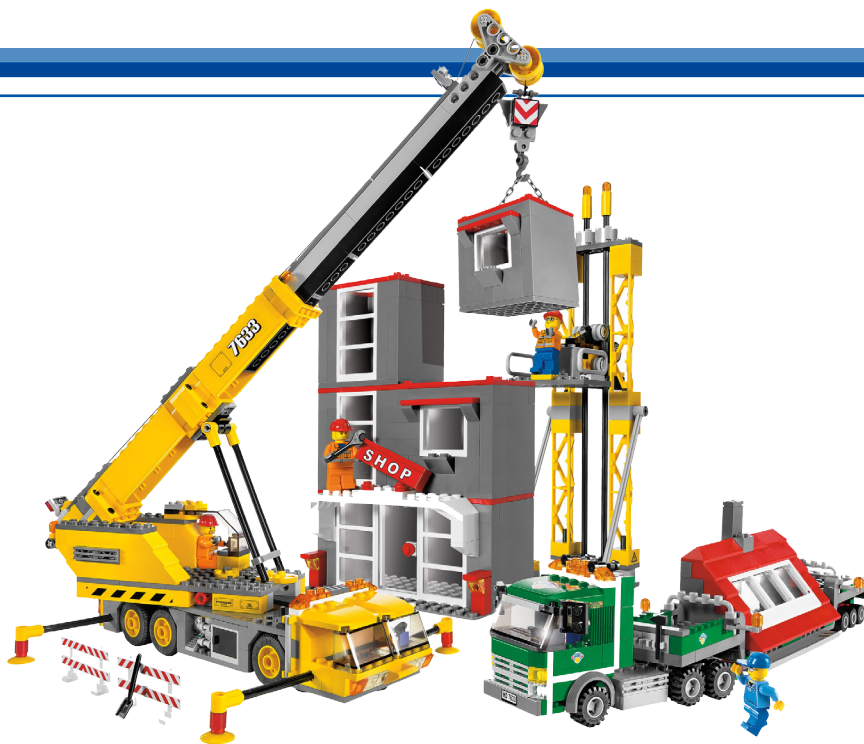


THE WISCONSIN TAXPAYER

Vol. 84, Number 9 | September 2016



The Municipal Development Tool

TIF: How Does It Work? Is It Necessary? Risky? Overused?

Since 1982, local governments in Wisconsin have used more than \$6.2 billion of property taxes on tax incremental finance (TIF) projects, including \$3.5 billion over the past 10 years. The state currently has 1,212 tax incremental finance districts, with nearly two-thirds located in municipalities with fewer than 15,000 residents. Despite its widespread use, most state residents know little about TIF.

Tax incremental financing (TIF) is a municipal development tool originally designed to help cities redevelop areas that were blighted, in need of rehabilitation or conservation work, or suitable for industrial development. Over the years, laws governing TIF have changed, resulting in a current law that is more expansive than the original. With expansion has come questions about appropriate use of TIF for some projects.

Unfortunately, most Wisconsin residents know little about TIF, even though local governments have used more than \$6.2 billion of property taxes on these projects since 1982, including \$3.5 billion over the past 10 years.

TIF BASICS

Wisconsin's TIF law permits cities and villages—and in some cases towns—to divert property taxes from their typical uses to subsidizing private development in a specific area.

Often, to attract private investment in a city or village, the local government borrows money to make improvements (streets, sewers, etc.) in a certain area or to provide grants to the developer.

Property taxes generated from new or refurbished buildings within the designated area are used to repay the debt. The greater the private investment and property value growth in the TIF district (TID), the faster the borrowing is repaid. A basic TID timeline is outlined on page two.

