TIF Policy Discussion

Joint Review Board Meeting

Department of Planning & Community & Economic Development
August 26, 2013

Key Principles of Economic Development Committee

- Budget pressures makes attracting capital and facilitating net new construction vital
- Madison has been a responsible and conservative user of TIF
- Madison can continue to be prudent and attract additional development with strategic expansion of TIF

Value of higher construction rates compounds

Hypothetical implications of achieving various growth rates over time

Net New Construction Benchmark	2013 year revenue implication*	2017 revenue implication**
5.0 %	$ 6.4 million	$ 35.5 million
4.0 %	$ 5.1 million	$ 27.8 million
3.0 %	$ 3.9 million	$ 20.4 million
2.8 %	$ 3.6 million	$ 19.0 million
2.0 %	$ 2.6 million	$ 13.4 million
1.0 %	$ 1.3 million	$ 6.5 million
0.7 %	$ 1.0 million	$ 4.8 million

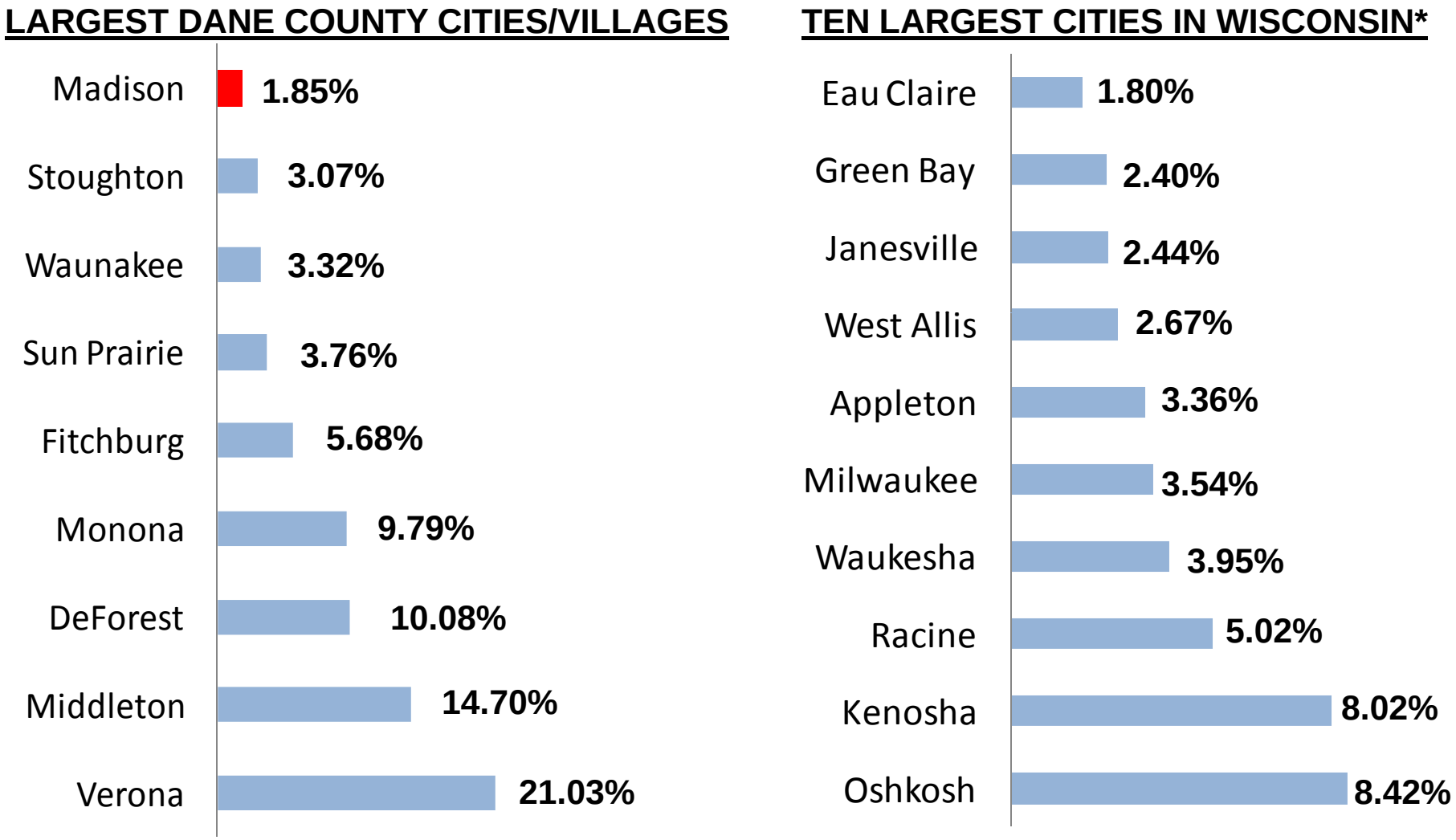
2013 budget deficit is approximately $11 million

* Assumes $128.4 million base levy; 2013 budget deficit less net new construction

** Assumes $128.4 million base levy; 5 years of net new construction at specified rate; does not account for other changes to levy

Madison has less property in TIDs than most cities

Percentage of Equalized Value in TIDs - 2012

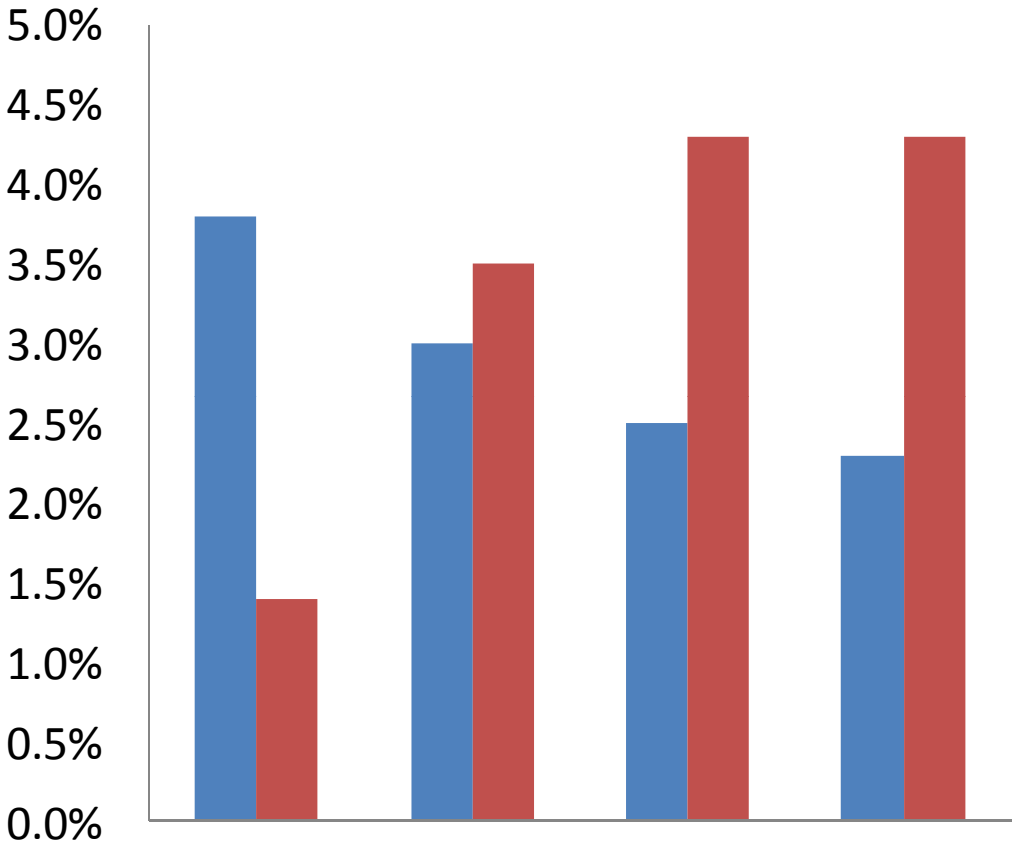


* Top eleven largest cities excluding Madison

Sources: Department of Revenue, analysis

Madison's relative use of TIF has declined

Share of Cumulative Wisconsin TIDs Created (1977-2011)



