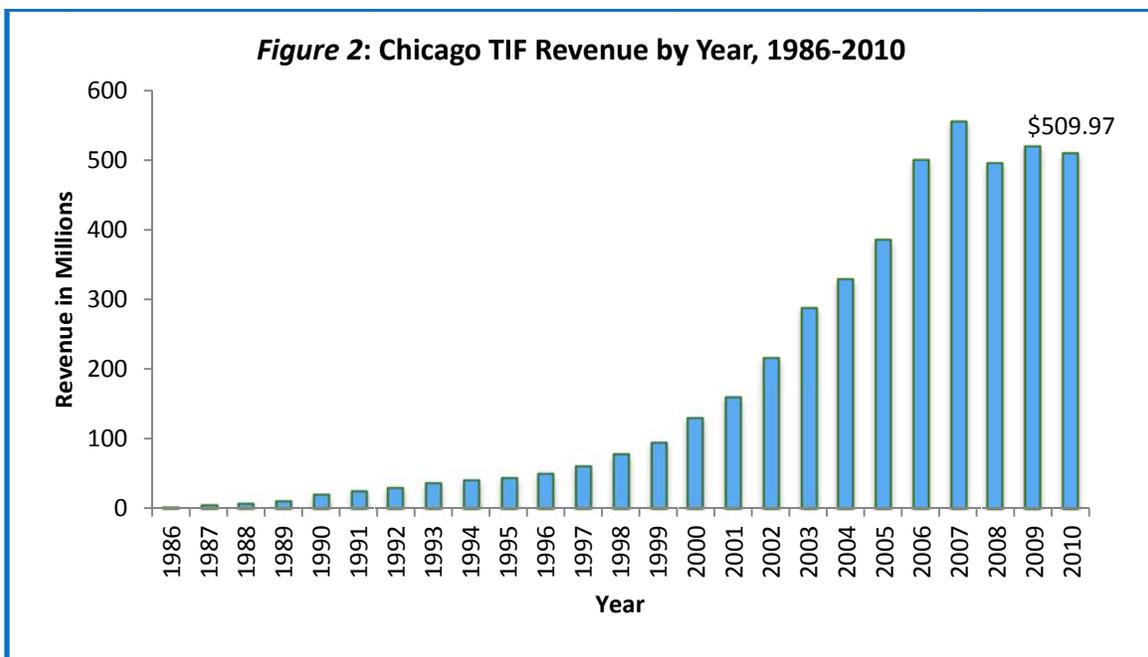
⁶ The TIF Panel Report found that 47% of TIF-funded development, or \$1.7 billion, was allocated to public works projects in the form of improvements to schools, parks, streets, and public buildings.

EROSION OF THE TAX BASE AND TIF

The question of how TIF impacts CPS' ability to increase its taxable base is distinct from whether CPS loses revenue due to TIF. The issues that come into play when exploring the erosion of CPS' tax base are: (1) the amount of incremental property tax revenue that is collected in TIF funds; (2) the interaction between growth in EAV and tax caps; (3) the impact of inflation on the "frozen" EAV baselines; and (4) the political challenges inherent with raising tax rates.

A. Incremental Property Tax Revenue in TIF Districts

Since 1986, nearly \$4.6 billion has been collected from all TIF districts throughout the City of Chicago (Orr, 2011). TIF districts will collect approximately \$510 million for the 2010 tax year, roughly a 2% decrease from the almost \$520 million generated the previous year. *Figure 2* shows TIF revenue growth from 1986 to 2010 in Chicago.



Source: Office of Cook County Clerk David Orr

In 2010, taxing districts maintained a total tax rate of 4.931 %. CPS' rate equaled roughly 50% of this amount, or 2.581 %. The argument that TIF "takes" money away from schools is based on the application of this tax rate to TIF revenue. All other limitations aside, if CPS was able to extend its extension to property value growth within TIF districts, it should have collected an additional roughly \$267 million in property tax revenue in 2010. *Table 1* demonstrates the cumulative impact of application of CPS tax rates on historic TIF revenue amounts.

