

# **An Examination of the State of Vermont** **Tax Increment Financing Program**

**Prepared by the Vermont Legislative Joint Fiscal Office**

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**Statutory Charge**

Per 24 V.S.A. § 1892, as amended by the Legislature in Act 69 of 2017

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## Executive Summary

Tax increment financing (TIF) is an economic development tool that the State has been using since the late 1990s. The program, authorized by the Legislature and administered by both municipalities and the Vermont Economic Progress Council (VEPC), is a property-tax based incentive to assist municipalities in funding infrastructure improvements (see Box, “What is tax increment financing?”). Vermont currently has established 11 TIF districts. Ten of these are active and one has been retired.<sup>1</sup> Six additional future districts received approval by the legislature as part of Act 69 of 2017 with one of those, Bennington, established in late 2017 (see Table 1).

As a part of Act 69, Sec. J.2. 24 V.S.A. §1892, enacted during the 2017 legislative session, the Joint Fiscal Office (JFO), in consultation with other relevant State entities, was charged with examining and reporting to the General Assembly “on the use of both tax increment financing districts and other policy options for State assistance to municipalities for funding infrastructure in support of economic development and the capacity of Vermont to utilize TIF districts moving forward.”

The primary findings of this examination are as follows:

- **Vermont’s TIF program is well-defined in statute and transparent relative to other states and cities, with some room to improve the approval, oversight, and evaluation process to ensure the program is maximizing statewide benefits.** Legislative action over the past three decades has created a program that sets limits on the potential downsides and excesses of TIF that have occurred in other states. TIF also aligns with previous State economic development policy promoting economic growth in denser, downtown centers. However, while the Vermont Economic Progress Council (VEPC) requires annual information reporting from State TIF districts in a way that exceeds other states, JFO finds that the current evaluation system at the State level is neither independent nor does it measure whether TIF is providing economic benefits to the State as a whole. JFO also finds that the VEPC’s TIF application review could do more to examine statewide benefits of a potential district, rather than solely the applicant municipality.
- **Using mid-range assumptions of TIF district growth into the future and what might have occurred absent the use of TIF, JFO estimates that Vermont’s TIF program represents a negative cost to the Education Fund of between \$3 million and \$7 million annually from 2017 to 2030.** This estimate includes the new Bennington TIF district but excludes the additional five districts approved in 2017.

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<sup>1</sup> Colchester was approved for a TIF district in 2006 but dissolved before incurring debt.

Cumulatively, the program will cost the Education Fund approximately \$68 million (nominal dollars) from 2017 to 2030. Moreover, JFO estimates that it will take over 50 years for Education Fund revenues from an average Vermont TIF district to catch up to revenues from the same geographic area without a TIF district.<sup>2</sup> Additionally, JFO estimates that TIF will cost, in aggregate, an additional \$1 million to \$4 million annually to municipal general funds between 2017 and 2030. It is important to note that estimates of TIF costs or benefits are very dependent upon the assumptions used. These could range from 0% baseline growth (no growth would have happened absent TIF) to baseline growth that is equal to TIF district growth (all the growth that occurs in a TIF district would have occurred anyway somewhere in the municipality or State). This second assumption is used for determining the revenue and grand list estimates in the Consensus Administration and JFO Education Fund projections.<sup>3</sup> For the purposes of calculating Education property tax rates each year, the Consensus Administration and JFO Education Fund estimates of TIF costs (approximately \$5 million to \$10 million per year) are used. Any approval of new districts beyond the current 10 active districts will generate further negative fiscal impacts.

- **The extent to which TIF has and will provide the expected economic benefits to the State is unclear.** Vermont's use of TIF to promote downtown economic development (also known as Smart Growth) may bring indirect benefits related to denser communities, such as productivity growth, environmental improvements, and more efficient provision of public services. TIF could also be drawing in other sources of economic development funding. However, Vermont's program also likely shifts some economic activity from one area of the municipality or State to the TIF districts, rather than creating new economic activity. Academic and other states' research focused on TIF has also found little economic benefit to using it. The economic benefits provided by each Vermont TIF district may differ because of the varying rules that existed at the time of their creation.
- **Vermont's TIF districts have largely achieved their projections of property value growth, but have missed incremental tax revenue and private investment estimates by wide margins.** Despite making accurate projections of property value growth on average, as of year-end 2016, revenues generated from a TIF district (tax increments) have fallen considerably short of projections, missing 70% of the time and with a median miss of 42%, likely resulting from original projections of property tax rates being higher than actual. Additionally, as of year-end 2016, total actual private real property investment in Vermont TIF districts has been less than one-half

<sup>2</sup> Using nominal dollars; If real dollars are used, this break-even point is pushed out further into the future.