	1977-85	1986-95	1996-05	2006-11
Cumulative TIDs created	**369**	**833**	**1428**	**1783**
Madison TIDs	**14**	**25**	**36**	**41**

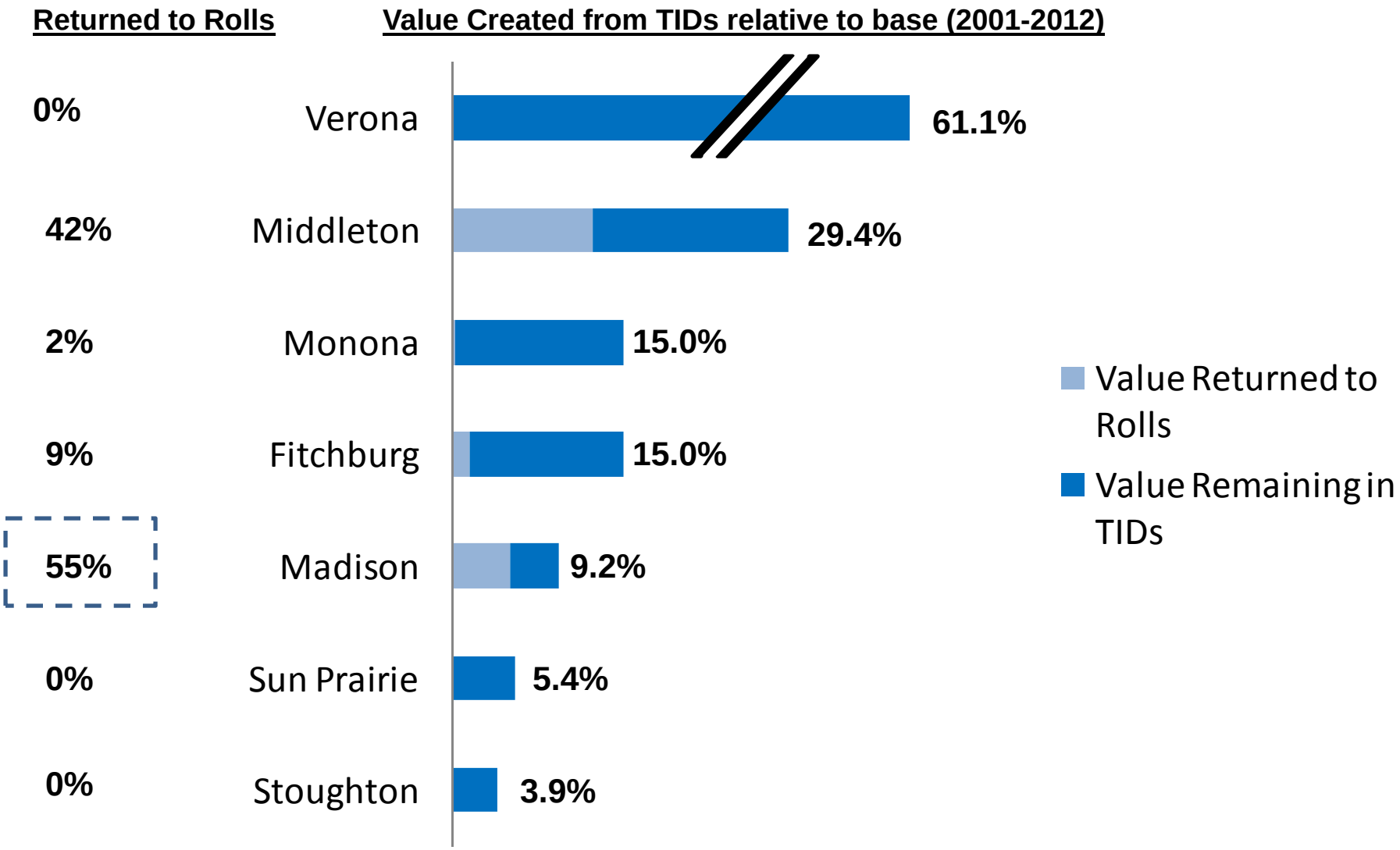
Madison was an early adopter of TIF but has seen its share of statewide TIDs decline

Some difference may be explained by size of TIDs (e.g., Milwaukee may have more single-purpose TIDs)

Sources: Department of Revenue, City of Madison, City of Milwaukee, Wisconsin Fiscal Bureau

...But less value relative to Madison's base

Tax Base Growth in and after TIDs (2001-2011) relative to 2001 base



Sources: Department of Revenue, analysis

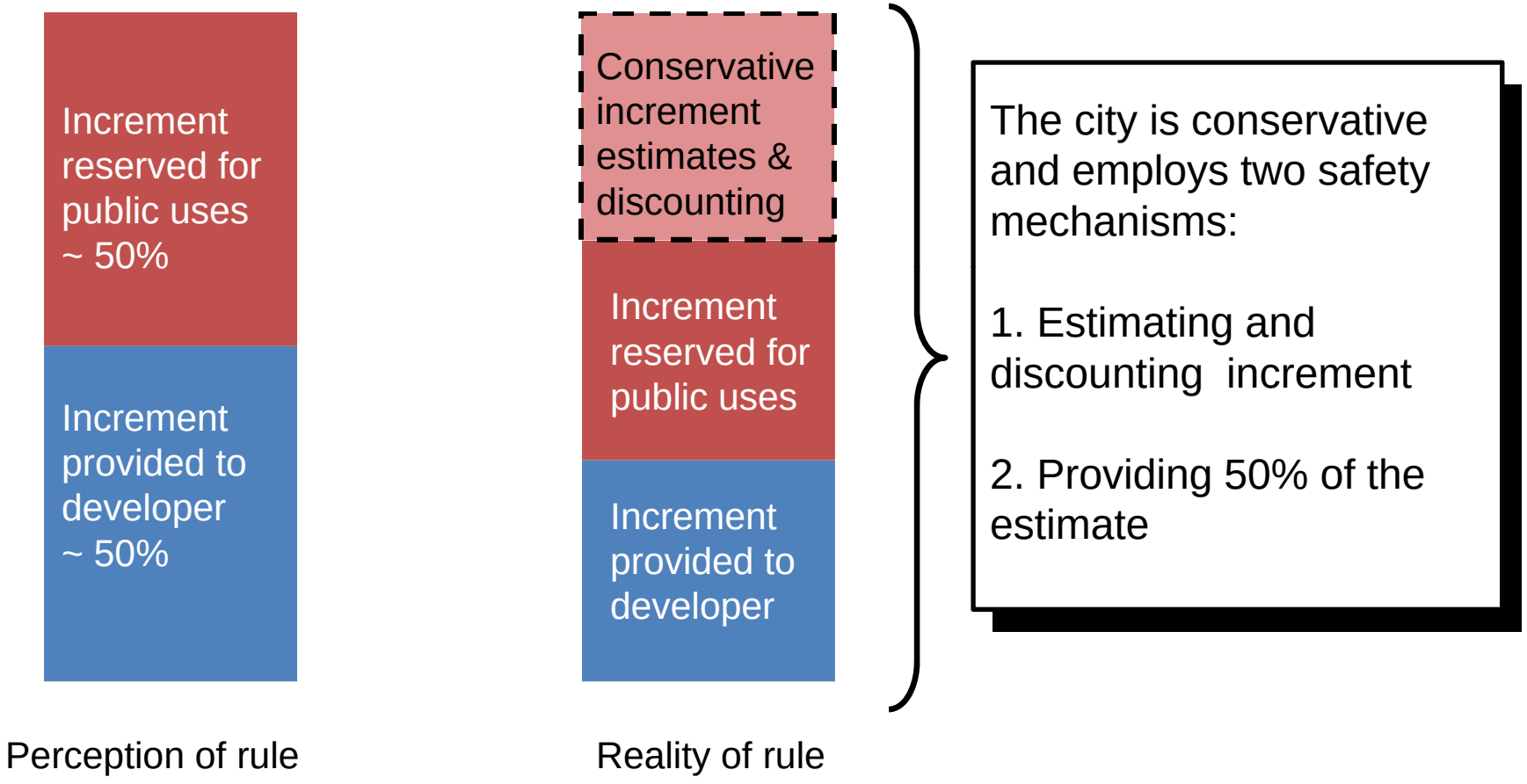
Current TIF Policy has produced positive results