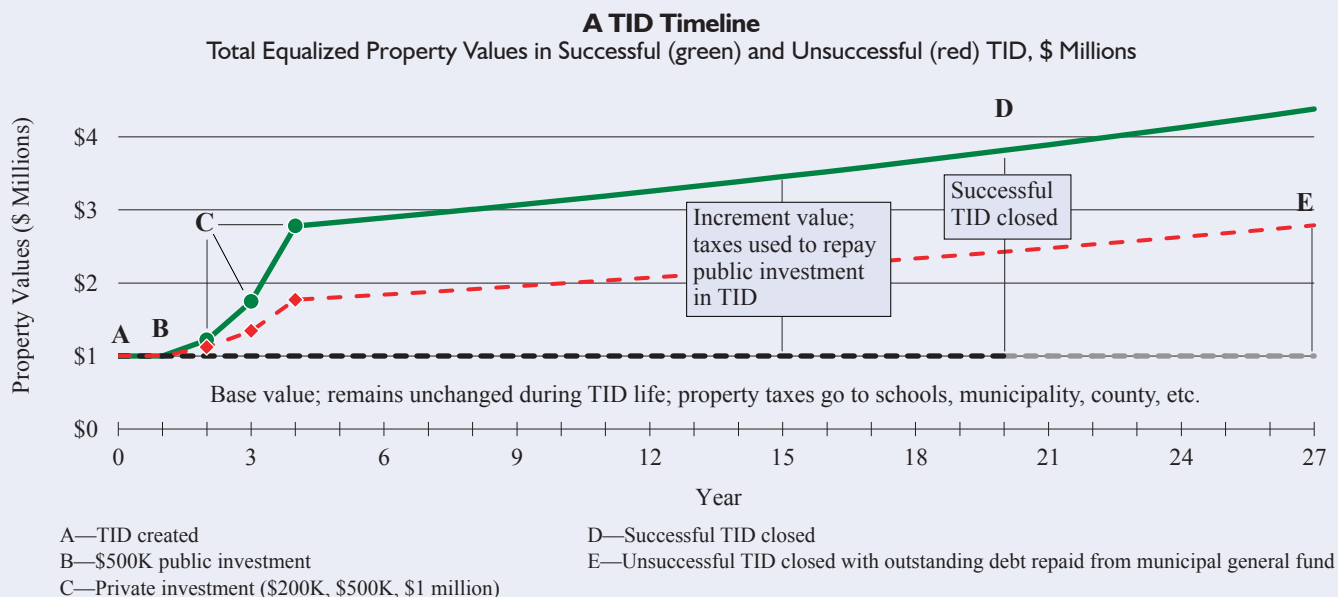
Brief History

Passed in 1974, the original TIF law was relatively narrow and meant to target urban areas. This was a time of federal retrenchment in redevelopment financing.

The 1973-75 recession increased state lawmaker interest in sparking local development. As mentioned at the outset, only certain areas were eligible for TIF. Municipalities were required to show that the development would not occur without TIF. And TIF use was limited; a municipality could not create additional districts if the value of a proposed TID

Also in this issue:

Highways Compared • New Construction



To aid understanding of TIF, a brief timeline of a hypothetical TID is discussed.

Proposing a TID

A local developer approaches city officials about a new development she would like to undertake. For it to be successful, public assistance in the form of TIF is needed. A new TID is approved (A) and the project moves forward.

Prior to development, all taxable property in the district is valued at \$1 million (the base). Throughout the TID's life, property taxes levied on the base value continue to fund various local units of government.

Public Investment

The city borrows \$500,000 for new sidewalks and street improvements in the district, and for a \$50,000 cash grant to the developer (B).

Private Investment

With improvements in place, the project moves forward. The developer spends \$200,000, \$500,000, and \$1 million, respectively, over three years (C).

The new investments, public and private, increase area property value. Ideally, following improvements, values continue to grow at rates greater than those in the rest of the community. Here, the district's value grows over 20 years from \$1 million to \$3.8 million.

Property Values and Taxes

While the TID exists, its value is split between the base—the area's value prior to district creation (\$1 mil-

lion)—and its increment (how much the area appreciated since district creation). For example, in year 15, the district's value is \$3.5 million, a combination of \$1 million in base value and \$2.5 million in increment.

