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AN INTRODUCTION TO
TAX INCREMENT ALLOCATION
REDEVELOPMENT FINANCING (“TIF”)

OVERVIEW OF TIF

Tax Increment Allocation Financing (TIF) is arguably the most powerful economic redevelopment tool available to municipalities in Illinois. TIF was brought to Illinois in 1977 when the legislature adopted the Tax Increment Allocation Redevelopment Act (the “TIF Act”). (65 ILCS 5/11-74.4-1 et seq.)

TIF is utilized to both eradicate and prevent “blight” as defined by the Act. The creation of a TIF District bestows a number of powers upon a municipality. The most important of those powers is the ability to capture the real estate tax “increment”. This “increment” is the tax generated as the result of an increase in the assessed value of the real property within a TIF District over and above the assessed valuation when the TIF District was created (the “base year”). The taxes resulting from the assessed valuation of the base year continue to be returned to the various taxing Districts as if the TIF District did not exist while the increment, i.e., the increase, in taxes over those in the base year is all captured by the municipality which created the TIF District. The municipality that creates a TIF District is permitted to expend the increment to pay for or to reimburse the payment of eligible redevelopment costs (“redevelopment costs”) as permitted by the TIF Act. The power of TIF is that it permits the municipality to utilize not only

its own property taxes to stimulate development and redevelopment, but also the property taxes of all the taxing bodies without their direct consent.

In order to create a TIF District, several important factors must be considered. First, the property located within the proposed District must meet certain eligibility criteria. Second, the municipality must determine that the proposed redevelopment project area as a whole has not been subject to growth and development through investment by private enterprise and would not reasonably be anticipated to with developed without TIF. (65 ILCS 5/11-74.4-3(n)) This is commonly referred to as the “but for” test. The First District Appellate Court provides a good discussion concerning the “but for” test in Board of Education of Community High School District No. 218 vs. Village of Robbins, 327 Ill.App.3d 599, 765 N.E.2d 449, 262 Ill. Dec. 312 (1st Dist. 2001). The municipality must also find that the proposed redevelopment plan complies with its comprehensive plan. (65 ILCS 5/11-74/4-3(n)(J)(2))

The municipality may become interested in establishing a TIF either through its own initiative or after being approached by a developer with a particular project and property in mind. A TIF proposal, no matter how initiated, will trigger a multi-level analysis to determine whether TIF is the correct tool for the circumstances.

Among the considerations for a municipality are whether the property qualifies for TIF designation, whether the “but for” test is satisfied and whether the TIF and the project are in the best interest of the community.

TIF ELIGIBILITY

In order to qualify as a TIF, the area must consist of at least 1 ½ acres and must satisfy the eligibility criteria of one of the following categories. The general categories for TIF qualifications include:

A. IMPROVED BLIGHTED

In order to qualify a proposed TIF as an “improved blighted” area, at least 5 of the

following factors must be present and documented to a meaningful extent. The factors must be reasonably distributed throughout the area extent. The factors are dilapidation; obsolescence; deterioration; presence of structures below minimum code standards; illegal use of individual structures; excessive vacancies; lack of ventilation, light or sanitary facilities; inadequate utilities; excessive land coverage and overcrowding of structures and community facilities; deleterious land use or layout; environmental clean-up; lack of community planning; or a decline in assessed valuation. Each of these factors has more definition in the TIF Act. (65 ILCS 5/11-74.3(a)(1)(A-M)) Additionally, the First District Appellate Court opinion in *Capital Fitness of Arlington Heights Inc. vs. Village of Arlington Heights* contains good discussion about many of these factors including the distinction of the lag in tax factor as it relates to the distribution in the area as a whole.

