How do TIF districts Work?

The following is a direct quote from the Illinois Tax Increment Association website:

“A tax increment is the difference between the amount of property tax revenue generated before TIF district designation and the amount of property tax revenue generated after designation. Establishment of a TIF does not reduce property tax revenues available to overlapping taxing bodies as the property taxes collected on properties included in the TIF at the time of designation continue to be distributed to them in the same manner as they would if the TIF did not exist. Only the new property taxes generated by the incremental increase in the value of these properties after the TIF is established are available for investment in the TIF.

“For example, assume that a municipality wants to develop an area that includes two parcels that contain substandard commercial buildings. Let’s also assume that both of these parcels are paying $30,000 per year in property taxes. However, the municipality finds that by making an investment of $500,000 to rehabilitate the buildings on the two parcels and provide necessary infrastructure, private developers will commit an additional $2,000,000, making the commercial buildings available for new use. This additional investment causes the property to increase in assessed value, for example — and conservatively — leading to the tax paid on each parcel going from $30,000 per year in property taxes to $60,000 per year. The public and private investment would increase the total property taxes paid from $60,000 each year ($30,000 per parcel), to $120,000 each year ($60,000 per parcel). The project would result in $60,000 in new tax increment, which the municipality could use to off-set its original investment in less than nine years. After this initial investment is paid-off, the newly generated increment can be used for additional investments in the area.

“Ultimately, after the conclusion of the TIF project, all of this new revenue growth is available to the various taxing bodies. Successful TIF investment therefore serves all of the investors, both public and private. Private investors are helped by a reduction in development cost and risk, and public investors by the generation of additional revenue available at the conclusion of the TIF project.”

In this example the municipality invested available funds to kick start the TIF, then recouped the investment over the next nine years. An alternative would be to accumulate the incremental property taxes for investment once a sufficient reserve fund has been established. This is how a TIF district is supposed to work.

Next time: What are some typical TIF projects?