- Approximately $1.5 billion of value created
- Investments of ~$100 million (approximately 14:1 leverage)
- TIF has built substantial infrastructure
- No failed or distressed districts
- Average TID closes in 12-13 years
- However, we have been a conservative user

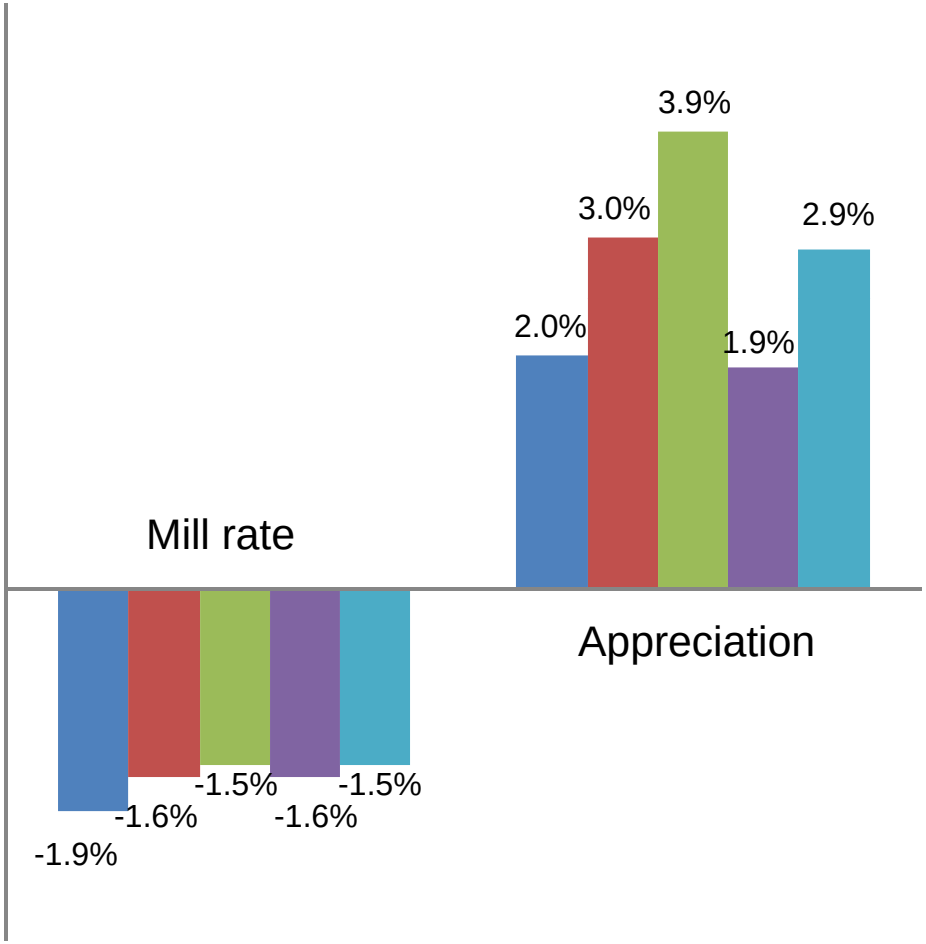
Major Policy Issues Addressed by EDC

1. 50% Rule
2. Equity Participation
3. Guarantees
4. Generator Requirement
5. Greenfield TIDs
6. Treatment of Employers
7. Affordable Housing
8. Conventional vs. Pay-As-You-Go Financing

The 50% Rule is misleading



City assumptions underestimate actual increment



SCENARIO

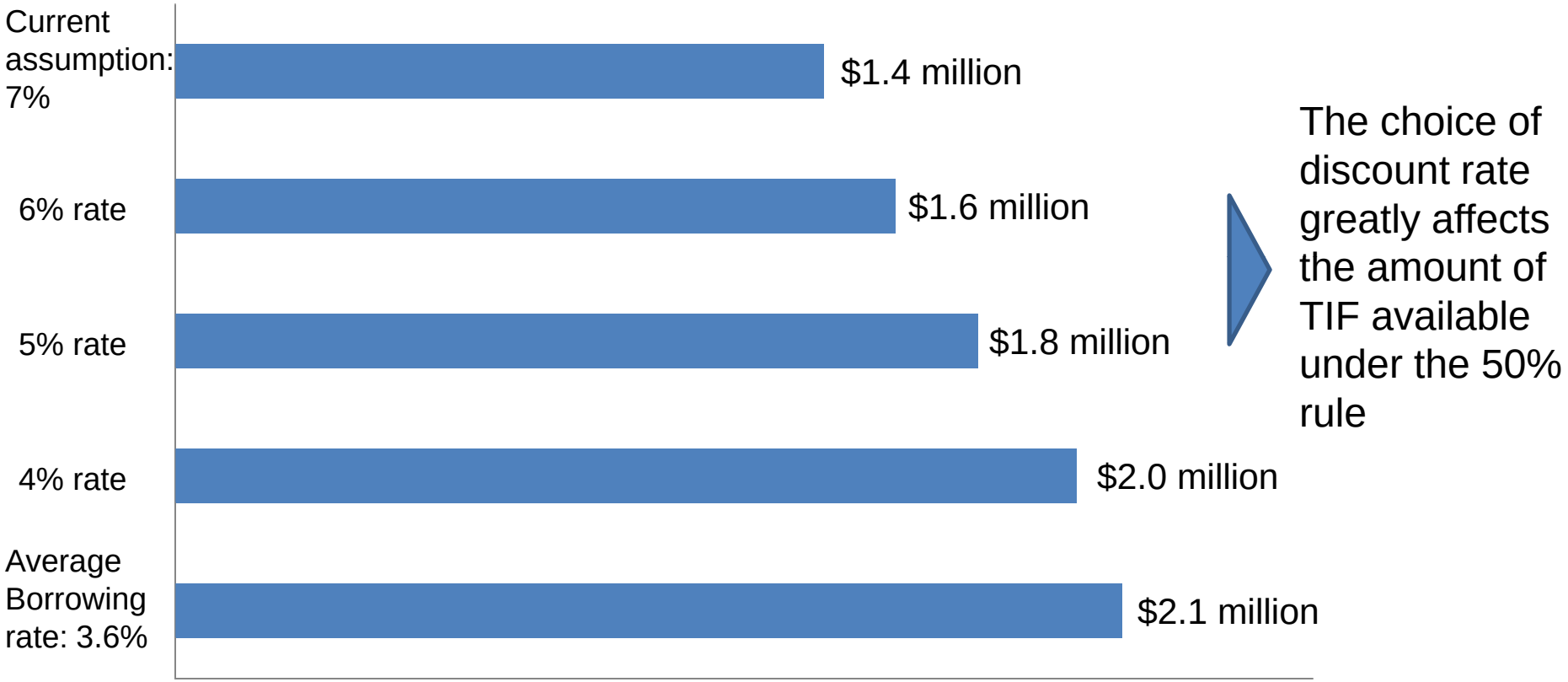
- Current Assumption
- Historical Data (98-11)
- Projected Scenario*
- Historical Data for Commercial (98-11)
- Projected Data for Commercial*

City's assumptions tend to underestimate TIF increment, though they are close for commercial property

* Projected scenario assumes real estate slump once every 27 years; Historical decline 98-09 = 3%

