Tax Increment Financing
Frequently Asked Questions

What is TIF?

Tax Increment Financing (TIF) is an economic development tool designed to foster the types of development Vermont has been encouraging for years, and in the places we want it to occur – such as downtowns, industrial parks, and compact village centers. TIF projects catalyze private development by removing key infrastructure barriers, using incremental tax revenues to cover the cost.

What is the purpose of TIF?

Every state that has a TIF program has its own goals and objectives for TIF. In Vermont the TIF enabling statute (Title 2 VSA, Chapter 53, Sub-chapter 5, § 1893) says:

> The purpose of tax increment financing districts is to provide revenues for improvements that serve the district and related costs, which will stimulate development or redevelopment within the district, provide for employment opportunities, improve and broaden the tax base, or enhance the general economic vitality of the municipality, the region, or the State.

Before being authorized to use incremental education taxes, a proposed TIF district goes through a rigorous review by the Vermont Economic Progress Council (VEPC), including an analysis of purpose. The project criteria examine such items as that the municipality doesn't have the financial capacity to make the infrastructure investments on its own, that the district will foster new affordable housing and/or new commercial or business investment, create new quality jobs, clean up brownfield contamination, and/or enhance transportation including multi-modal transportation. Through this review, the District must be found to show consistency with the statutory purpose.

How does it work?

The basic concept is that a Tax Increment Financing (TIF) district is used to foster private development that would not have otherwise occurred "but for" the District.

To implement a District, a limited geographic area is defined in which the municipality believes there is potential for development to occur, but in which there are public infrastructure barriers that make private real estate investment difficult or impossible. Specific boundaries are selected and define the "TIF district."

Depending on the issues in each specific location in the district, the infrastructure barriers could include insufficient or deteriorating water or wastewater utilities, inadequate parking, substandard streetscape amenities, stormwater management issues, and similar limitations. In Vermont, TIF is also used to clean up contaminated brownfield properties and otherwise prepare sites for development.

Once the district is established, the host municipality works with property owners and developers to identify specific private developments that could be supported or incentivized by public infrastructure investments.

How does the municipality pay for a TIF infrastructure project?

A municipality has a ten-year window to incur debt (typically through a bond vote held during a general election or special election) for the selected infrastructure projects. For twenty years from the time the first debt is issued, the municipality may retain the increment. The “life of the district” runs from the time the municipal body approves the TIF District Plan, which is anticipated to be in January 2025, through the repayment of all debt accrued to pay for that same infrastructure projects.

How does the municipality pay for the public infrastructure investments?

At the time a TIF district is established, the total taxable grand list value of the properties in the district is calculated. This is called the “Original Taxable Value” or OTV. During the life of the TIF district, all taxes generated by the OTV continue to be disbursed to the funds they have otherwise gone to – principally the municipality’s general fund and the state education fund. Not a nickel of those dollars is taken away.

New incremental taxes generated by the increased grand list value created by the new private development are disbursed to the TIF fund, but not all the new taxes. The percentage shares vary from district to district; however, for TIF districts approved under current State statute, not less than 85% of the municipal increment and not more than 70% of the education increment may be retained by the TIF fund.

These new incremental taxes in the TIF fund are used to pay the accrued debt on the money the municipality borrowed via the voted on and approved bond initiatives. The money in the TIF fund also pays for costs to plan and manage the construction of the public infrastructure projects, and the costs to set up and operate the TIF district. These are referred to as “Related Costs”.

Is the public invited to participate?

By law, establishing a TIF district and issuing TIF debt requires substantial public participation. Public hearings are required before every application to VEPC for initial approval or for a “substantial change” to a TIF district. Public hearings and public notices are also required before each bond vote.

Can you give a hypothetical TIF project example?

Suppose we are looking at one individual property in a TIF district rather than the district as a whole. Let's say that property is currently worth $1 million and pays $10,000 per year in combined local and education property taxes, with $3,500 going to the municipality and $6,500 to the state education fund.

Now imagine the owner redevelops the property and its assessed value increases to $2 million and it now pays $20,000 per year in taxes (for this example, we assume tax rates have not increased). The taxes on the original $1 million value (the OTV) continue to go where they did before. Thus, those funds still receive their original shares of the OTV's $10,000 taxes: $3,500 to the municipality and $6,500 to the state education fund.

But the taxes from the new incremental value of $1 million are handled differently. Of the new $3,500 in municipal taxes, not less than 85% must go to the TIF fund, meaning not less than $2,975 goes to the TIF fund and not more than 15% ($525) goes to the municipality's general fund (a municipality can choose to send up to 100% of the new taxes to the TIF fund). Of the $6,500 in new education taxes, not more than 70% or $4,550 may go to the TIF fund and not less than 30% ($1,950) must go to the education fund.