The total property tax rate (the sum of the municipal, school, county, technical college, and state rates) is applied to the value of the TID. Taxes from the base value go to all governmental units. Taxes on the increment, however, are used to repay the initial \$500,000 borrowing. When the public investment is paid off, or at a time set by state law (see page three), the district is closed (D). Then, all property taxes from the district fund local governments.

Because of state-imposed tax limits, local governments generally do not receive additional revenue when a TID is closed. Rather, the increase in property value lowers property tax rates for all taxpayers in the municipality.

Unsuccessful TID

Not all TIDs are successful. The dashed line shows values in an unsuccessful TID with the same \$500,000 public investment. Private investment totals just \$700,000, or \$1 million less than in the successful one. As a result, taxes on the increment are insufficient to repay the \$500,000 borrowing. The district must close after 27 years, and the municipality repays what is remaining on the loan.

If the municipality has a second, successful TID, under certain circumstances it can use revenues from it to repay the borrowing in the unsuccessful TID (see page 5).

plus the value of all existing TIDs was more than 5% of total municipal property value.

Over time, many changes were made to the law, including some that were technical in nature. For example, early changes: clarified that a TID's base was its equalized (or fair market) value as determined by the Department of Revenue, and; specified the types of municipal expenditures that could be funded with TIF.

In addition to technical changes, the law was altered for specific cities or villages; current law includes 38 such paragraphs. Often, these targeted changes were ultimately expanded to all TIDs.

For example, prior to 1989, TID expenditures were limited to the first five years following creation of the district. However, lawmakers extended the expenditure period for TIDs in certain municipalities. In 1989, the expenditure period was extended to the first seven years for all TIDs.

Other legislation was not technical or targeted, rather it broadly expanded or limited TIF use.

Then vs. Now

The end result is a TIF law that is significantly different—and more expansive—than the original. Space limitations limit discussion to major changes.

Eligible Areas. Under the original law, only areas that were blighted, in need of rehabilitation or conservation, or suitable for industrial use were eligible for tax incremental assistance. In 2004, state lawmakers added “mixed-use” to the list of eligible projects. This type of project contains a combination of industrial, commercial, and residential properties, though new residential property cannot comprise more than 35% of total TID area.

Of 1,212 current TIDs, 284 (23.4%) are mixed use. That figure understates their popularity, however. Of 673 districts created since 2005, 284 (42.1%) were of that type.

TID Life and Expenditure Period. The 1974 law limited the maximum life of a TID to 20 years, though the district had to be closed earlier if all costs were reimbursed. Public expenditures were limited to the first five years.

Under current law, the maximum life depends on the type of district (blighted, rehab/conservation, industrial, or mixed use) and ranges from 20 to 27 years. However, extensions that add years to the life of the TID are allowed in some cases.

Now, expenditures can be made up to five years prior to the original maximum life of the district. In other words, expenditures can be made for the first 22 years in a district with a maximum life of 27 years.

Beginning in 2004, mixed-use developments were allowed under TIF law. Since then, 284 TIDs of this type have been created, or 43% of all new TIF districts.

Allowable Costs. State statutes delineate costs eligible for TIF reimbursement. Generally, these have changed little over the years. However, when lawmakers made mixed-use projects eligible for TIF in 2004, they added certain cash grants to developers to the list of reimbursable expenditures.

A second major change occurred in 2009. Since October of that year, municipalities can extend the life of a TID for up to one year after all costs are repaid. The tax dollars collected from the district during this period must be used to improve housing, with at least 75% benefitting affordable housing in the community.