Available increment sensitive to discount rate

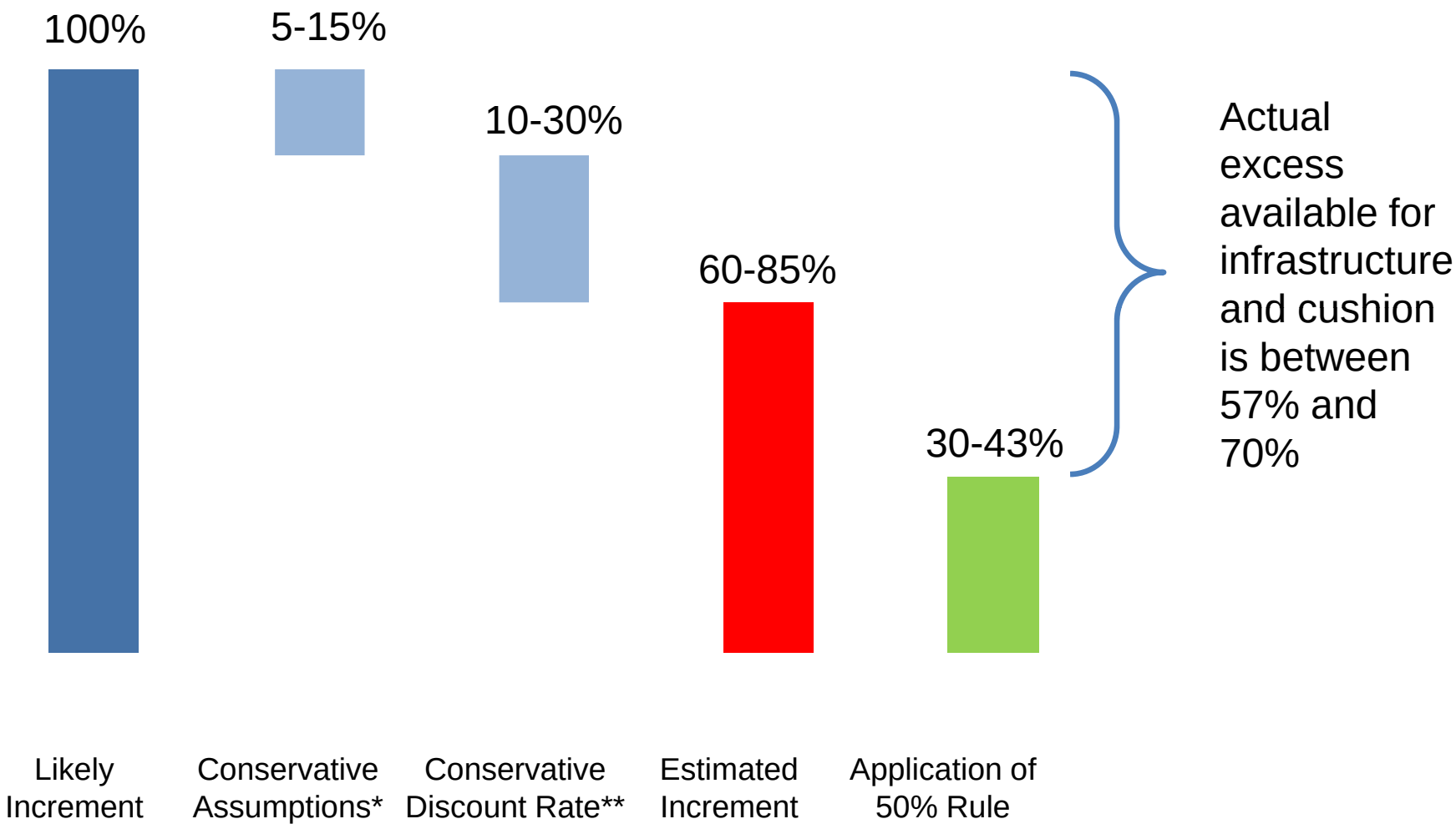
TIF Increment available for $10 million project at 50% of discounted increment



Note: The average cost of the city to borrow at taxable rates for TIF projects over the previous 6 years is 3.59%

Our actual “cushion” is greater than 50%

Percentage of Increment on hypothetical $10 million project



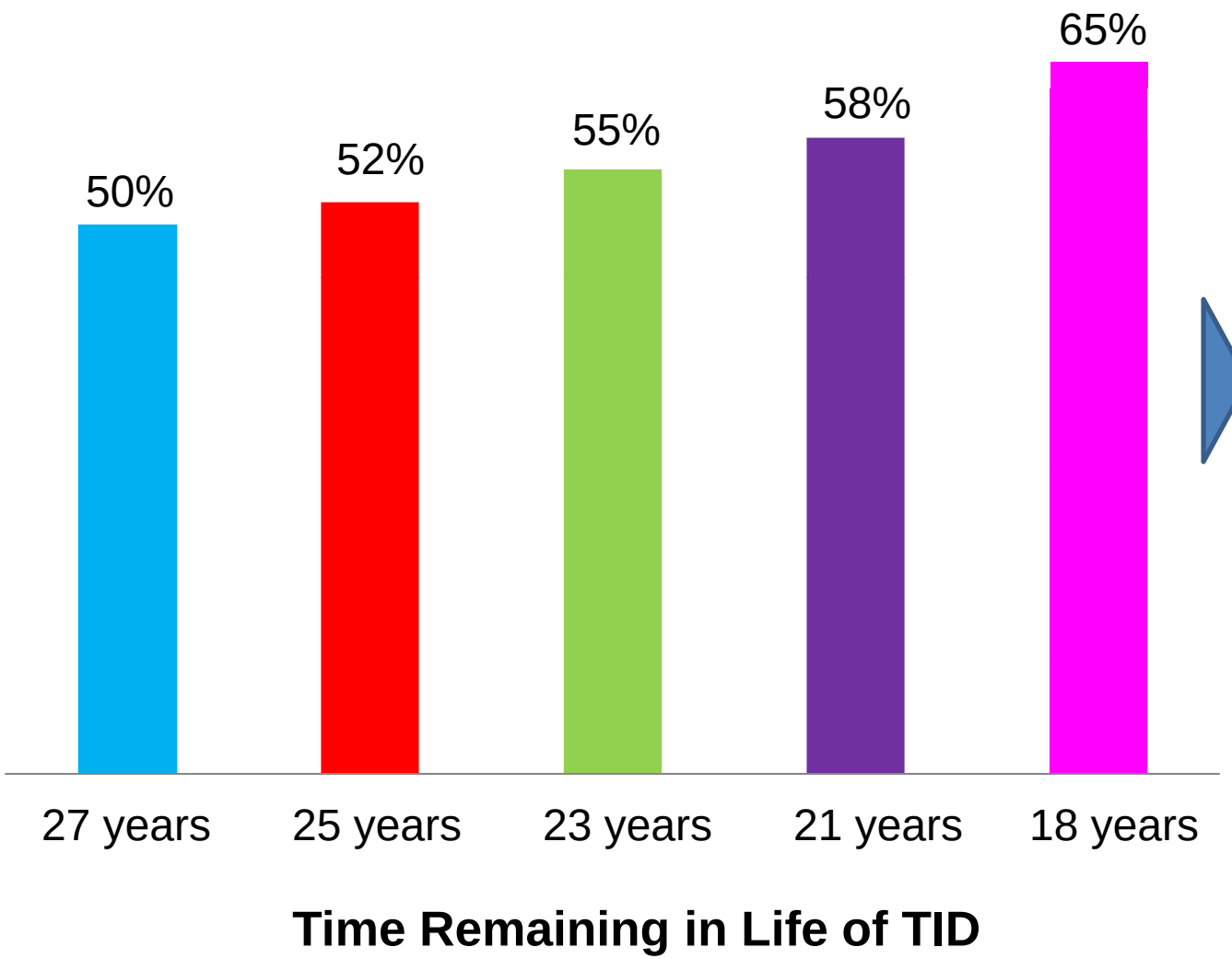
* Assumptions consider mill rates and appreciation for all classes and commercial only