This results in the TIF fund having $2,975 municipal + $4,550 education taxes = $7,525 available annually to pay debt service. At the same time the municipality's general fund which previously received $3,500, now gets $4,025 ($3,500 on the OTV + $525 increment) and the state's education fund which previously received $6,500 now gets $8,450 ($6,500 on the OTV + $1,950 on the increment).

Now think of that concept across an entire TIF district with perhaps dozens of properties. Each time any of those properties in the TIF district is redeveloped and the taxable assessed value goes up, the taxes on the OTV of that building and the entire district continue to go where they always have, whereas the newly generated incremental taxes are split three ways based on the percentages in that particular district: to the TIF fund, the municipality's general fund and the State education fund.

Is TIF "free money?"

No. TIF uses tax dollars being paid by property owners. However, the concept is that "but for" the public investments being made, the private development would not have occurred, or would have occurred in a smaller or less desirable manner. Accordingly, most or even all of these new incremental taxes would not have existed without the public investments made possible by the TIF district.

Does TIF take money away from the education fund?

TIF uses only new incremental tax revenue. The core idea is that “but for” the use of TIF to make public investments, the private development would not have occurred, and the tax dollars being used for TIF would not have existed. Therefore, the education fund would not have had those taxes in the first place. In fact, the most recent annual report regarding TIF, issued annually by the Vermont Economic Progress Council (VEPC), shows that through June 30, 2020 TIF districts around Vermont had contributed over $5 million from new incremental revenues to the state education fund.

What kinds of public improvements are typical in TIF districts?

Sometimes the public improvements are specific to an individual property or private project. Perhaps the site is a brownfield that needs to be cleaned up, or existing infrastructure needs to be relocated to open the site for redevelopment, or more public parking is needed to support the project.

Other times, general enhancements in the District make the District as a whole more attractive for private investment. Such general improvements might include streetscape enhancements, providing sanitary sewer service to an area, or making street modifications that enhance traffic flow or make multi-modal transportation more attractive.

Does TIF offer a reduction in taxes for property owners or developers in a TIF District?

No. Tax Increment Financing does not inherently reduce the tax rate for any property owner, inside or outside the District. Property owners are permitted to apply for municipal tax stabilization of their property value through the proper City tax stabilization procedures. This would not reduce their tax rate. However, the amount of incremental taxes available to invest in infrastructure would be reduced, which is why each project is analyzed by a City team with each specific stack of funding sources.

Is TIF a hand-out to developers?

No. In Vermont, a municipality is not permitted to use TIF money to invest in a private development. TIF funds can only be used for public infrastructure, brownfield cleanup, or site preparation that supports private development, as defined in the TIF statute.

Does creation of a TIF district raise property taxes for taxpayers who are not improving their properties?

No. In a TIF district, like any other area, property taxes increase for properties that make improvements, thus increasing that property’s assessed value. Regardless of the creation of a TIF District, a municipality has regular property reappraisals that affect individual property values and have votes for budgets that can affect the tax rate.

Will the municipality collect more taxes as a result of reappraisal?

No, the reappraisal does not result in more tax revenue to the City. The municipality can only collect more taxes through voter approval of the proposed budget. A reappraisal does not increase or decrease tax revenue; it only redistributes the total tax burden more fairly based on the indicated market value of properties. Property values change over time at different rates for properties in different locations and property types. In general, when there is an overall increase in the total grand list because of a reappraisal, the municipal tax rate adjusts downward proportionately.

Will I pay higher or lower taxes after the reappraisal?

Your taxes may go up or down or stay the same; it won't be the same for everyone. The reason being that the City tax rate will go down as the total value of the grand list goes up. It is assumed that the reappraisal will raise all property values in the grand list, in order to reflect current real estate values. But that doesn't necessarily change the City budget, which is a separate item considered by voters on Town Meeting Day. As grand list values increase, and if the City budget stays relatively the same, then a lower tax rate will be used to raise the relatively same amount of tax revenues.

How does the existence of a TIF District affect the reappraisal?

The tax rate will not decrease as much as it would without a TIF District. The revenue needed for the municipal budget will come from the existing tax base within the TIF District and the new tax base for the rest of the City. Because the tax base used to calculate the new tax rate will not include the increase of the properties within the District, there will not be as much revenue generated and the tax rate will not decrease as much. Of note, however, only 85% of the incremental municipal tax revenue goes to the TIF Fund; 15% will go to the General Fund, thereby offsetting some of the lost revenue after the reappraisal and also moderating future tax rate increases. And the benefit of the TIF District is strong: the incremental tax revenue within the District will be used to invest in public infrastructure to catalyze more private development, thereby growing the Grand List for the long term.