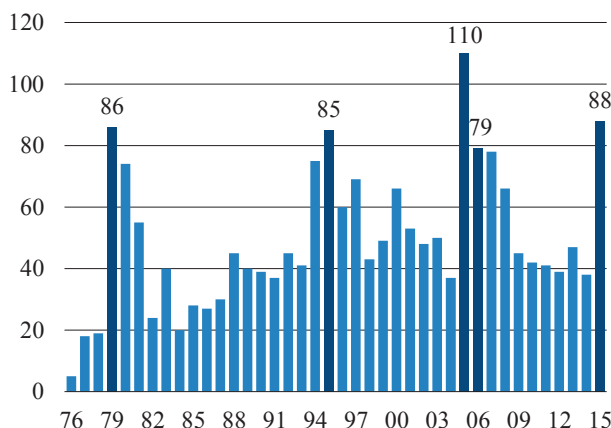
Limits on New TIDs. As mentioned, state law limits TID use by capping the percent of total property value in these districts. Under the original law, the cap was 5% (see above); under current law, the limit is 12% of total value.

INCREASING USE

Due partly to liberalization of the law, use of TIF has grown over the years.

TID creation is somewhat cyclical in nature. When the economy is growing and development is

Figure 1: TID Creation Follows Economic Cycle
Number of TIDs Created by Year, 1976-2015



strong, use of TIF expands somewhat. For example, during 1985-2000, as Wisconsin's economy emerged from recession and then boomed during 1985-2000, the number of TIDs created rose from 28 (1985) to 66 (2000). During 1994-97, municipalities created an average of 72 TIDs per year (see Figure 1, page 3).

Then, as both national and state economies retrenched after 2000, TID creation slowed. The number of new districts declined from 66 in 2000 to 37 in 2004.

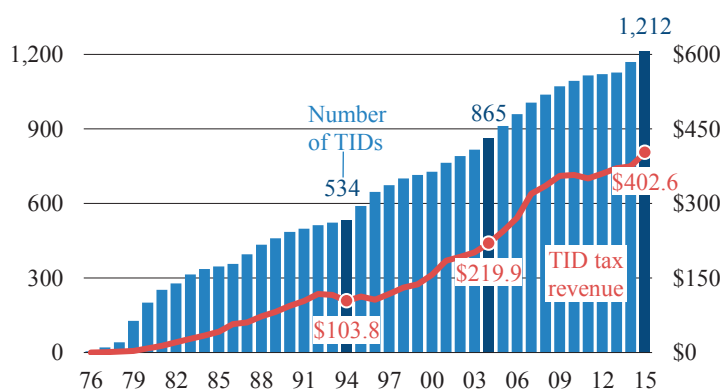
TIF use also expanded due to liberalization of the law. For example, in the three years after lawmakers allowed mixed-use TIDs (2005-07), municipalities created 267 new districts, including 116 (43%) of this type.

Growing Numbers of Districts

Since tax increment districts generally exist for 20 or more years, newly-created districts add to those already in place. In other words, the number in existence grows annually.

Figure 2 (bars) shows that by 1994, 18 years after creation of Wisconsin's TIF law, cities and villages here were operating 534 TIDs. Ten years later, that number had climbed to 865, a 62% increase. During 2004-15, the number increased another 40% to 1,212.

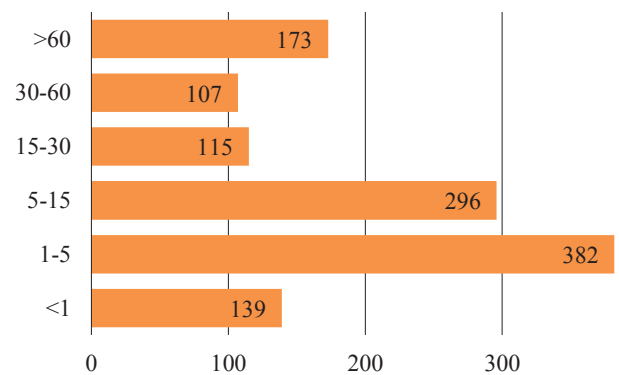
Figure 2: Number of TIDs Growing
Number of Existing TIDs by Year, 1976-2015



TID Location

Although TIF districts were originally intended to address urban blight, more than two-thirds of all TIDs today are located in communities with fewer than 15,000 residents (see Figure 3). In 2015, 139 TIDs (11.5%) were in municipalities with fewer than 1,000 residents, 382 (31.5%) were in communities with 1,000 to 5,000 residents, and 296 (24.4%) were in cities and villages with 5,000 to 15,000 residents.