** Sensitivity tested between 3.59% and 7%

Sources: City of Madison data; Department of Revenue; analysis

Lifespan of TIDs also creates issues for the 50% rule

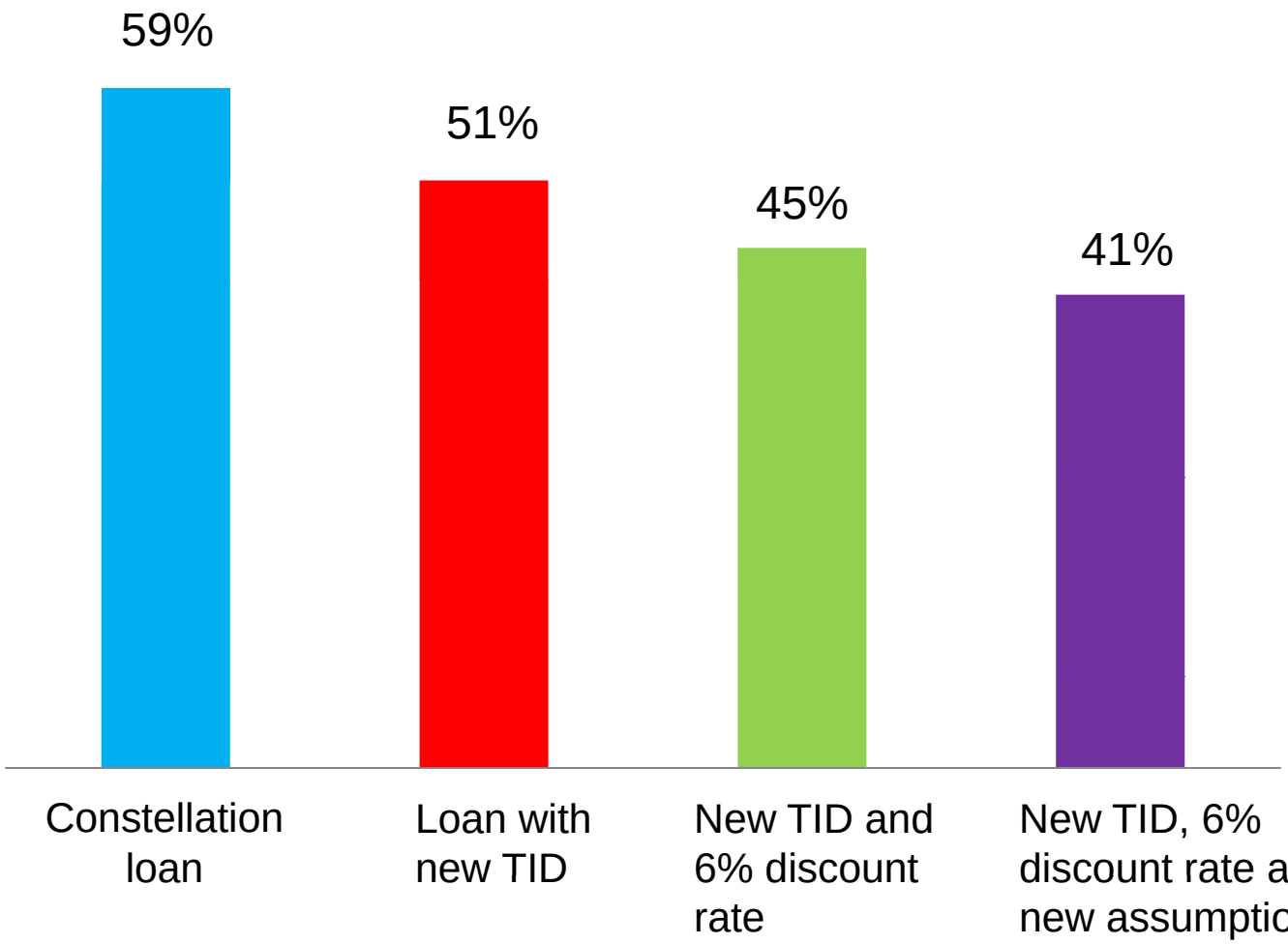
Percent of Increment Consumed for Identical Loan in TIDs with varying lifespans



A loan conforming to the 50% rule in a new TID would use 65% of the increment in a TID that is nine years old

Example: Constellation Capitol East District Project

Percent of Increment Consumed for Constellation Loan under varying assumptions



The $3.4 million TIF loan to the Constellation (Gebhardt) would nearly conform to the 50% rule if the TID had been new.

* Assumes mill rate declines at 1.6% versus 1.9%, commercial appreciation at 2.8% versus 2%

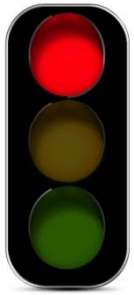
EDC recommended flexibility within criteria

EDC Criteria

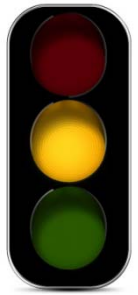
1. **Type of the project**
2. **Financial gap**
3. **Projected increment**
4. **Financial health and age of the TID**
5. **Evaluation of competitive factors**
6. **Location in a Targeted Development Area**
7. **Other demands for increment**
8. **Likelihood of catalyzing other development**
9. **Extraordinary strategic or civic purposes**
10. **Current economic conditions**