<sup>3</sup> The Consensus Administration estimate uses this assumption because separate analyses completed by State economists using the REMI State model have shown TIF developments do not result in net positive fiscal benefits to the State.

of what was projected in their applications. This is likely partly the result of construction or planning delays.

- **Vermont’s TIF statute does not guarantee geographic diversity of TIF districts, especially to those areas of the State that are economically distressed.** State statute attempts to create geographic diversity of TIF districts in Vermont by stating that no municipality that has a TIF district will be eligible for another.<sup>4</sup> However, State statute does not explicitly require that TIF be located in an economically distressed area. The complexity of TIF may also preclude towns with less staff capacity and expertise from establishing TIF districts. Finally, research has shown that in areas where another government’s tax revenues are eligible for TIF district debt (such as Vermont’s), municipalities with faster economic growth are more likely to create TIF districts.

In light of these findings, JFO presents the following considerations to legislators should they seek to make changes to the program:

1. **Legislators may want to consider requiring municipalities to repay TIF district debt as incremental tax revenues accrue, rather than solely the required bond payment.** Under current TIF district rules and statute,<sup>5</sup> if the amount of incremental tax revenues exceeds the amount required for debt service, municipalities may, but are not required to, use the surplus to repay outstanding debt early. Legislators may want to consider requiring this surplus tax increment to pay down debt early, to the extent that there are no prepayment penalties for the debt instrument and that there is enough revenue to pay the remaining debt service in the TIF fund. The benefit to early repayment is that it shortens the life of the TIF district, allowing the municipality and State to receive the full fiscal benefit earlier (rather than waiting 20 years). It also allows the municipality to mitigate the downside risks of future uncertain incremental tax revenues.
2. **Legislators may want to consider whether the current system of approval, monitoring, and evaluation ensures TIF district accountability for results.** JFO finds that the current program could be improved to ensure that TIF districts are providing *statewide* economic benefits, not just municipal benefits. These improvements extend from the approval process to the evaluations of TIF districts once they are established. Specifically, JFO recommends the following:
  - As part of the approval process, VEPC should be required to examine whether the TIF district applicant will provide statewide economic benefits to

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<sup>4</sup> 32 V.S.A. § 5404a

<sup>5</sup> 24 V.S.A. § 1896(d).

justify the tax expenditure on the Education Fund. This should include an examination of whether the developments in the proposed TIF district would have occurred elsewhere in the State. This process could also be informed by use of a quantitative model, such as the VEGI Cost-Benefit Model. JFO recommends that VEPC adopt these practices as it reviews TIF districts which have been authorized but not approved.

- Once a TIF district is established, VEPC's Annual Report should provide information on the level of statewide economic benefits, in addition to the value created within TIF districts themselves. It should also report whether incremental tax revenues are meeting projections and information on whether investment in the TIF districts is meeting the plans laid out in their applications.
- The State Auditor's evaluation of TIF districts should be supplemented with an independent review of TIF districts' fiscal impacts and economic benefits every five to seven years.
- If a municipality bonds against TIF incremental tax revenues, should these tax increments not materialize as projected because of delays in private investment, the Legislature should consider recourse for VEPC and the municipality to mitigate the negative fiscal impact of this situation.

**3. Consideration should be given to whether TIF is the most effective way to achieve infrastructure development in downtowns.** Current location and project criteria limit the use of TIF to denser, downtown areas, effectively making TIF a downtown infrastructure financing tool. TIF can encourage municipal ownership of local economic development, as well as draw in other types of financing. However, it is a complex tool that requires significant town capacity to apply and administer and has unique associated downside risks if revenues from the TIF fall short of projections. Before approving new districts beyond the 6 approved in Act 69 of 2017, or in the event that the Legislature chooses to reopen the discussion of TIF districts in the upcoming year, the Legislature might want to weigh the advantages and disadvantages of the program in its current structure against other development tools (see Table 11) that could achieve the same goals as those of the TIF program.