Table 1: Application of CPS tax rates to Chicago TIF district revenues, 1995-2010

FY	TIF Revenue Totals	CPS Levy	Total Levy	CPS Share of Levy	Hypothetical Extension
1995	\$ 43,968,797.00	4.251	9.345	0.454895666	\$ 20,001,215.20
1996	\$ 50,090,002.00	4.327	9.453	0.457738284	\$ 22,928,111.57
1997	\$ 60,756,489.00	4.084	8.843	0.461834219	\$ 28,059,425.66
1998	\$ 77,215,944.00	4.172	8.872	0.470243463	\$ 36,310,292.87
1999	\$ 93,702,895.00	4.104	8.536	0.480787254	\$ 45,051,157.58
2000	\$ 129,302,548.36	3.714	7.788	0.476887519	\$ 61,662,771.52
2001	\$ 159,088,851.42	3.744	7.692	0.486739470	\$ 77,434,823.16
2002	\$ 216,609,284.50	3.562	7.277	0.489487426	\$ 106,027,521.15
2003	\$ 287,454,306.36	3.142	6.433	0.488419089	\$ 140,398,170.46
2004	\$ 328,700,220.63	3.104	6.280	0.494267516	\$ 162,465,841.53
2005	\$ 386,502,771.48	3.026	5.981	0.505935462	\$ 195,545,458.37
2006	\$ 500,369,348.17	2.697	5.302	0.508675971	\$ 254,525,864.20
2007	\$ 555,310,568.29	2.583	4.994	0.517220665	\$ 287,218,101.30
2008	\$ 495,590,381.02	2.472	4.816	0.513289037	\$ 254,381,109.19
2009	\$ 519,715,715.20	2.366	4.627	0.511346445	\$ 265,754,783.26
2010	\$ 509,971,274.25	2.581	4.931	0.523423241	\$ 266,930,817.04
TOTAL					\$ 2,224,695,464.07

There are three major assumptions inherent in the argument that TIF “takes” money away from schools: (1) all of the additional revenue would not have been limited by any tax cap; (2) the increase in property values experienced within TIF districts would have occurred without use of TIF; and (3) CPS was not able to compensate for lost revenues with use of other sources. All of these variables are discussed in greater detail below. If we conceptualize the issue of how much money TIF annually diverts from CPS along a spectrum, we could place \$267 million on one polar extreme (*Figure 3*). The other polar extreme would be \$0, signifying that CPS is not losing any revenue to TIF.



Figure 3: Two polar extremes illustrating the amount of revenue CPS annually “loses” to TIF

B. Interaction between CPS’ Extension and the Tax Cap

The first assumption listed above depends on the absence of any law restricting CPS’s access to potential additional revenue. However, the Property Tax Extension Limitation Law (PTELL), commonly referred to as the “tax cap,” limits the annual growth of a non-home rule jurisdiction’s tax extension to the lesser of 5% or the growth in the Consumer Price Index (CPI).⁷ While under Illinois law, “home rule” governments are not limited by property tax rate limits or tax caps, non- “home rule” jurisdictions such as CPS are subject to these extension limitations.

⁷ Although PTELL is commonly referred to as a “tax cap,” use of this phrase is misleading as the law neither “caps” individual property bills or individual property assessments. Rather, PTELL allows taxing districts to receive limited inflationary increases in tax extensions on existing properties, plus additional amounts for items considered “outside” of the cap including new construction and voter-approved limitation increases. PTELL is designed to slow the growth of property tax revenues to taxing districts when property values and assessments are increasing faster than the rate of inflation, providing property owners with some protection from tax bills that increase only because the market value of their property is rising rapidly. For more information about PTELL and the local property tax cycle, see PTAX-1004, *The Illinois Property Tax System*, available on the website of the Illinois Department of Revenue, www.Iltax.com.

An argument for a minimalist TIF impact on schools stresses that because tax caps limit the amount of property tax revenues that non-home rule taxing bodies can receive annually, property tax revenues are insensitive to increases in EAV. In other words, CPS cannot “lose” revenues to TIF because tax capped non-home rule jurisdictions cannot access increases in value of existing property within TIF districts (The Civic Federation, 2007). If we add the interaction with the tax cap to our TIF impact spectrum and make no allowance for the value of exemptions to the law, we observe a shift towards the left (*Figure 4*).

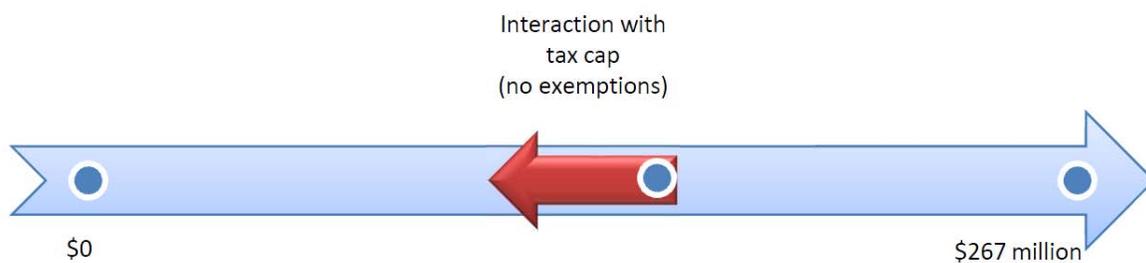


Figure 4: Spectrum illustrating the directional pull of CPS’ annual revenue loss to TIF with inclusion of the tax cap and no allowance for the exemption of increased property values attributed to new construction.