EXAMPLES OF HEALTH OF TID

TID #40
TID is $20 million below base value



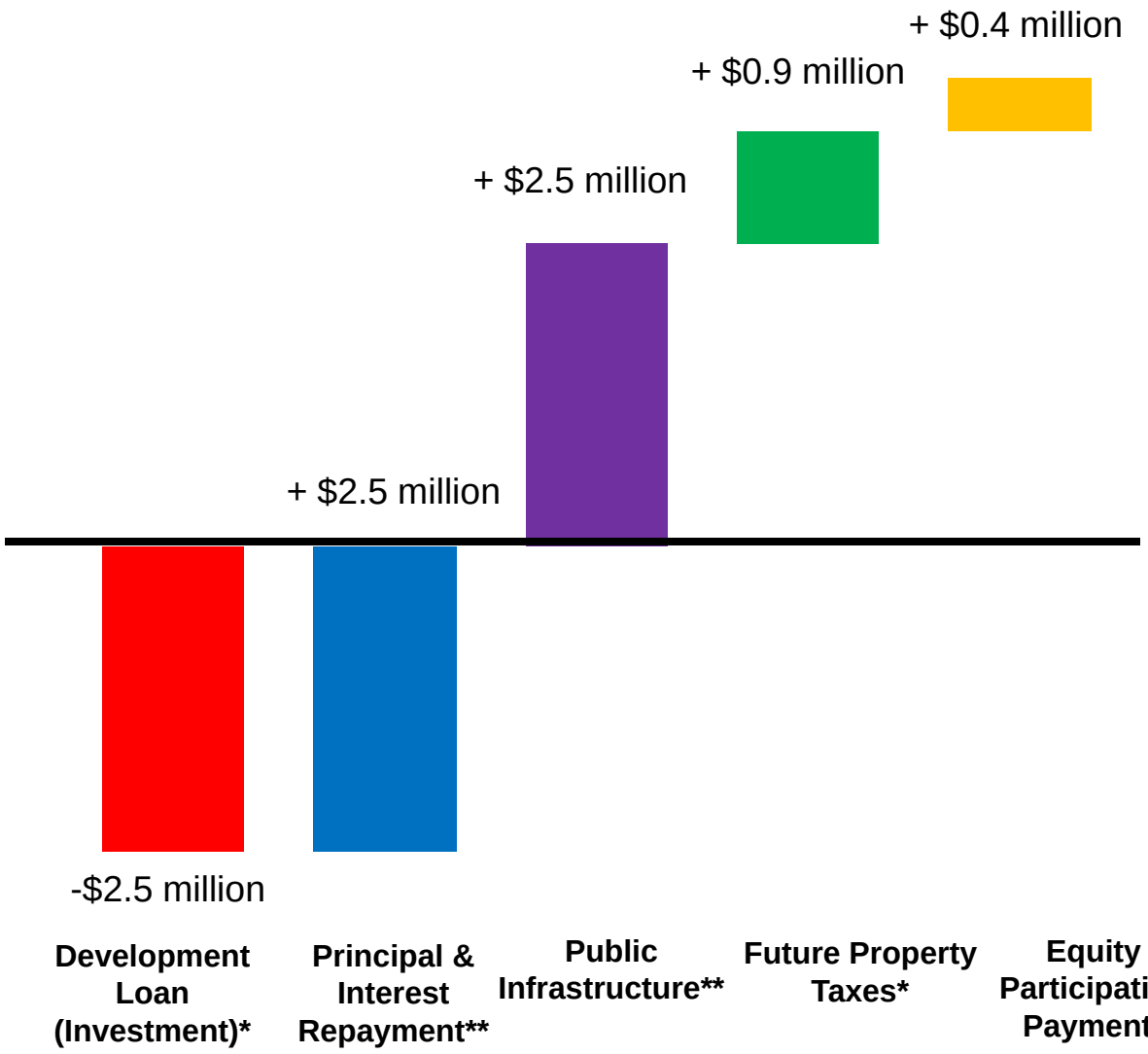
TID #37
TID has no excess increment



TID #25 or #32
TIDs are generating strong cash flow

Equity participation the least important component

Hypothetical return from $20 million project

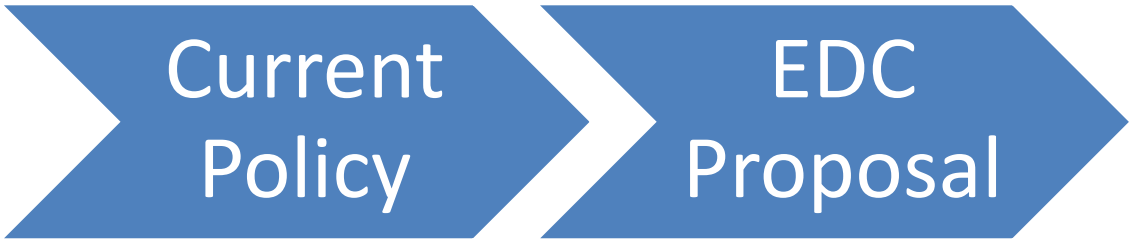


Equity participation payments are the least important part of the city's return but one of the biggest sticking points in closing deals

* Calculated on standard city assumptions at 50% of increment using a 7% discount rate with 100 year time horizon

** Paid through property taxes, not direct payment; assumes actual interest rate in lieu of using 7% discount rate

The Issue of Guarantees



Personal Guarantee Required

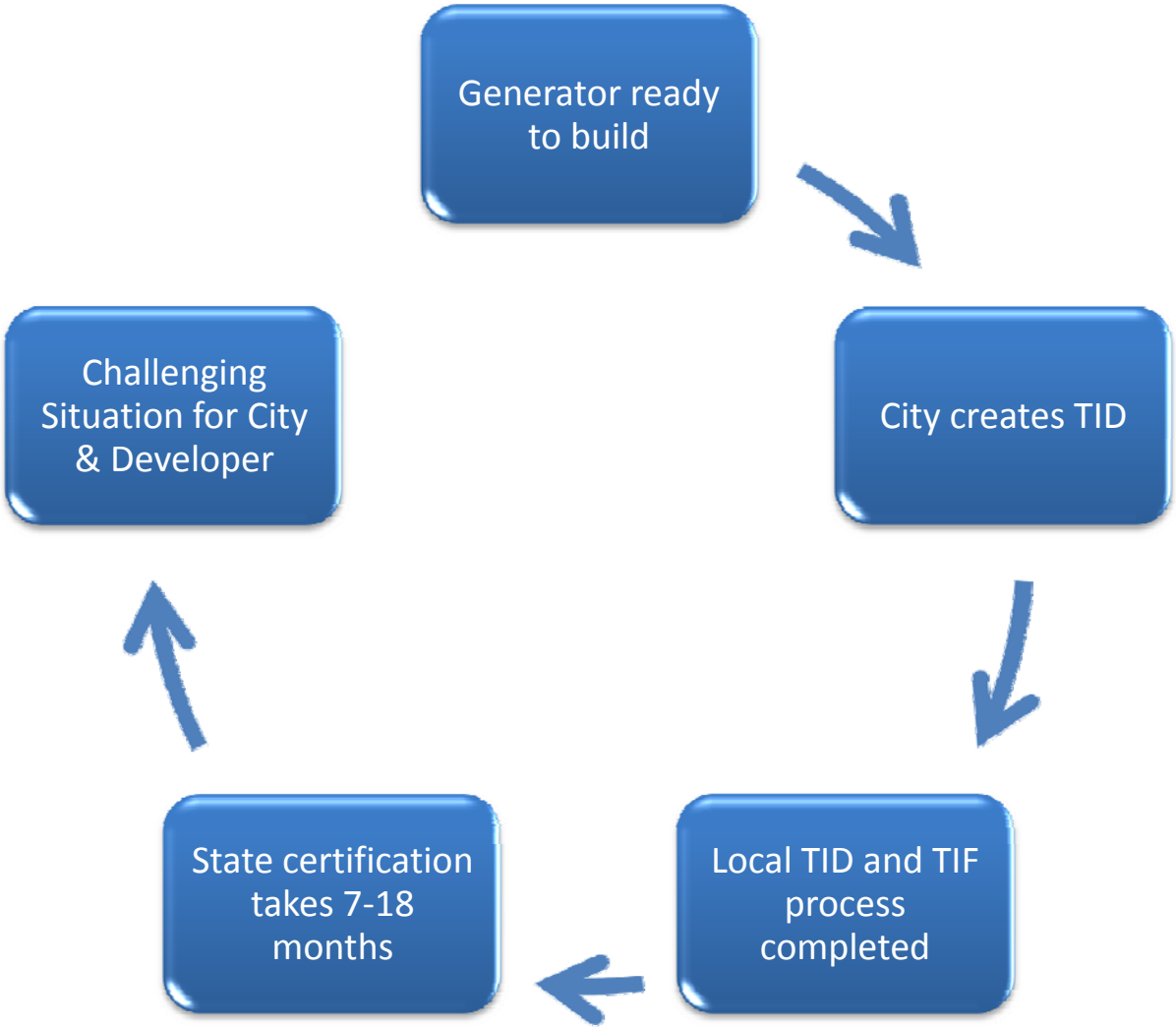
Guarantee acceptable to City required

Personal Guarantee generally desired

Possible reasons for other guarantee

- Nonprofit
- Corporation or employer is applicant
- City TID need for generator greater than need for security
- High risk, highly desirable development