B. VACANT PROPERTY

If property is “vacant” as defined by the TIF Act, to qualify the proposed area must be impaired by at least two of the following factors present to a meaningful extent and reasonably distributed throughout the area: Obsolete platting; diversity of ownership; tax delinquencies; deterioration of structures or improvements on neighboring adjacent areas; environmental clean up or decline in the assessed valuation. (65 ILCS 5/11-74.4-3(2)(A-F)) As an alternative, if any one of the following factors is present to a meaningful extent and reasonably distributed through the area, the vacant property is eligible for TIF designation: the area consists of one or more unused quarries, mines or strip mine ponds; the area consists of unused rail yards, rail tracks or railroad rights of way; the area is subject to chronic flooding or contributes to flooding of other properties or the area qualified as blighted improved property immediately prior to become vacant. (65 ILCS 5/11-74.4-3(3)(A, B, C, D and F))

C. CONSERVATION AREA

Recognizing the importance of redevelopment prior to an area actually becoming

blighted, the legislature created a classification of TIF known as a “conservation area”. Property may qualify as a conservation area if fifty percent (50%) or more of the structures in the proposed area are at least 35 years of age and at least three of the criteria set forth in the Improved Blighted category are present. (65 ILCS 5/11-74.4-3(b))

D. INDUSTRIAL PARK CONSERVATION

A vacant area may be designated an “industrial park conservation area” TIF if it is located within 1 ½ mile of a labor surplus municipality (as defined by the TIF Act), the area is zoned industrial and includes vacant land suitable for use as an industrial park and a blighted area or a conservation area are contiguous to the proposed TIF. (65 ILCS 5/11-74.4-3(d))

E. INTERMODAL TERMINAL FACILITY

An area may be designated as a “Intermodal” TIF if it (i) does not include any existing intermodal terminal facility as defined by the TIF Act; (ii) consists of at least 150 acres but not more than 2 square miles (exclusive of lakes and waterways); (iii) has at least one class one railroad right-of-way either on the property or within one-quarter mile; and (iv) has no boundary limit further than 3 miles from the right-of-way. A property is deemed to be blighted and may be designated as a TIF if the proposed area meets these criteria. (65 ILCS 5/11-74.4-3.1)

F. STAR LINE TIF.

An area may be designed a TIF without demonstrating blight if the area is within a one-half mile radius of an existing or proposed Regional Transportation Suburban Transit Access Route (Star Line) and the Joint Review Board provides unanimous consent. (65 ILCS 5/11-74.4(p-1))

PRELIMINARY CONSIDERATIONS

Before establishing a TIF District, the municipality must satisfy a number of procedural requirements of the TIF Act. These requirements include creating an interested parties registry, conducting a public hearing, preparing a redevelopment plan and project, preparing an eligibility

report, convening a Joint Review Board consisting of representatives from certain overlapping taxing districts, and in some instances preparing a housing impact study as well as convening a public meeting. The TIF Act also requires several notices, both by mail and by publication.

In order to insure compliance with all of the procedural requirements and to provide support for the municipal fundings required in conjunction with establishing a TIF District, most municipalities assemble an experienced TIF Team. This team will often be lead by an experienced and respected TIF consultant who can assist the municipality in determining whether the proposed site is eligible for designation TIF and determining whether the “but for” test is satisfied. Additionally, the TIF consultant will be an extremely valuable resource in assessing the viability of the proposed TIF and in negotiating a business deal with prospective developers. Others on the TIF Team should include an attorney experienced in TIF related matters as well as the municipal staff and often land planners, engineers and other advisors. When retaining consultants to assist the municipality in the establishment of a TIF District, it is important to note that the TIF Act prohibits paying for professional services which are based on a percentage of the tax increment collected. (65 ILCS 5/11-74.4-3(q)(1)) Additionally, lobbying expenses cannot be paid for utilizing tax increment. Id.

THE INITIAL PROCESS

The TIF process is generally commenced by the adoption of an ordinance or resolution calling for a feasibility study. This resolution or ordinance is not mandatory unless a housing impact study is required for the particular project. A feasibility study is a preliminary report to assist in determining whether TIF is appropriate for the proposed area. The TIF Act provides for minimum requirements to be contained in the ordinance or resolution and requires that after adoption it must be sent to all taxing districts that would be affected by the TIF designation. (65 ILCS 5/11-74.4-4.1)

The municipality must create an interested parties registry. (65 ILCS 5/11-74.4-4.2)

Interested persons and entities which register in the interested parties registry are entitled to notices and certain information as required by the TIF Act.