**4. The combination of Vermont's statewide property tax system and TIF raises equity issues among municipalities.** This report estimates a net cost to the Education Fund of \$3 million to \$7 million per year stemming from the ten active TIF districts. The cost would grow with the creation of the additional authorized TIF districts, and the State break-even point would be pushed out farther if the costs and revenues were adjusted for inflation. This would imply that property tax rates in non-

TIF municipalities would be higher to fund infrastructure in TIF municipalities, despite non-TIF municipalities potentially not seeing benefits and perhaps suffering loss of development themselves from these investments. Legislators need to consider whether such a highly town-specific development program has statewide benefits to justify using statewide revenues from nonparticipating municipalities.

- 5. Because TIF allows municipalities to keep State education property tax revenues to fund their own infrastructure, there could be an incentive for nonparticipating municipalities to establish TIF districts.** Vermont's TIF program, by allowing municipalities to retain up to 70% of statewide education property taxes, leads to a large portion of TIF district financing being borne by non-TIF municipalities. As the number of TIF districts increases, the larger the cost becomes on the non-TIF municipalities. While recent legislation requiring a larger municipal share has helped address this incentive, this incentive could still be very large because most municipalities in Vermont (with some exceptions) have a lower municipal property tax rate than their education property tax rates. This misalignment of incentives has been shown in the academic literature and has historically led to rapid expansion of TIF districts in several states with serious fiscal consequences. This raises the broader question of what level of State-municipal cost sharing is appropriate for municipal infrastructure.
- 6. Legislators need to be mindful that TIF involves considerable uncertainty.** TIF districts are subject to both upside and downside risks. On the upside, TIF districts could draw in funds from non-TIF sources and increase property values in surrounding areas. On the downside, if a municipality borrows money against inaccurate growth projections that fall short, it could put financial pressure on municipal budgets. Moreover, TIF could cause the State to bear unnecessary fiscal cost if either of the following conditions are met: if a proposed TIF district is in an area that was likely to grow without TIF, or if a comparable development would have occurred elsewhere in the State and if there is no compelling case to be made that the proposed district would produce statewide benefits resulting from downtown, denser development (Smart Growth). Further approval of new TIF districts, both by VEPC and the Legislature, needs to ensure that applications use realistic assumptions to mitigate these downside risks and weigh whether other development tools could achieve the same goals of TIF with less uncertainty. Legislators also need to be mindful that because TIF's fiscal costs are uncertain going forward, there is no way for them to control the costs of the TIF program in the same way there is for other annual appropriations.



Table 1: TIF Districts In Vermont						
	Year Created	Increment Retention Period	Original Property Value at Creation	Education Fund Increment Split	Municipal General Fund Increment Split	Debt Incurred as of 2017
<b>Active TIF Districts</b>						
<b>Burlington Waterfront</b>	1997	1996-2035 <sup>a</sup>	\$42,412,900	Original: 100% to TIF, 0% to Ed. Fund Beginning 2010: 75% to TIF, 25% to Ed. Fund	Original and post-2010: 100% to TIF, 0% to municipal general fund	\$27,099,873
<b>Milton North and South</b>	1998	1999-2019 <sup>b</sup>	\$26,911,151	Original: 100% to TIF, 0% to Ed. Fund Beginning 2010: 75% to TIF, 25% to Ed. Fund	Original: 100% to TIF, 0% to municipal general fund Beginning 2010: 75% to TIF, 25% to municipal general fund	\$9,295,300
<b>Winooski</b>	2000	2004-2024	\$24,822,900	Original: 95% to TIF, 5% to Ed. Fund Beginning 2004: 98% to TIF, 2% to Ed. Fund	Original and post-2004: 100% to TIF, 0% to municipal general fund	\$29,998,000
<b>Milton Town Core</b>	2008	2011-2031	\$124,186,560	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$3,422,600
<b>Hartford</b>	2011	2014-2034	\$31,799,200	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$900,000
<b>Burlington Downtown</b>	2011	2016-2036	\$174,412,200	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$200,000
<b>St. Albans</b>	2012	2013-2033	\$107,909,150	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$14,500,000
<b>Barre</b>	2012	2015-2035	\$50,851,870	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$2,200,000
<b>South Burlington</b>	2012	2017-2037	\$36,228,700	75% to TIF, 25% to Ed. Fund	75% to TIF, 25% to municipal general fund	\$0
<b>Newly-Approved TIF Districts</b>						
<b>Bennington</b>	2017	2018-2037	\$8,419,000	70% to TIF, 30% to Ed. Fund	100% to TIF, 0% to municipal general fund	\$0
<b>Retired TIF Districts</b>						
<b>Newport</b>	1998	1997-2015	\$48,500	100% to TIF, 0% to Ed. Fund	100% to TIF, 0% to municipal general fund	\$300,000

Note: In 2017, 6 additional districts were approved by the Legislature.