Generator requirement can cause an issue

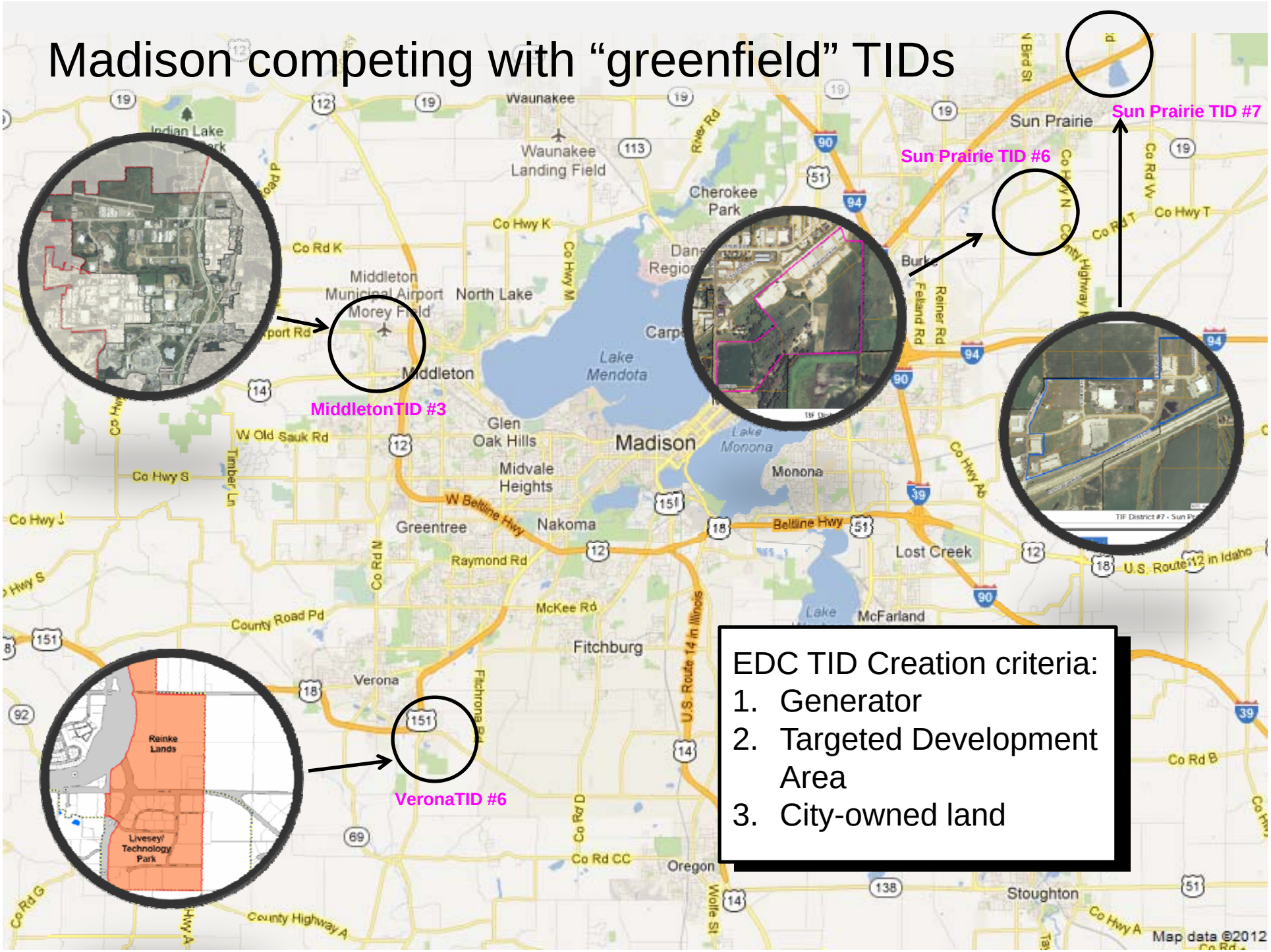


Waiting until a generator is 100% ready to go can increase risk for either city and/or developer

<u>Current Solutions</u>

- Conversion to Loan (increases developer risk)
- City bears risk (increases city risk)

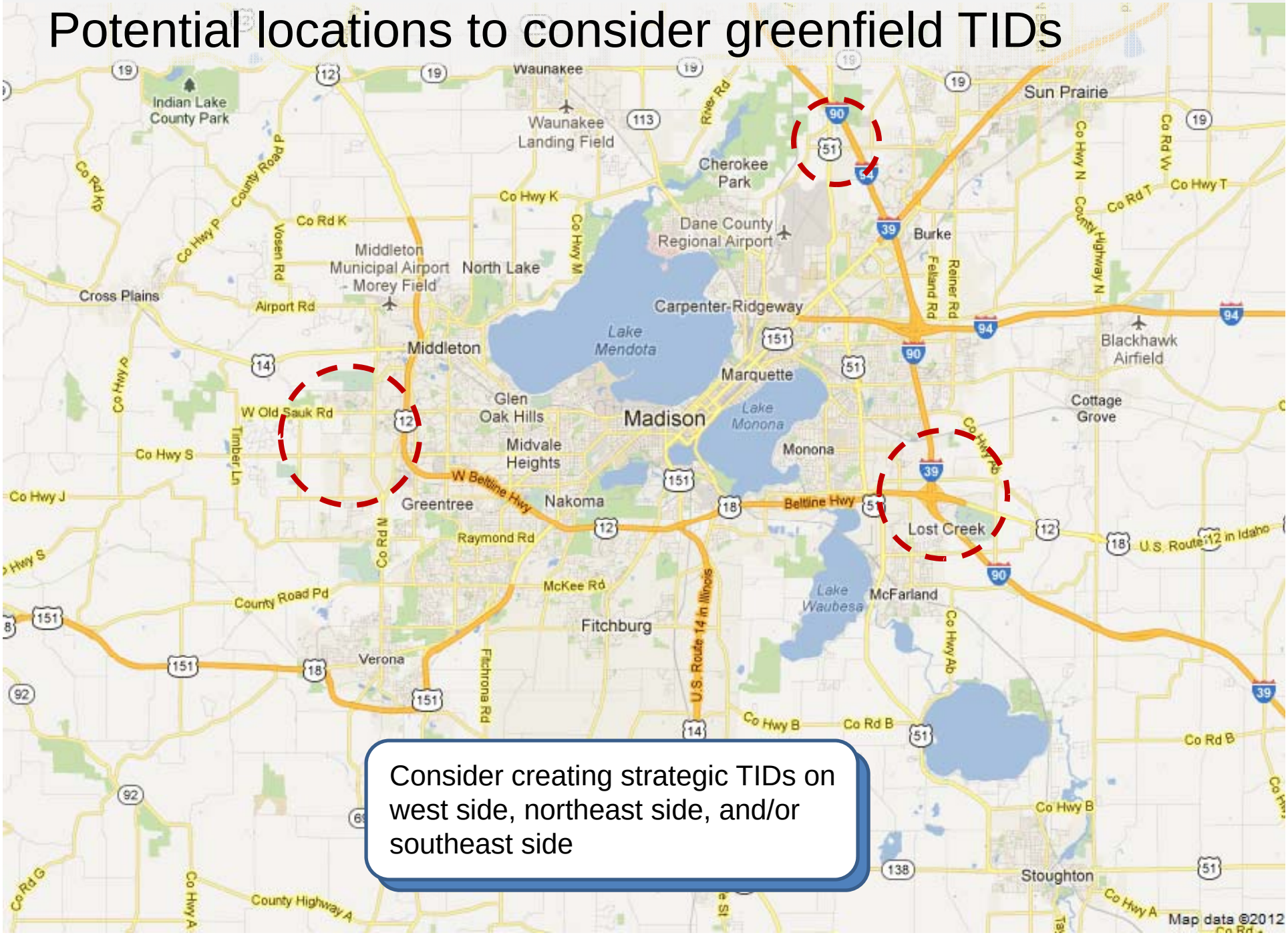
Madison competing with “greenfield” TIDs



EDC TID Creation criteria:

1. Generator
2. Targeted Development Area
3. City-owned land

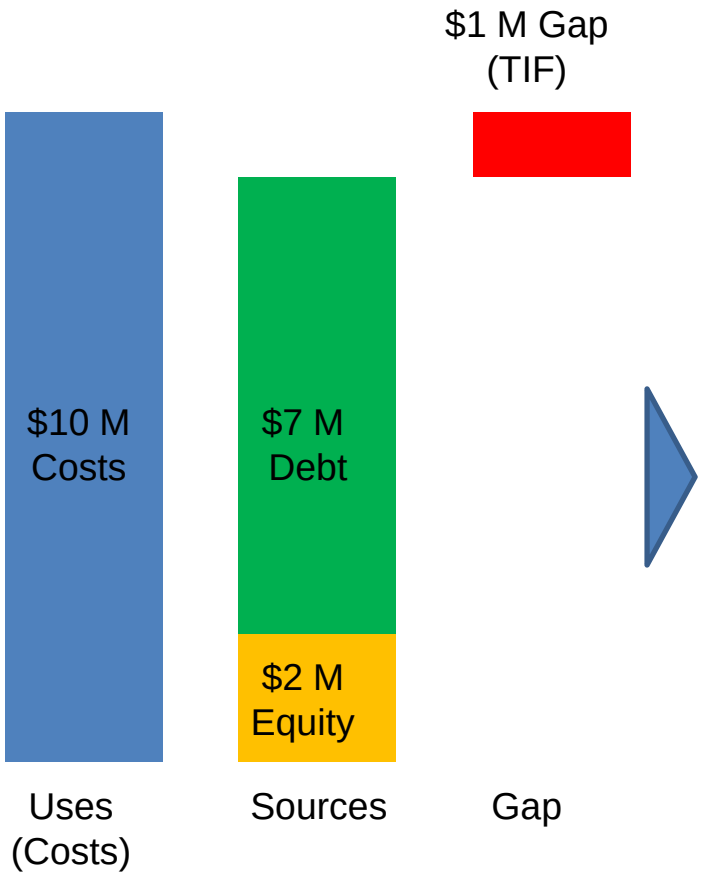
Potential locations to consider greenfield TIDs