A counter argument for a more robust TIF impact looks at the exception PTELL provides for some property considered “outside” of the tax cap. This exception concerns additional revenue available from new construction and dissolution of TIF districts. New property is exempt from the cap in the first year after its construction and can be taxed “outside” of the cap. It is therefore reasonable to conclude that CPS does in fact lose tax revenues that are generated from new construction. A critically important but unanswered question is how much of the growth in EAV that has occurred within TIF districts is directly tied to new construction. Conventional wisdom holds that a successful TIF district would spur considerable new construction activity within its boundaries. Unfortunately, the limiting effects PTELL could have on CPS’ ability to spread its extension to EAV growth within TIF districts is currently unknown because the city has not determined or not published the value of new construction within TIF boundaries. However, the widespread usage of TIF throughout Chicago suggests that city officials believe the tool to be successful and that TIF is accomplishing its mission of fostering economic

development. Therefore it is equally likely that new construction has occurred and the loss of revenue to CPS is greater than would be predicted by applying the tax cap. The impact then shifts rightward (*Figure 5*).

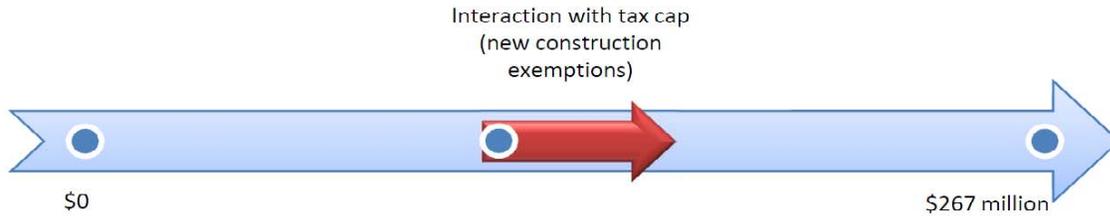


Figure 5: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of the tax cap and allowance for the exemption of increased property values attributed to new construction.

Another opportunity for CPS to capture additional revenue “outside” of the tax cap is when a TIF district is dissolved. With TIF dissolution, tax-cap limited overlying taxing bodies have the ability to receive a one-time increase in revenues as the frozen increment is restored to the tax rolls. This increase in revenue will raise the extension by more than 5% or the CPI in one year, though in subsequent years this new base extension will be subject to the tax cap limitations discussed above. Effectively, TIF is able to create a revenue “windfall” for overlapping taxing bodies upon district expiration. In other words, the exemption within PTELL that allows CPS to collect revenues in excess of the tax cap limitations when a TIF district dissolves suggests that CPS is able to receive additional income it would have not have had access to were it not for the use of TIF. Capturing property value growth generated by the now dissolving TIF district pushes the CPS impact back towards the left (*Figure 6*).

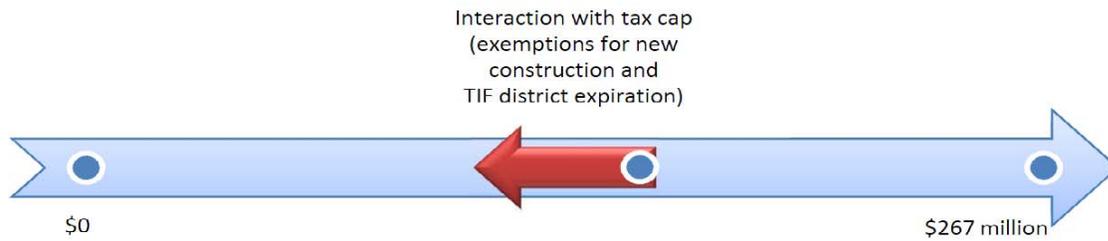


Figure 6: Spectrum illustrating the directional pull of CPS’ annual revenue loss to TIF with inclusion of the tax cap and allowance for the exemption of increased property values attributed to new construction and TIF district expiration.