Figure 3: Most TIDs in "Small" Communities
of TIDs by Municipal Population (Thousands), 2015



The state's most populous cities, those with populations greater than 60,000, operated only 173, or 14.3% of all TIDs.

Many large cities have multiple TIDs. Milwaukee, the state's most populous city, has 48. Other cities with 10 or more TIDs include Oshkosh (18), Madison (17), Kenosha (15), Green Bay and Waukesha (both 14), La Crosse (13), Janesville, Menasha, and Racine (all 12), West Bend (11), and Fond du Lac, Manitowish, and Sheboygan (all 10).

Increasing Revenues

As the number of districts has risen, so has TIF tax revenue (line in Figure 2). This is to be expected; if a TID is successful, its value rises each year, generating additional tax revenue. In 1994, the 534 TIDs generated \$103.8 million in property taxes used to pay for public investment in the districts. That amount more than doubled over the ensuing 10 years to \$219.9 million in 2004. In 2015, 1,212 districts generated \$402.6 million in tax revenue.

Share of Value

Not only have TIF collections increased, they have grown as a share of all property taxes levied. In 1994, TIF tax collections accounted for 1.9% of all levies. By 2007, that percentage had climbed to 3.5%. With recession impacting new construction in the state, TIF revenues flattened somewhat during 2008-11. However, they have resumed growing since and now account for 3.8% of all property taxes.

Statewide percentages provide perspective on TIF usage. However, for individual municipalities, the percentage of total property value in TIDs is also used to cap usage. As mentioned, if that percentage is 12% or more, new TIDs cannot be created.

Table 1: TID Value as Pct. of Total Property Value
10 Highest Pct. and 10 Largest Cities, 2015

Municipality	Pop.	Tot. Mun. Value	TID Incr.	% of Val.
<i>10 Municipalities With Highest TIF %</i>				
Warrens	356	\$55.1	\$38.2	69.3%
Weyerhaeuser	228	\$27.1	\$18.5	68.4
Pittsville	875	\$59.5	\$32.7	55.0
Brokaw	241	\$20.9	\$10.0	48.1
Glen Flora	88	\$5.5	\$2.6	48.1
Cashton	1,107	\$73.0	\$31.1	42.5
Blue Mounds	938	\$69.1	\$26.4	38.1
Johnson Creek	2,933	\$313.0	\$113.1	36.1
Wilton	501	\$26.6	\$8.9	33.5
Oakdale	293	\$23.7	\$7.6	32.2
<i>10 Largest Cities</i>				
Milwaukee	594,666	\$27,042.0	\$1,496.8	5.5%
Madison	247,206	\$24,596.4	\$761.5	3.1
Green Bay	105,078	\$6,080.6	\$246.8	4.1
Kenosha	99,488	\$6,072.6	\$699.3	11.5
Racine	78,165	\$3,212.4	\$89.0	2.8
Appleton	74,286	\$4,938.7	\$168.5	3.4
Waukesha	71,699	\$5,877.2	\$249.5	4.2
Eau Claire	67,381	\$4,872.7	\$151.6	3.1
Oshkosh	66,717	\$3,776.2	\$264.1	7.0
Janesville	63,470	\$4,165.1	\$179.2	4.3

Of 420 municipalities with TIDs in 2015, 112 (27%) were above the 12% threshold and cannot create more TIF districts. Cities and villages with the highest percentages were generally small. Of the 10 with the largest percentages of total property value in TIDs, eight had fewer than 1,000 residents (see Table 1).

Among Wisconsin's 10 most populous cities, TIDs ranged from 2.8% of total value in Racine to 11.5% in Kenosha.