In instances when the proposed area includes 75 or more inhabited residential units or the project would result in displacement of 10 or more inhabited residential units, a housing impact study will be required to determine the extent and type of impact the project might have on the areas residents unless the municipality certifies that such displacement would not occur. (65 ILCS 5/1-74.4-(3)(n))

The municipality must prepare a redevelopment plan and project for the proposed area. This “redevelopment plan” must contain all the requirements of the TIF Act (65 ILCS 11-74.4-3(n)) and is generally designed to demonstrate how and to what extent the TIF designation will enhance the proposed area and to establish a budget for redevelopment costs.

After a draft redevelopment plan has been on file with the municipality, a public hearing must be conducted to receive input from the public and other taxing districts regarding the proposed redevelopment plan and TIF designation. (65 ILCS 5/11-74.4-5(a)) The public hearing must be convened after adoption of an ordinance calling for such hearing and other notices. Id. The municipality must also organize and convene a “Joint Review Board”. (65 ILCS 5/11-74.4-5(b)) The Joint Review Board consists of representatives of many of the affected taxing districts and a public member. After reviewing the proposed redevelopment plan and eligibility criteria, the Joint Review Board is called upon to give its recommendation to the municipality as to whether the redevelopment plan should be approved and the area designated as a TIF. While the Joint Review Board has only advisory powers (except in the case of Stap Line TIFs as noted above), failure to receive a positive recommendation from the board will require that the municipality approve the TIF by a super-majority. Id.

Every step along the way in the TIF process requires certain notices, publications and procedures which must be adhered to or risk a TIF designation rendered invalid by a Court.

These notice requirements and pre-requisites are all set forth in detail in the TIF Act.

If a municipality determines to create the TIF district, it may do so by adopting ordinances which have been introduced 14 to 90 days after concluding the public hearing. TIF will be valid for a period of up to 23 years. While a TIF district may be extended by action of the General Assembly it is the current practice of the General Assembly that TIF extensions will not be considered without the written support of all affected taxing bodies.

TIF POWERS

The municipality which adopts a TIF will then enjoy the numerous powers which are provided by law including entering into contracts with property owners and others, eminent domain, demolition, renovations, incurring redevelopment project costs and others. (65 ILCS 5/11-74.4-4)

CONFLICTS OF INTEREST AND DISCLOSURES

The TIF Act prohibits certain conflicts of interests and also requires certain disclosures which must be considered by the municipality contemplating the establishment of a TIF. (65 ILCS 5/11-74.4-4(n))

The conflict provisions apply to (i) members of the corporate authority; (ii) members of an optional commission established pursuant to the TIF Act; and (iii) employees and consultants of the Village who are involved in the planning and preparation of a redevelopment plan or proposed redevelopment project area of the municipality who owns or controls an interest, whether direct or indirect, in any property located within an existing or proposed redevelopment project area (TIF).

Any such interest must be disclosed in writing to the municipal clerk and if the interest is disposed of, the individual must disclose the dates, terms and disposition of any such interest. When such a disclosure is made, the corporate authority must acknowledge the disclosure and enter the disclosure upon the minute book of the corporate authority.

The individual holding such an interest shall (i) refrain from any further official involvement in regard to such redevelopment plan, project or area; (ii) refrain from voting on any matter pertaining to the redevelopment plan, project or area; and (iii) refrain from communicating with members of the corporate authorities, commission or employees concerning any matter pertaining to the redevelopment plan, project or area.

The TIF Act also prohibits acquiring interests which are prohibited. The TIF Act provides that no member of the corporate authority or employee involved in the planning and preparation of the plan or project area shall acquire either a direct or indirect interest in any existing or proposed redevelopment project area after the person obtains actual knowledge of the plan, project or area or the first notice of public hearing is provided according to the TIF Act.