C. Inflationary Impacts

A TIF district’s frozen EAV or base is set at the time the district is designated and remains constant for its 23-year lifespan or dissolution. The base only changes when parcels are added or dropped from the district and is not adjusted for inflation. By not accounting for inflationary effects, property value growth related to changes in the national economy, as opposed to growth resulting from introduction of TIF, is not captured by overlapping taxing jurisdictions. Cook County Commissioner Mike Quigley claimed that the Illinois TIF Act, while allowing “overlapping local governments to collect tax dollars throughout the lifespan of a TIF on ‘frozen’ property value, [it] fails to protect local governments from the falling value of these dollars over time – in other words, from inflation,” (Quigley, 2007). A 2007 report produced by Quigley found that local taxing districts in Chicago lost \$3.6 million in taxes to a single TIF district in just six years because the Illinois TIF Act fails to adjust the base for inflation.⁸ The effect of inflation on the “frozen” EAV moves the spectrum towards the right indicating an increase in lost revenues (*Figure 7*).

⁸ The study compared property values and tax increments with inflation-adjusted base in Chicago’s Midwest TIF from 2000-2006.

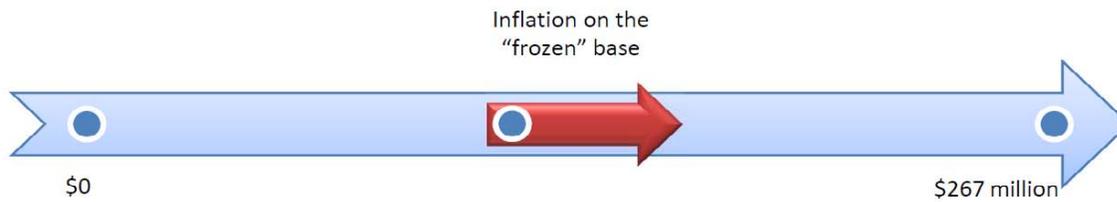


Figure 7: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of inflationary effects on the "frozen" base.

D. Political Realities and Tax Rates

The ability of CPS to increase its tax rate is restricted not only by tax caps and rate limits, but also by political pressures to keep taxes from rising too rapidly. The amount of property tax revenues a taxing body requests from taxpayers is the levy. In recent years, CPS has chosen not to request the maximum levy available to them under tax laws. An argument that has resulted from this policy decision asserts that "if a taxing district has voluntarily chosen not to maximize its property tax levy, it is illogical to contend that it has lost revenue to TIF," (The Civic Federation, 2011). Quigley counters this claim by arguing that school districts, like CPS, "operate under fiscal stress, which most often stems from a combination of high costs and low property values (especially in Illinois, where the majority of school districts' local revenue comes from the property tax), and are already likely to be demanding a lot of taxpayers," and are unable or unwilling to ask for more (Quigley, 2007).

The issue of whether or not CPS can increase its tax rate is central to the question as to whether or not TIF reduces CPS' revenue. While CPS could conceivably raise its rate to capture additional revenue, political pressures from taxpayers make this option untenable at best. If, on the other hand, CPS were able to maintain its rate but have access to a larger EAV base, revenues would increase without the need to raise property taxes. Recognizing the political disincentives to increasing rates the current restrained EAV base likely increases the revenue loss to CPS (*Figure 8*).

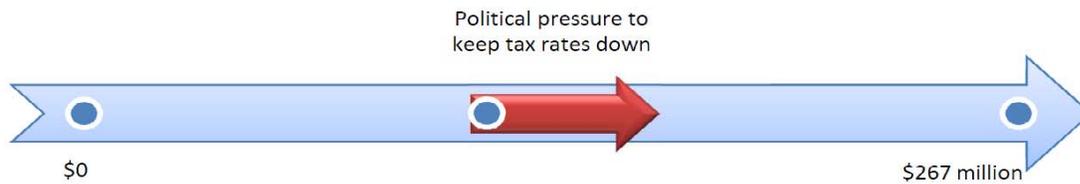


Figure 8: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of political pressures to keep tax rates down.

EROSION OF CPS REVENUE DUE TO TIF

TIF's impact on CPS' EAV base is distinct from its impact on the school district's annual revenue. While TIF does diminish available EAV for CPS and other taxing bodies, this impact does not necessarily correspond with a decrease in revenue. In order to compensate for the loss in property tax collection, CPS raises funds through other sources, most notably, aid from the State of Illinois. This section explores the ways in which CPS is able to offset revenues "lost" to TIF.

A. Interaction with State Aid

State subsidization of school funding provides one mechanism in which CPS can compensate for revenue shortfalls attributable to TIF. The distribution of General State Aid (GSA) to Illinois common schools is determined by a statutorily defined funding formula. The formula provides for different methods of funding allocation, dependent primarily upon the EAV of property within a particular school district. The Illinois state legislature annually sets a target "foundation level" for students which represents the minimum cost of quality education for one pupil adjusted by average student attendance and student income levels.⁹ GSA assists school districts whose "available local resources" (ALR) do not meet this foundation level. Increases in EAV within TIF districts are not included in a school district's ALR calculation for state aid.