What if there is not enough revenue in the TIF fund to pay the debt service on the TIF bonds?

A municipality pledges its full faith and credit for a TIF bond. That means that if there is not enough TIF revenue to pay the debt, the general fund must pay it. There are numerous ways a municipality can protect itself from that.

Frequently, a municipality enters into one or more contractual agreements with developer(s), known as a development agreement, in which the developer commits to doing a development and the municipality agrees to make the needed public investments. This may provide protections for the municipality, such as a minimum agreed assessed tax value for the developer's project that is sufficient to generate the necessary incremental taxes.

A development agreement might also provide that the municipality will not commence its infrastructure improvements until the developer has closed on their financing and entered into a binding construction contract for their project.

To note, a TIF district not having enough incremental tax revenue in its early years is common because the private developments often take a few years to hit the "tax rolls," which only begins to generate the new incremental taxes at that time. A well-planned TIF district should anticipate this phenomenon and there are a range of ways a municipality can fund the early cash flow deficit and repay those costs once the TIF revenue grows.
While there are no guarantees, the track record of TIF in Vermont is excellent. All eight currently active Vermont TIF districts are fully paying their costs, including debt service.

Can you provide more about the experience in Vermont regarding TIF?

Experience shows that the most successful TIF districts are ones in which the municipality is proactive. Simply setting up a TIF district and waiting for things to happen rarely accomplishes much.

Being proactive means having an ongoing program to market the district and the availability of TIF to property owners and developers. Being proactive also means identifying underutilized properties in the district and actively working to negotiate agreements to get the property redeveloped, including what the municipality's associated infrastructure investment will be for each respectively. Funding up-front feasibility studies for housing, or a hotel, or other uses are also other means of being proactive, and in some cases, has involved the municipality purchasing properties, paying to demolish deteriorating buildings, remediating contamination issues (i.e. accomplishing any needed brownfield cleanup), and otherwise preparing a property for development. With that work done, the municipality then sells the properties to developers, typically for less than the municipality's full cost, and sometimes for as little as one dollar, contingent on the developer promptly getting construction of a new project underway. TIF can be used to pay for all these types of costs that the municipality may incur.

And the results can be dramatic. For example, the Town of Hartford established a TIF district in its downtown in 2011 with an OTV of about $31.8 million. Ten years later the taxable grand list value in their TIF district had grown to over $57.9 million, an increase of more than 80%!

The City of St. Albans created its downtown TIF district in 2012, with an OTV of $123 million, which has grown to over $180 million, an increase of nearly 50%.

Both communities were proactive. They did not wait for developers to come to them. They went out and actively made projects happen.

What happens at the end of the life of a TIF district?

A TIF district ends when all TIF debt is paid. Thereafter, the taxes that had been used to pay for the debt go to the general fund and education fund for their usual purposes. If there is a surplus in the TIF fund at the end, that surplus is distributed to the general fund and education fund in direct proportion to the amounts that came from those tax sources.

What is the difference between Project Phases and Project Tiers?

When developing a TIF Master Plan, the Vermont Economic Progress Council (VEPC) requires municipalities to identify several redevelopment projects across the district. In that work, the projects are classified by Tier 1, 2, and 3. Tier 1 are the most likely projects expected to commence in the near future. Tier 2 includes properties that have owner interest or investor interest in pursuing the development potential of the buildings and/or land located in the proposed TIF District. These Tier Two projects can possibly move forward independent of other development initiatives but will certainly benefit from the economic momentum created by the Tier 1 projects. Tier 3 includes properties that have development potential identified within the planned vision for Rutland City, and could have infrastructure needs within the ten-year debt window.

“Project phases” simply refers to the sequencing and timing of infrastructure. In some cases, the investment is sufficiently complex or costly and needs to be broken out.

Why is the Lynda Lee site considered a “Tier I” project?

The redevelopment of the abandoned factory is a top priority for the City given the building’s significant deterioration and ongoing safety concerns, as well as the prime locational opportunity it presents. Fortunately, an interested developer has conducted due diligence and land planning to assess both the challenges and opportunities of the site. With the availability of TIF and other funding sources supporting public-private partnerships, the development of the Lynda Lee site is more viable than it has ever been in its decades of vacancy and deterioration. Plans for the private investment and the municipal infrastructure are evolving and will require further review and approval from the Board of Aldermen and VEPC before there is a public vote for any debt. The TIF District Plan sets the intention for construction to commence in 2026.