Certain exceptions to the conflicts provisions are available for members of the corporate authority who own or lease residential property. The Act should be consulted to determine whether any particular set of facts creates an exception.

The municipality should proactively attempt to identify prohibited conflicts and work to be sure that proper disclosures are made. Each TIF proposed will present a different set of challenges with respect to conflicts. The number of potential conflicts obviously increases or decreases depending upon the geographic area covered by the proposed TIF.

REDEVELOPMENT PROJECT COSTS

As previously stated, the TIF designation's greatest strength is the ability to capture the tax increment. Each county is required to transfer the increment when collected to the municipality which will then deposit the funds into the TIF account. The municipality is then empowered to spend money from the TIF account to pay or reimburse for what are defined as "redevelopment project costs" under the TIF Act. These costs are defined by the TIF Act (65 ILCS 5/11-74.4-3(g)). Most typical among the costs are costs of studies; surveys; plans; architectural; engineering; legal; financial planning and other services; administrative costs;

marketing costs; costs for property assembly; property preparation; rehabilitation, reconstruction and repair of remodeling of buildings; costs of public works; job training; financing; taxing district capital costs related to the TIF; repayment to schools and library districts and for certain public buildings. Redevelopment project costs are generally not intended to financing private construction of building or structures. The redevelopment project costs available in a Star Line TIF are limited to costs associated with the proposed or existing Star Line stations. (65 ILCS 5/11-74.4-3(q-1))

REDEVELOPMENT AGREEMENTS

Redevelopment agreements are the primary mechanism for documenting the business deal between the municipality and the developer with regard to TIF related matters. At the heart of most redevelopment agreements is the “incentive” provided to the developer through the sharing of tax increment. While the redevelopment agreement is the document to memorialize the business deal, the due diligence leading up to the agreement is critical. Before entering into a redevelopment agreement the municipality must consider a number of issues including the level of increment available to developer, whether the project is good for the community, whether the project furthers the redevelopment plan, how the project will be financed, and whether bond should be issued to help finance redevelopment costs.

Careful consideration should be given to the amount of increment that is made available for the project. The goal of the municipality should be to provide a sufficient level of increment so as to make the project viable and profitable to the developer. Without profit, the project will not work, however, the municipality should take care as to how much incentive is necessary in order to provide the developer with a reasonable rate of return on its investment. This analysis will require a good understanding of the project finances.

The redevelopment agreement should provide a clean and concise description of what the developer must do to be eligible for the TIF incentive, what the amount of the incentive will be

and the source of payment. Most often the municipality's liability for payment is limited to TIF increment actually received from the county. Often times this revenue is further restricted to the increment generated from the particular project rather than from the TIF as a whole.

In addition to the amount and source of funds available, the redevelopment agreement should include a number of requirements including compliance with applicable laws, such as the prevailing wage act, equal opportunity and fair employment laws and other laws and ordinances. Further, the redevelopment agreement should provide for the maintenance and availability of records and supporting documentation, procedures for what documents are provided and certificates must be made prior to disbursement of funds to the developer, indemnification to the municipality, project insurance and provisions for what happens if the project for some reason fails and other important considerations.

A redevelopment agreement should be used in all instances where TIF funds are paid out to a developer. No matter how small the project, the municipality faces risk when public funds are used to support a project and the redevelopment agreement is an excellent tool to minimize the risk and lay the groundwork for a successful project.

ANNUAL REPORTING

Once established, all TIF districts are subject to annual reporting requirements. (65 ILCS 5/11-74.4-5(d)) The TIF Act provides for specific information which must be provided annually prior to the meeting of the Joint Review Board. The required information must be submitted to all taxing districts overlapping the TIF and the State Comptroller. Id.

CONCLUSION

The establishment of a TIF District is an important step for a municipality, a step which should not be taken without careful analysis and consideration. The municipality as the steward of the tax funds for all the taxing districts should, and is in fact required to, consider the impact of the project upon other districts. Good communications between the taxing districts from the

beginning of the process throughout the life of the TIF will greatly increase the likelihood of success in carrying out the objectives of the redevelopment plan.