⁹ The foundation level for the 2010-2011 school year was \$6,119.

Studies have shown that state aid appears to equalize CPS for their loss in property tax revenues due to TIF. Findings show that decreasing the ALR in school districts that use the foundation-level formula for calculation of state aid “will incur a one-to-one substitution of state dollars for local ones” (Weber, 2003). While TIF reduces the amount of EAV subject to the CPS levy, it does not seem to produce a corresponding decrease in CPS revenue because of the impact of GSA subsidization. However this interplay between state aid and lower ALR for CPS effectively signifies that Illinois taxpayers on the whole are paying for usage of TIF as an economic development tool in Chicago. On our TIF impact spectrum GSA moves the debate towards the left, as CPS is able to compensate for loss in revenue due to TIF by increasing its reliance on state aid (*Figure 9*).

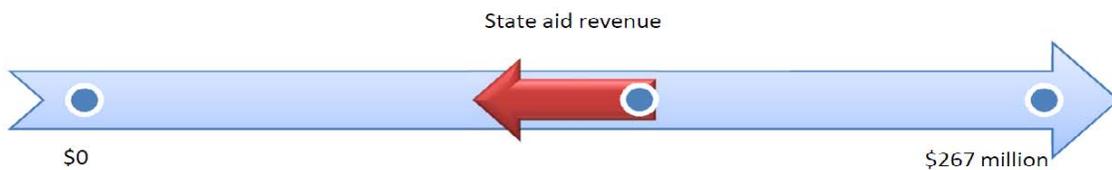


Figure 9: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of state aid revenue.

B. TIF Fund Transfers to CPS

TIF's impact on CPS must also take into account the historical transfers of TIF funds to the school district. The primary way in which TIF funding has been used to support CPS is through intergovernmental agreements. As of 2010, TIF had provided more than \$813 million in funding for CPS capital improvements projects (TIF Reform Panel, 2011). The majority of this funding was connected with Mayor Richard M. Daley's Modern Schools Across Chicago (MSAC) program. Unveiled in 2006, this \$1.1 billion program was jointly funded by the City of Chicago and the Chicago Board of Education and renovated or constructed 27 schools throughout Chicago. An additional almost \$150 million in TIF funds has been granted to individual schools through use of intergovernmental agreements throughout the past decade (City of Chicago, Department of Community Development; Chicago Public Schools, 2010).

TIF district surpluses provide another way funds have been transferred to CPS. The Illinois TIF Act states that the balance in any TIF district that is not already designated for current projects or earmarked for future planned or anticipated projects should be declared as surplus and returned to the overlapping taxing districts. In 2010, Mayor Richard M. Daley declared a TIF surplus and returned \$123 million in TIF funds to CPS. For 2012, Mayor Emmanuel has declared that a surplus of 20% of uncommitted TIF funds will be returned to overlapping taxing bodies. As with the interaction with state aid, the use of TIF funds through both intergovernmental agreements and dispersal of surplus TIF balances causes a leftward shift in the TIF impact spectrum (*Figure 10*).

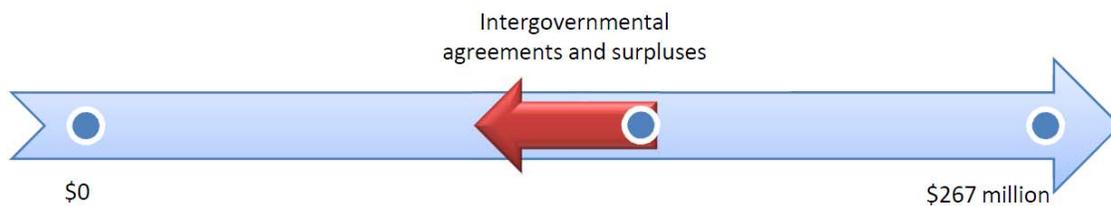


Figure 10: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of intergovernmental agreements and TIF surpluses.

C. The “But For” Issue

The Illinois TIF enabling legislation defines an area eligible for TIF if it “would not derive the benefits of an increased assessment base without the benefits of tax increment financing.”¹⁰ This provision is often referred to as the “but for” requirement, meaning that development would not have occurred in absence of TIF incentives. The “but for” question is central to concerns over designation of TIF districts in the “hot” markets found in the downtown Chicago Loop and adjacent neighborhoods. If development would have happened in these areas even without TIF, then TIF districts are capturing property tax revenues from growth they did not induce. In such instances, taxing bodies like CPS effectively subsidize private development through their reduced ability to tax growth in property values.

