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Tax Incremental Financing Explained

I receive a lot of questions about Tax Incremental Financing (TIF). Citizens want to know what it is, how it works and whether it affects property taxes and public services.

TIF is a public financing tool created by state law that enables local governments to expand their tax base (the assessed value of all real property within the city) by investing in infrastructure and development costs for real estate development projects. The size of the tax base is extremely important to cities in Wisconsin including Milwaukee. To understand why, it is necessary to briefly discuss how Milwaukee prepares its annual budget, determines the property tax levy (the total amount of money raised through property taxes), and calculates each property owner's property tax bill.

The first step is to determine how much revenue will be generated from non-property tax sources. This includes state shared revenue, state/federal road aids, income from licenses and permits, payments in lieu of taxes such as the annual payment to the city from the Forrest County Potawatomi, fees for services (like the sewer maintenance fee, snow removal fee and solid waste fee), and fines and penalties.

The second step is to determine how much revenue the city needs to fund on-going operations and the delivery of city services such as police, fire, infrastructure maintenance, public health, the library, trash collection, snow plowing and debt service; and capital needs such as road and bridge reconstruction, sewer and water main replacement, major repairs to city buildings, and heavy vehicle purchases such as fire trucks, snow plows and garbage trucks. Ultimately the city comptroller certifies how much non property tax revenue will be available and the Common Council approves the total amount authorized to be spent on operations and capital projects.

Once these two numbers are determined (non-property tax revenue and the city budget) the amount of non-property tax revenue is subtracted from the budget. The difference is the property tax levy—the amount of money that will be raised from property taxes. This property tax levy is then divided by the assessed value of all non-tax exempt real estate in the city (tax exempt property is not included such as churches, most hospitals, most private educational institutions, etc.). This process generates the tax rate.

The actual property tax for each property is then calculated by multiplying the assessed value of each property by the property tax rate. The tax bill received by each property owner in the city contains the property tax for six units of government: City of Milwaukee, Milwaukee County, Milwaukee Public Schools, Milwaukee Area Technical College, Milwaukee Metropolitan Sewage District and the state forest fund.



As can be seen from this simplified description, the total tax base of the city is a critical component of the property tax rate, and the amount each property owner will pay. The bigger the total tax base, the lower the property tax rate will be assuming all other factors remain the same. In other words, growing the tax base is key to the city's financial health, its ability to fund city services and provide public infrastructure and keeping property taxes for each owner as low as possible.

Tax Incremental Financing enables the city to expand this tax base.

Here is how it works.

Take a piece of vacant or improved property in the city. That property has an assessed value. The property tax for that property is determined by multiplying the assessed value by the tax rate. At some point a developer or property owners approach the city with a plan to construct a new building or renovate an existing building on that property. The developer or property owner demonstrates to the city that this new building or renovation cannot be accomplished solely with private funds because of the blighted condition of the property or neighborhood or other factors. This is the "but for" test; namely, that the property improvement cannot occur without a public investment in the form of Tax Increment Financing. Keep in mind that the redevelopment plan may apply to a single property, or, in a more frequent scenario, multiple properties. The properties contained within the redevelopment plan comprise what is known as a Tax Incremental District, or TID.

The city then identifies how much public investment is required to enable the property improvement to occur. This public investment may involve public infrastructure improvements or covering a gap between the cost of the improvement and the amount of private funds available. This "gap financing" is in effect the "TIF budget".

The city then looks at the projected assessed value of the property upon completion of the property improvement and subtracts the assessed value that would exist if no improvement occurred. This difference is called the "value increment" or incremental tax base"—the additional tax base created by the improvement of the properties within the TID. Based on the anticipated tax rate for future years, the city then determines whether the city's investment will be repaid through the property taxes generated from the incremental tax base. If it will be repaid within 27 years, (the time specified in state law) the investment is deemed "financially feasible".

If the "but for" and "financial feasibility" tests are met, the city is legally entitled to make the investment under state law. When the city's investment is recouped, the incremental tax base is added to the overall city tax base. The tax base has been expanded.

The city has created 79 Tax Incremental Districts (the geographical area where the property improvement is planned to take place) over the last 35 years or so. Forty eight Tax Incremental Districts are open at this time. The remainder have been closed out meaning the TIF investment has been recouped. The total amount of incremental tax base added to the overall city tax base from these closed out TIDs is approximately \$1,163,953,280.00.

I have heard several misconceptions about Tax Incremental Financing. One misconception is that TIF reduces the property tax revenue available to the Milwaukee Area Technical College and the Milwaukee Public Schools. This is false. As described above, the revenue that needs to be raised by each government body is determined by that government body through the budget process. TIF does not reduce the revenue of any government body. It impacts the tax base—the value of property within the TID.

Another misconception is that Tax Incremental Financing causes everyone's property taxes to increase. Again this is false. As demonstrated above, each property owner's property tax bill is determined by multiplying the property's assessed value by the property tax rate. Tax Incremental Financing does not increase the tax rate and does not increase the assessed value of any property other than the property actually being improved within the Tax Incremental District. In fact, after the City recovers its investment, the increased tax base becomes available to reduce the tax rate for all the local taxing jurisdictions.

In summary, Tax Incremental Financing is a public financing tool created by state law that has been used by cities throughout Wisconsin to expand their tax base. Milwaukee has used this tool to expand the city's tax base and add significant value to the built environment of the city in the form of residential, commercial and industrial real estate developments that would not have occurred but for the use of this public financing tool. These developments in turn have created thousands of construction and permanent jobs, created thousands of new or renovated housing units, created thousands of square feet of new or renovated commercial and industrial space, created numerous public amenities and have revitalized blighted or underutilized areas of the city.

Tax Incremental Financing is our most important economic development tool. I am proud to have supported over \$290 Million in Tax Incremental Financing during my 11 years serving as your representative on the Common Council.

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