

Tax Increment Financing in the City of Chicago

Tax Increment Financing (TIF) is the primary incentive for real estate development utilized by the City of Chicago. It is a special investment tool that the City (and many other Illinois municipalities) use to promote economic development as well as to construct infrastructure improvements in areas (TIF districts) that are blighted, or at risk of becoming blighted. TIF funds are generated by incremental increases in property taxes that exceed an established base level within a given TIF district. The City uses the incremental funds to stimulate real estate development investment and public infrastructure improvements. In turn, economic development is promoted within (and often outside) the district; there are 165 active TIF districts in Chicago. The use of TIF is not without controversy, however.

This article describes some of the fundamentals of the process and the standards associated with approval of TIF for private development projects. It also briefly focuses on some of the common arguments for and against TIF.

TIF Approval Process and Standards

1. The developer must obtain City approval of its TIF application. TIF applications are reviewed by the Department of Community Development and negotiated with the developer, resulting in an agreed-upon Term Sheet. The proposal is then considered in a public meeting by the Community Development Commission, which recommends approval of the applicant as the “designated developer,” whereupon the Commission is considered to have recommended approval of the Term Sheet. Thereafter, the developer and the City negotiate a lengthy redevelopment agreement. The proposal is subsequently considered by the City Council Committee on Finance and its recommendation is submitted to the full City Council for consideration of approval. Once the developer has funding commitments, the TIF closing can occur. The entire process can be expected to take between nine and 12 months.
2. The developer must satisfy certain economic standards. First, it must demonstrate that the project will not be economically viable without (or “but for”) the TIF funds. In other words, it must be proven that the project cannot make a reasonable return on investment without the TIF assistance. Second, the project must include TIF-eligible costs in an amount equal to or greater than the amount of TIF assistance. Third, projected property tax increases must show the increment over the remaining life of the TIF District will be equal to or greater than the TIF amount requested. Fourth, the City generally limits reimbursement to between 10% and 20% of project cost, and therefore the developer must be able to privately fund the remainder.
3. The developer must satisfy certain City policy requirements. These include construction of affordable housing units or a cash-in-lieu of housing contribution (residential projects only), minimum minority and women-owned business enterprise participation, minimum number of Chicago residents employed in the construction of the project, minimum wages paid to employees in accordance with the Prevailing Wage requirements, establishment of covenants, such as job creation/retention, and contribution of a “public benefit,” among others.
4. The developer takes the risk that the anticipated increment payments will be generated. In most instances, the developer receives reimbursement for development costs it has already expended; i.e., it does not receive TIF funds until the project is complete. Under the typical “pay-as-you-go” approach, reimbursement payments will be made to the developer on an annual basis solely to the extent of the actual incremental revenue generated (less a percentage reserved by the City). Generally, the revenues allowed to reimburse the developer are limited to those that arise solely from the TIF revenue generated by the project’s property itself.

5. The developer is contractually obligated to complete the project. In return for the right to receive TIF revenue, the project must be completed within a specified time period regardless of whether or not TIF funds for reimbursement have actually been received.

6. The developer's reimbursement is limited to TIF-eligible project costs. These costs include, among others: land acquisition; site preparation and demolition; legal, architectural, engineering and financial-planning services; existing building rehabilitation; limited construction-period interest; workforce training and; public improvements. With certain exceptions, new construction does not qualify.

Controversy Over Chicago TIFs

Various concerns about the use of TIF have been raised by the public and the media. These include the sufficiency of controls over uncommitted TIF District funds, the necessity of TIF districts where property tax revenues might otherwise have been sufficient without establishment of a TIF district, the impact on school districts resulting from diversion of increased property taxes and lack of transparency in the administration of TIFs. These may be legitimate policy issues to be considered by the City. Some critics, however, have referred to TIF as a vehicle for the City to keep development-generated money for its own use and that of "politically-connected" developers. They have characterized TIF funding as "goodies" and "giveaways" handed out to developers.

Supporters of TIF disagree. They assert that developers are carrying out the central purpose for which TIF financing was originally established; i.e., to encourage economic development that would otherwise not occur. Supporters call attention to the long-term economic benefits of development that have occurred as a result of TIF, noting that by the City's estimate, new development assisted with TIF funds has generated more than \$12 billion in increased property values throughout the City since the inception of the TIF program in 1984. Proponents further note that the process for approval of TIF assistance (as described above) is rigorous and thorough and that the City's staff and its Law Department work hard to assure that all standards are met and all applicants are treated fairly. Supporters contend that developers are subject to a high standard enforced by the City, and that developers take substantial risks with their own funds.

In light of the upcoming Mayoral race, as well as the continuing controversies noted above, we expect that the use of TIF will continue to be a hotly debated issue. Though adjustments and refinements to the TIF process may be implemented, we also expect that TIF will remain one of the most important tools for economic development in Chicago.

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