¹⁰ 65 ILCS 5/11 – 74.24-2.

Determining how much development activity is attributable to TIF is plagued with assumptions and limitations. In his 2007 study analyzing change in property value growth rates in areas with and without TIF, Quigley finds “evidence that a significant portion of the growth taking place inside TIF districts would have happened even without TIF,” (Quigley, 2007). Byrne’s 2006 study examined evidence that some TIF districts overlap areas with “natural advantages,” and contain properties where values were rising before introduction of the TIF and that are likely to experience continued property value growth (Byrne, 2006).

The question of whether or not TIF causes or captures property value growth is one of the greatest sources of contention between TIF supporters and critics (Quigley, 2007). Proponents argue that taxing bodies like CPS benefit in the long-run from TIF because of the revenue “windfalls” they receive after a TIF district dissolves. This argument is based on the belief that CPS is able to collect additional revenue after this 23-year period that would not have existed were it not for the implementation of TIF. On the other side of the discussion, many argue that the use of TIF in areas that were experiencing growth before designation of TIF districts is a flagrant misuse of the tool and is supporting corporate subsidization at the expense of schools, park districts, libraries, and other cash-strapped government entities. This debate is largely a guessing game that, at best, can inform future guidelines for designation of new TIF districts. While it can reasonably be assumed that considerable growth within TIF districts is attributable to TIF, much of the redevelopment in the central city districts would have arguably occurred without public subsidy. Accordingly, the inclusion of the “but for” variable on our spectrum has an undetermined impact on revenue loss for CPS (*Figure 11*).

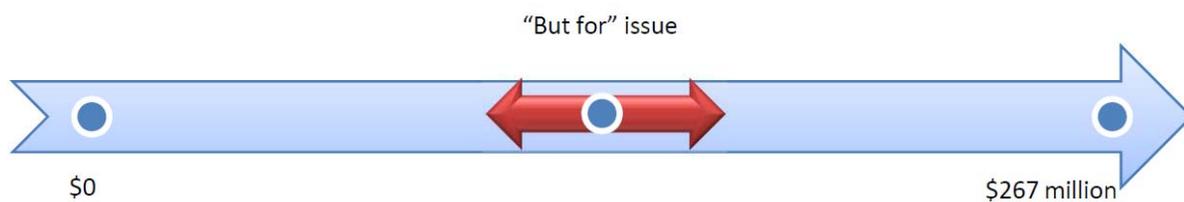


Figure 11: Spectrum illustrating the directional pull of CPS’ annual revenue loss to TIF with inclusion of the “but for” question.

By placing all of the variables discussed above on a single spectrum, we can visually assess the multifaceted impact TIF has on CPS revenue (*Figure 12*).

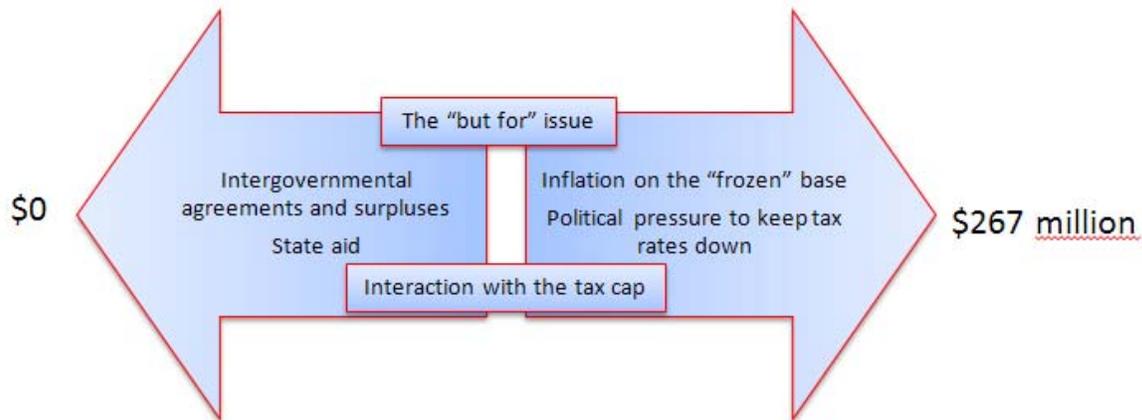


Figure 12: Spectrum illustrating the directional pull of CPS' annual revenue loss to TIF with inclusion of impacts from the tax cap, inflation on the "frozen" base, state aid, and intergovernmental agreements and TIF surpluses, and the "but for" question.