<sup>a</sup>Act 134 of 2016 extended the period to incur indebtedness to 2020, and the increment retention period to 2035. This extension was made to accommodate the redevelopment of the Burlington Town Center

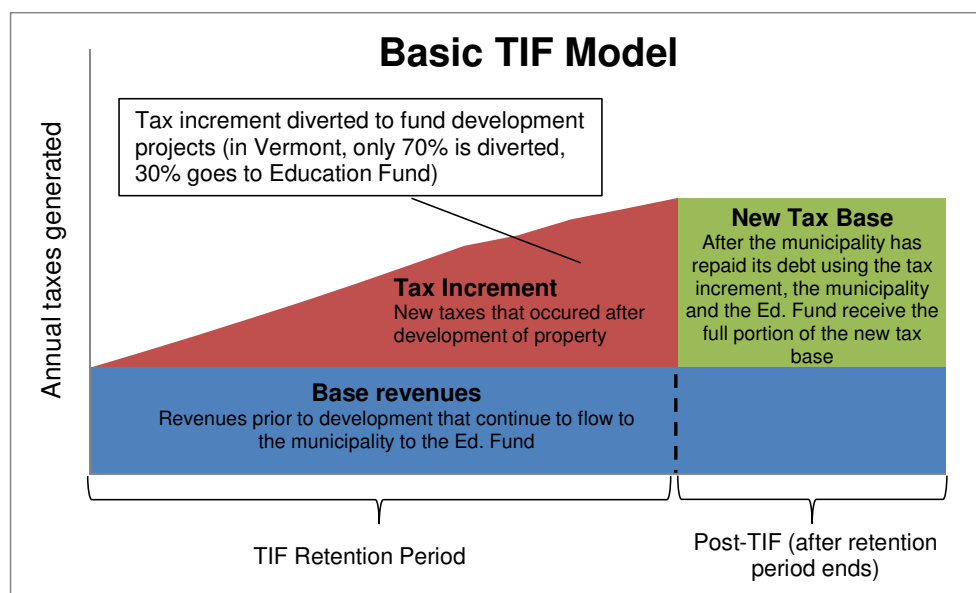
<sup>b</sup> In 2006, the Legislature enacted special provisions allowing the Milton North and South TIF Districts to be extended for an additional ten years

### What is tax increment financing (TIF)?

Tax increment financing (TIF) was originally developed as an economic development tool to stimulate real estate revitalization in blighted neighborhoods, where little if any new investment was considered likely. It has since been adopted by both municipalities and states to spur economic development in targeted geographic areas. TIF originated in California in the early 1950s but proliferated nationwide during the 1980s and 1990s following the scaling back of federal funding for economic development. Currently, every state except Arizona allows some form of tax increment financing, albeit in substantially different forms.

At its core, TIF is an economic development tool that allows for an entity to finance new construction by diverting a portion of the growth in future property tax revenues. The TIF process generally goes as follows:

- A municipality seeks to improve a geographic area, such as a downtown or plot of land that has seen little or no growth over an extended period, by investing in new infrastructure (e.g., parking garages, new sidewalks, streetlights, septic systems, etc.). These infrastructure improvements, in theory, will stimulate private investment that would not otherwise have occurred in the designated TIF area. The combination of both public and private investment is expected to increase property values, generating property tax revenue. The municipality subsequently designates this area a “TIF district.”
- The municipality builds the promised infrastructure with borrowed funds. To repay these debts, the municipality agrees to split future property tax revenues from the TIF district. The municipality agrees to keep the property taxes that existed prior to any development. This is called the “base revenue” or “original taxable value.” Some portion of any property taxes that result from increased property values is dedicated to repaying infrastructure debt. These additional property taxes are called “tax increments.”
- The municipality defines what portion of the tax increment goes to pay debt. In some states, cities and states are entitled to use 100% of the tax increment, while in others, such as Vermont as of 2017, a TIF district can retain only 70% of the tax increment.
- Once the retention period ends, this split in revenues ceases and the municipality and state receive the full amount of tax revenue.