While some might look unfavorably at high TID percentages, that view is not necessarily warranted. Comparing Brokaw and Weyerhaeuser is instructive. Both have large percentages of their total property value in a TID, though one appears to be more successful than the other.

The Brokaw district was created in 1997 and was expected to close in 2020. However, its life has been extended 10 years to 2030, and municipal officials have designated it as distressed (see page 6). By contrast, the Weyerhaeuser TID was created in 2013, and its value has grown rapidly since inception.

RISKS

TIF use can be beneficial to a community by reinvigorating a stagnant or declining area, or by attracting new businesses. However, there are risks.

Over/Under Investment

A common use of TIF is funding infrastructure to attract business. The amount of public investment is an important factor in whether a district succeeds or fails.

A municipality may invest heavily in an area, hoping for growth to follow. However, large public investments require greater private development to repay the infrastructure costs. Insufficient development leaves a municipality—and local taxpayers—responsible for unpaid costs.

There is also a risk to underinvestment. If improvements in an area are insufficient, businesses may not find the site attractive. In that case, despite limited public investment, there would be little or no private investment to tax and the municipality would be left responsible for unpaid costs.

Donor Districts. In municipalities with multiple TIDs, these risks can be reduced. Under certain circumstances, cities and villages can use revenues from successful TIDs to fund the costs of unsuccessful ones. The “donor” district must have the same overlying tax jurisdictions as the recipient.

For example, the City of Appleton is in multiple counties. If it had a struggling TID in the Calumet County part of the city, it could not transfer revenues from another TID in the Outagamie County part of the city. Taxes from donor districts can only be allocated for costs related to low-cost housing, environmental remediation, blight, or rehabilitation, or to certain “distressed” districts (see below). “Donations” are limited to 10 years.

Dislocation

Some municipalities use TIF to encourage retail growth. Sometimes these TIDs are not downtown or in the community's main commercial district.

While the TID may be successful in terms of attracting new retail activity, it might adversely affect existing retail establishments. In some cases, retail stores move from the traditional commercial district to the TID, adding little value to the community.

Funding Public Services

Another risk with TIF is funding the increased demand for public services, such as police, fire, street

maintenance, and sometimes garbage pickup. This is of particular concern if the TIF project includes residential development. Since property taxes on the new development are used to repay infrastructure investments, the costs of these additional services are paid by residents and businesses outside the TID.

As of 2015, municipalities identified 88 TIDs as “stressed” and another 18 as “severely stressed”, conditions that allow local officials to extend district lives.

Distressed TIDs

The 2007-09 recession significantly affected many TIDs. For those created in the few years prior to recession, the construction downturn after 2007 meant some of the expected development never occurred. Without this new activity, some TIDs were at risk of not generating sufficient tax dollars to repay municipal borrowing.

Other districts were underperforming prior to recession, and likely would not generate sufficient tax revenues to repay public investment. In 2009, lawmakers allowed cities and villages to declare certain TIDs either distressed or severely distressed.

A distressed TID is one in which project costs exceed expected revenues. A severely distressed TID is a distressed one whose value has declined at least 25% from its highest value. Only TIDs created before October 2008 are eligible for these designations. After September 2015, municipalities could no longer designate new distressed or severely distressed districts.

State law allows time extensions of these districts: for a distressed TID, 10 years beyond the original end date; for a severely distressed one, to 40 years of total life. It also allows the life of donor districts to be extended up to 10 years. The state currently has 88 distressed and 18 severely distressed TIDs.

By Type. Industrial TIDs (45 total, see Figure 4, left) accounted for 42% of stressed or severely stressed TIDs. Mixed-use (20), blighted (11), and rehabilitation/conservation (7) districts comprised smaller shares of the total. TIDs created before 1995 did not have to designate type; they accounted for 23 of the 106 financially stressed districts.