IV. TIF BEST PRACTICES

A growing number of municipalities and states across the country are implementing policy fixes to counter the perceived negative impacts associated with TIF. These governments attempt to balance TIF's value as a powerful tool for spurring local economic development with its potential burden on overlapping taxing bodies and taxpayers on the whole. This section of the paper explores ways in which these governments are addressing many of the TIF-associated challenges addressed above.

A. Consent and Opt-outs

Eleven states out of the 49 that use TIF provide overlapping jurisdictions with the power to "opt-out" of participation (Mullins, 1994). If a municipality establishes a TIF district in Delaware, then only the municipal portion of the property taxes can be pledged to a TIF project unless the municipality obtains the consent of the overlapping taxing bodies. (Polsky Associates LTD, 2011). Taxing units in Texas are

not required to provide any tax increments to TIF funds unless they enter into an agreement to do so with the governing body of the municipality or county that created the reinvestment zone (TIF district)¹¹. In Georgia, school district tax extensions can be pledged for projects in TIF districts, however their actual usage is contingent of the school district's approval of the TIF district in question (Polsky Associates LTD, 2011).

B. Division of TIF Funds and Reimbursements

Overlapping taxing bodies in Texas have the ability to retain up to 15% of the tax increment for themselves¹². A comparable allowance in Chicago could have afforded CPS an additional \$40,039,622 in property tax revenue in 2010. Both Texas¹³ and Wisconsin's TIF statutes provide that surplus revenue in TIF accounts be returned to overlapping taxing jurisdictions after project costs and bond debts have been satisfied (State of Wisconsin , 2005).

Several school districts in suburban Cook County have signed inter-jurisdictional agreements with municipalities to share in the new property tax wealth created by TIF. Arlington Heights School District 24 negotiated a settlement whereby it recoups some of its lost property tax revenue from fees provided by a parking garage built in the TIF district (Arlington Heights School District 24, 2010). Other municipalities provide in-kind assistance to school districts such as utility charge abatements and new infrastructure (Quigley, 2007).

In Ohio, school districts that overlap TIF districts are able to receive value-based payments known as payments-in-lieu of taxes (PILOTs) to offset foregone property tax revenue. Municipalities in Ohio can also provide school districts with other forms of compensation such as waivers for building and zoning fees (Sullivan M. , 2009).

¹¹ Texas Tax Code §311.013(f).

¹² Texas Tax Code §311.013(b)(2).

¹³ Texas Tax Code §311.014.

C. Inflationary Effects

The State of California allows taxing entities to keep growth from inflation of the EAV base, up to two percent, plus any increase in tax increment stemming from reassessments after an ownership transfer.¹⁴ The TIF-enabling legislation passed in Massachusetts in 2003 specifically defined the EAV base as “the aggregate assessed value of the district as of the base date, increased each year by a percentage equal to the inflation factor.”¹⁵

D. Non-Performing TIF Districts

Some legislative bodies have established performance criteria as a condition for diversion of incremental property values from overlapping taxing bodies. Taxing units in Texas, for example, are allowed to retain tax increments collected in non-performing TIF districts.¹⁶

E. Interaction with School Aid

In Minnesota, municipalities that use TIF are limited in the amount of school aid they can receive. The Minnesota legislature enacted these limitations after auditors found that TIF cost the state at least \$100 million of additional school aid in a single year (State of Minnesota, 1996).

F. Other Restrictions

In California, TIF has been widely used for developing new towns in areas with ample vacant land. Critics believe this contradicts the original intention of the economic development tool for use in ‘redevelopment’ projects as opposed to primary ‘development’ purposes. This use of TIF is potentially

¹⁴ California Code – Part 1: Community Redevelopment Law §33492.78.

¹⁵ Massachusetts General Laws, Chapter 40Q §1A.

¹⁶ Texas Tax Code §311.013. (d) If the reinvestment zone is created on or after August 29, 1983, a taxing unit is not required to pay a tax increment into the tax increment fund of the zone after three years from the date the zone is created unless the following conditions exist or have been met within the three-year period:

- (1) bonds have been issued for the zone under Section 311.015;
- (2) the municipality or county that created the zone has acquired property in the zone pursuant to the project plan; or
- (3) construction of improvements pursuant to the project plan has begun in the zone.

unwarranted as development of these lands would likely have occurred in the absence of TIF. Accordingly, California has revised its state rules for TIF to restrict the amount of vacant land in a TIF district to 20% of the total land area (Sullivan, Johnson, & Soden, 2002).

New Hampshire restricts TIF's usage by claiming that "TIF is primarily a tool for public projects and its use for private projects is limited. Public use is narrowly defined such that it may not include the public benefits derived from private economic development activities (including job creation) except in certain limited circumstances¹⁷" (Polsky Associates LTD, 2011).