City's Method Doesn't Always Translate for Companies

Schematic of City's Underwriting Method

City's Underwriting Method

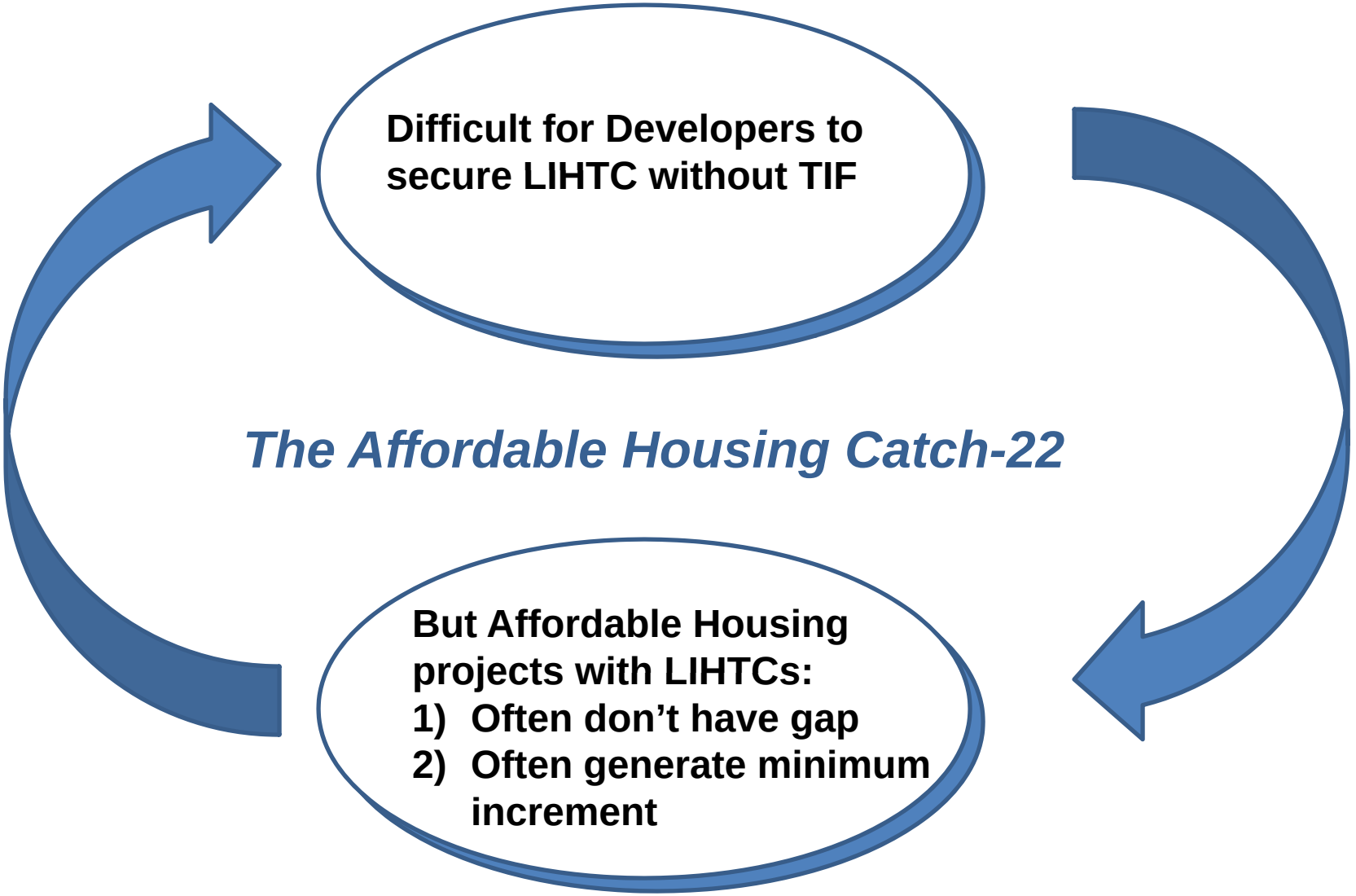


Comments

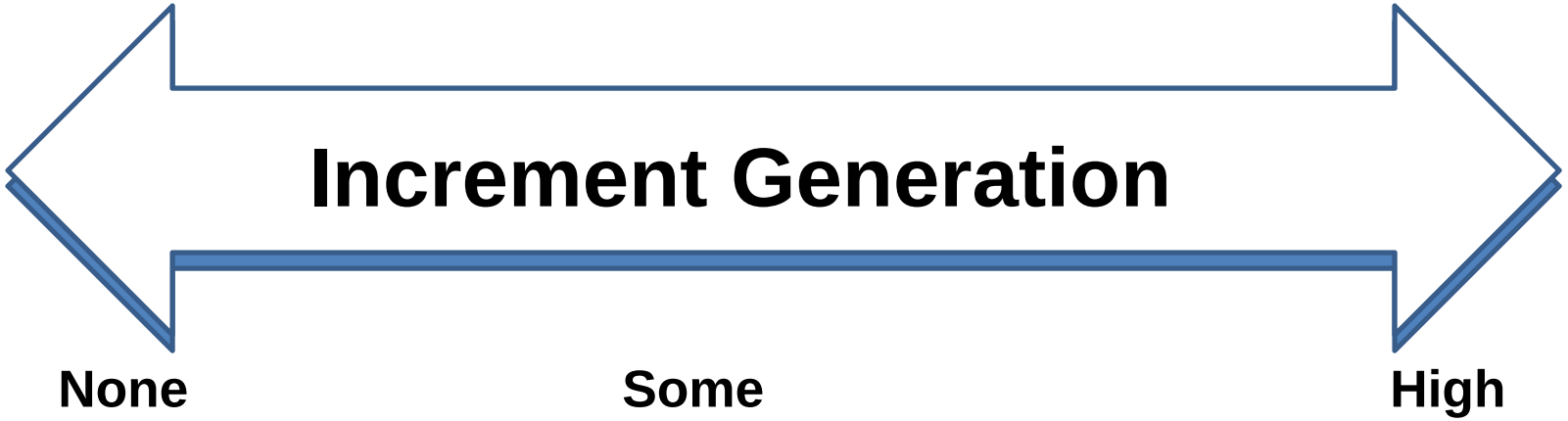
- Analysis of gap useful in demonstrating that "but for" TIF, the project would not occur
- Gap financing method especially relevant to developer real estate projects
- Gap analysis is less useful in situations where employers are making location or investment decisions
- Companies allocate capital based on expected returns
- Sometimes a subsidy is required to make Madison projects more attractive than other projects ("but for" the subsidy, the project may happen elsewhere)
- Other communities use TIF as an incentive
- City needs to develop policy to address situations where "competitive factors" are at play*

* See City Attorney Opinion, "Legal Limitations on Tax Incremental Financing (TIF)" dated August 5, 2009

Affordable housing challenges City's TIF Policy



EDC's affordable housing solution



Public Good

User of increment

Example: Public Infrastructure

Hybrid Good

Small user; small generator of increment

Example: Affordable Housing

Private Good

Generator (and user) of Increment

Example: Private development

Consider employing Pay-As-You-Go when indicated

	Traditional Financing	Pay-As-You-Go
Who incurs Debt?	City	Developer
Timing of TIF expenditure	Up front	Over time
Interest rate	Low (City rate)	Higher (Developer rate)
Method to transfer risk to Developer	Guarantee	N/A (Nature of Pay as you go)
Interface with multi-phase projects	Difficult to negotiate multi-phase guarantees up front	Creates incentive to complete multi-phase projects

Conventional vs. Pay-As-You-Go

Method	CONVENTIONAL FINANCING	PAY-AS-YOU-GO FINANCING
Chief Advantages	Lower interest payments More increment for infrastructure	Shifts risk more effectively Creates greater incentive to develop
Likely Scenario	Straightforward single-phase projects Lower risk projects Increment around 50%	Complex multi-phase projects Higher risk projects Increment above 50%