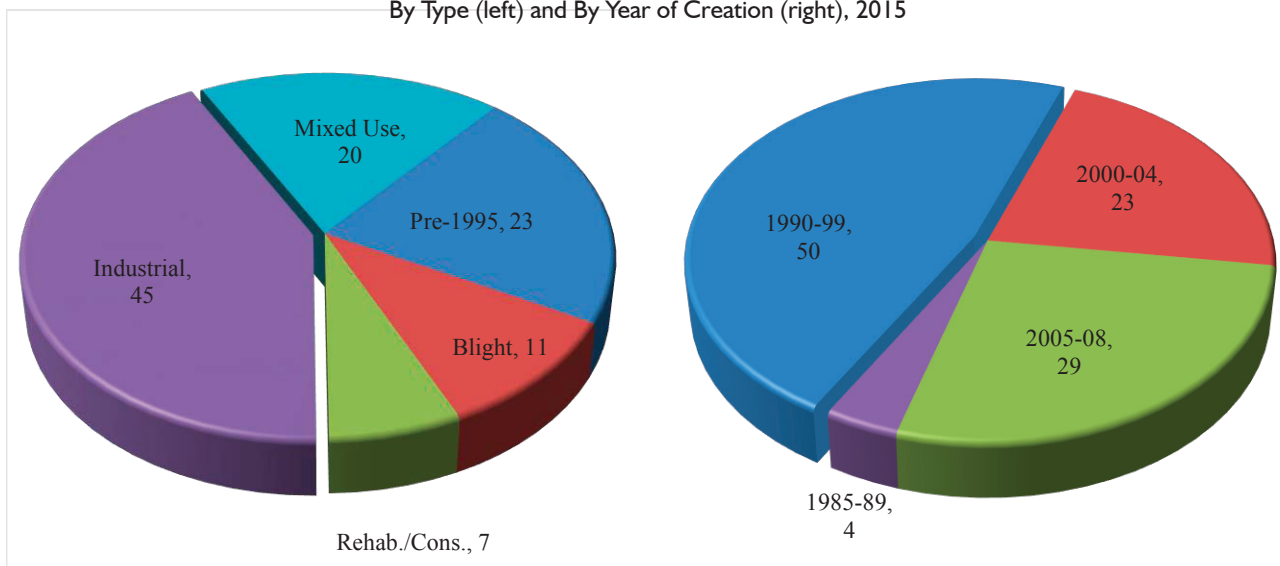
By Base Year. A second way to view stressed districts is by base (or creation) year. Nearly half (50 of 106) of these TIDs were created in the 1990s (Figure 4, right). Another four were created before 1990. In other words, more than half of all stressed TIDs had been in existence between eight and 23 years prior to the recession. For many of these, it was factors other than recession that made them “unsuccessful,” but recession may have been the tipping point.

Another 23 stressed TIDs were created during 2000-04, and 29 during 2005-08. This last group was likely affected most by the 2007-09 construction slowdown. Of the 29 created during this latter period, 20 were mixed use.

MEASURES OF SUCCESS

Often, it is difficult to measure the success of a TID. First, although a development might pass the “but for” test (the development would not occur *but*

Figure 4: Stressed and Severely Stressed TIDs
By Type (left) and By Year of Creation (right), 2015



for the use of TIF), there is often no way of knowing if other development would have occurred had TIF not been used.

Measuring success also requires knowledge of a district's aims. Was it job creation? Increased property values? More tourism? The ultimate success of a district should be based on meeting the TID's objectives.

Statewide data are not available on objectives. However, examination of 57 recently closed TIDs can provides insight into relative financial success.

Value Growth

The 57 closed TIDs existed for an average of 18 years. Combined, they added \$934.8 million in property value to a base of \$210.0 million, an average increase of 9.8% per year.

These totals mask wide variation in property value growth. Six of the 57 had either no gain or declined in value. Another 16 averaged gains of less than 5% per year.

By contrast, 24 of the 57 (42.1%) had annual gains of 10% or more; 10 had annual increases averaging more than 20%.