V. CONCLUSION AND RECOMMENDATIONS

The public debate over the impact of TIF on CPS funding has careened between contrasting narrative frames. One frame stresses the draconian theft of tax dollars from the city's neediest school children. An alternative frame portrays TIF as a benign influence on public education. The parties aligned with these frames are largely talking past each other. Each cites substantive variables and data that appear to validate its perspective. The subsequent public rhetoric generates a lot of heat but little light. The affect is not an enlightened debate over an important public policy tool but instead a war of positioning where conflicting parties battle to establish their framework as the correct one.

What we have attempted to do in this white paper is to acknowledge and situate the validity of conflicting claims about TIF and the public schools within a spectrum of multiple outcomes. We are not offering a new dollar figure of lost revenue or presenting a new statistical analysis. Insightful work

¹⁷ New Hampshire Code Title XII, § 162-K: 2 Definitions IX-a. "Public use" means:

- (a) (1) The possession, occupation, and enjoyment of real property by the general public or governmental entities;
- (2) The acquisition of any interest in real property necessary to the function of a public or private utility or common carrier either through deed of sale or lease;
- (3) The acquisition of real property to remove structures beyond repair, public nuisances, structures unfit for human habitation or use, and abandoned property when such structures or property constitute a menace to health and safety; and
- (4) Private use that occupies an incidental area within a public use; provided, that no real property shall be condemned solely for the purpose of facilitating such incidental private use.

(b) Except as provided in subparagraphs (a)(2) and (4) of this paragraph, public use shall not include the public benefits resulting from private economic development and private commercial enterprise, including increased tax revenues and increased employment opportunities.

done by others, including University of Illinois at Chicago Professors Rachel Weber, David Merriman and Richard Dye, as well as studies conducted by Commissioner Quigley, the Grassroots Collaborative, and the Civic Federation have already identified the relevant variables and raised important questions. Instead, it is our view that the conversation over TIF and schools would be best engaged by recognizing how the relevant variables likely shift the impact on school funding.

Depending on the factor and the weight of its influence, the loss of local property tax dollars to city schools because of TIF will shift between more or less. For a school system with a \$700 million budget deficit the shifting is not without consequence. Our graphic assessment is a device for generating a new way to approach or “see” the dynamic interrelationship of factors shaping TIF’s impact on school funding.

As a thought-piece the spectrum model is presented to primarily trigger public discussion and comment. We do however want to make three recommendations, involving data collection, a new departure for problem solving and possibilities for amending the use of TIF.

First, it is essential that the dollar value of annual new construction generated within TIF districts be calculated and made available to the public. The absence of a published citywide new construction increment is a significant limitation on conducting an accurate assessment of TIF’s impact on school funding. This data is undoubtedly collected by the Cook County Assessor and yet it remains subject to speculation.

In addition we would also encourage the city, CPS, and the Chicago Teachers Union to begin a serious conversation about school funding that recognizes the equanimity of the competing narratives. Instead of tossing absolute if speculative dollars’ values of lost income into the public square we would encourage a pragmatic, problem-solving approach that embraces competing narratives. For example, state aid may be bridging the funding gap caused by TIF but if so it is also shifting the burden to tax payers from around the state. The property tax base may be frozen but incremental allowances from TIF surpluses have been transferred to the school district. Tax caps do reduce the loss of potential tax revenue within TIF districts, but if new construction is a sizeable portion of that property value growth, the cost to schools increases. Frozen EAV does serve to limit the base of available taxable property, but

if the increased property values would not have occurred “but for” TIF designation, when the TIF district sunsets the schools will reap a funding windfall. CPS has not utilized its taxing authority to the maximum, but if its base of taxable property was not frozen and growth would have occurred without public incentives, then revenue would have increased without raising unpopular taxes. By stating these dichotomies we do not claim to be certain of the outcomes. But we do strongly contend that the TIF-school policy discussion would be elevated by an acknowledgement and full assessment of alternative narratives.

Finally, TIF legislation is no longer an exotic measure but a mature economic policy tool with multiple data points. The City of Chicago now has almost a three-decades-long experience with TIF and should not hold itself captive to past practice. There are instead TIF “best practices” that should be seriously investigated and if appropriate adopted.

As a university-based school dedicated to facilitating the capacity of institutional stakeholders to find solutions to public policy problems, we respectfully submit that a TIF program that equally serves both the city’s economic development needs and Chicago’s school children is more likely to arise from within a process sketched within this paper than from the current polarized approach.

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