While value growth gives some indication of TID success, it can be misleading. A TID with little public investment may be able to repay public costs with relatively small value growth, while one with significant costs may have difficulty repaying borrowing, despite relatively rapid growth.

Donor or Donee?

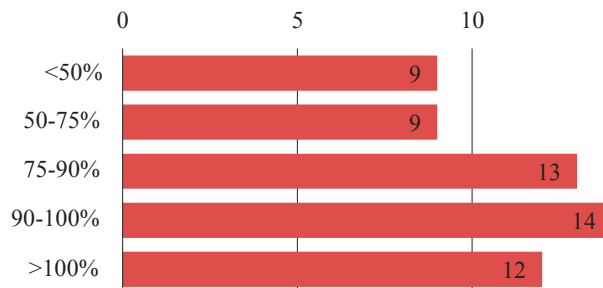
One indicator of financial success or failure is a TID's status as a donor or donee district: A district must have repaid its costs in order to help fund another TID. Of the 57 TIDs studied, 13 were donor districts, sharing \$33.9 million in tax increments to help finance less successful TIDs.

A similar number of less successful TIDs (12) received \$16.0 million in assistance from other TIDs.

Tax Increments

A variety of revenue sources are used to repay public TIF costs: state computer aid, developer guarantees, and property sales are examples. However, the primary source is tax increments, which funded 86.7% of the costs in the 57 closed districts. However, that varied from less than 50% in nine (see Figure 5) to more than 100% in 12 TIDs. In only 26 of 57 TIDs did tax increments cover more than 90% of district costs.

Figure 5: Tax Increments Relative to Total Costs
of TIDs by Share of Covered Costs, Districts Closed in 2014-15



FINAL THOUGHTS

TIF is municipal government's main, even sole, development tool in Wisconsin. It has been used successfully to rehabilitate stagnant or declining areas in the state. However, some argue that it is encouraging cities and villages to take on more debt than they can responsibly afford. Others say that it is being used in areas that would likely develop without public assistance. There is also growing concern that TIF is used to subsidize profitable development firms that probable do not need the help. □

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WISTAX NOTES

■ **Highways Compared.** A study released this month finds that, in 2013, 3.7% of Wisconsin's rural interstates and 7.2% of its urban interstates were in poor condition. While the percentages are not large, the state ranked 41st and 38th, respectively, among the states on these two measures. The higher the percentage, the lower the rank. The Badger State also ranked low (40th) on the percentage of other main rural highways rated poor, according to the Reason Foundation.

On two other transportation measures, the state fared better. While nationally, 20.4% of bridges were in deficient condition, that percentage was 13.8% here. Only six states had lower percentages. Wisconsin's fatality rate was also relatively low. At 0.9 per million vehicle miles, it ranked 11th among the states.

■ **New Construction.** Net new construction during 2015 totaled \$7.0 billion, or 1.4% of the total value of all taxable property in the state. Both figures are the highest since 2007, prior to recession. However, they lag well behind the \$12 billion in new construction in 2005, which added 2.8% to property values.

At the local level, new construction figures are important as they help determine how much local property taxes will rise next year.

New construction varied throughout the state. It averaged

more than 2% in Calumet, Dane, Eau Claire, Lafayette, Outagamie, and Trempealeau counties. It was less than 0.5% in Bayfield, Iron, and Price counties. Net new construction was less than 1% in most northern counties.

Figures for all counties are on the WISTAX website at wistax.org/facts. □

In FOCUS . . . recently in our biweekly newsletter

- Property values up 3% statewide; still trail pre-recession peak (#15-16)
- State of Wisconsin's cities and villages (I): Fiscal and economic health (#16-16)
- State of Wisconsin's cities and villages (II): Citizen engagement (#17-16)

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		1. Mailed outside-county	15	16	
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		E. Total free or nominal rate distribution	251	227	
		F. Total distribution (C + E)	3,249	3,028	
		G. Copies not distributed	1,413	1,320	
		H. Total (F + G)	4,661	4,348	
		I. Percent paid	92%	93%	
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