Vermont granted municipalities the right to create TIF districts in 1985, although the program has undergone substantial changes over the past three decades. Legislation has placed new regulations and limits on TIF districts in the State in the years since the creation of the program. Vermont’s 11 TIF districts were created at various points in time and are thus subject to different statutory requirements. Vermont’s statewide property tax means that a TIF district is entitled to two tax increments: the tax increment from the State education property tax and the tax increment from the municipal property tax.

## **Statutory Charge**

Per 24 V.S.A. § 1892, as amended by the Legislature in Act 69 of 2017:

(e) On or before January 15, 2018, the Joint Fiscal Office, with the assistance of the consulting Legislative Economist, the Department of Taxes, the State Auditor, and the Agency of Commerce and Community Development in consultation with the Vermont Economic Progress Council, shall examine and report to the General Assembly on the use of both tax increment financing districts and other policy options for State assistance to municipalities for funding infrastructure in support of economic development and the capacity of Vermont to utilize TIF districts moving forward.

(f) The report shall include:

- (1) a recommendation for a sustainable statewide capacity level for TIFs or comparable economic development tools and relevant permitting criteria;
- (2) the positive and negative impacts on the State's fiscal health of TIFs and other tools, including the General Fund and Education Fund;
- (3) the economic development impacts on the State of TIFs and other tools, both positive and negative;
- (4) the mechanics for ensuring geographic diversity of TIFs or other tools throughout the State; and
- (5) the parameters of TIFs and other tools in other states.

(g) Beginning in 2019 and annually thereafter, on or before January 15 of each year, the Joint Fiscal Office, with the assistance of the consulting Legislative Economist, the Department of Taxes, and the Agency of Commerce and Community Development in consultation with the Vermont Economic Progress Council, shall examine the recommendations and conclusions of the tax increment financing capacity study and report created pursuant to subsection (e) of this section, and shall submit to the Emergency Board and to the House Committees on Commerce and Economic Development and on Ways and Means and the Senate Committees on Economic Development, Housing and General Affairs and on Finance an updated summary report that includes:

- (1) an assessment of any material changes from the initial report concerning TIFs and other tools and an assessment of the health and sustainability of the tax increment financing system in Vermont;

(2) short-term and long-term projections on the positive and negative fiscal impacts of the TIF districts or other tools, as applicable, that are currently active or authorized in the State;

(3) a review of the size and affordability of the net indebtedness for TIF districts and an estimate of the maximum amount of new long-term net debt that prudently may be authorized for TIF districts or other tools in the next fiscal year.

(h) Annually, based on the analysis and recommendations included in the reports required in this section, the General Assembly shall consider the amount of new long-term net debt that prudently may be authorized for TIF districts in the next fiscal year and determine whether to expand the number of TIF districts or similar economic development tools in addition to the previously approved districts referenced in subsection (d) of this section and the six additional districts authorized by 32 V.S.A. § 5404a(f). (Added 1985, No. 87; amended 2013, No. 80, § 3; 2017, No. 69, § J.2, eff. June 28, 2017.)

## I. Background

Tax increment financing (TIF) is an economic development tool that allows municipalities and states to fund development or infrastructure. In many municipalities around the country that face slow economic growth or aging infrastructure (or both), TIF offers a way to finance these improvements without substantial up-front budgetary outlays. Additionally, supporters of TIF argue that making these improvements will drive private investment to the area. These two reasons are the key arguments used to support TIF.

TIF is not a new program; California pioneered the first TIF program in 1952. However, it was not until the 1980s and 1990s, following the scaling back of federal funding for economic development, that TIF proliferated substantially. Many states adopted TIF programs and those that had them already significantly loosened restrictions on their use. The number of TIF bonds in circulation has nearly tripled over the past 30 years.<sup>6</sup> Currently, every state except Arizona allows TIF, albeit in significantly different forms.

### **Description of the Vermont's TIF Program**

Although Vermont has permitted the use of TIF since 1985, the program has changed substantially over time. This section provides a summary of the statutory history of TIF in Vermont, reviewing the changes to statutory definitions and limits of the program. It also gives an overview of current active and inactive districts in the State and current rules for establishing TIF districts.

Vermont's TIF program has undergone several statutory changes since its creation. Because Vermont's ten active districts were created at different points in time, they are subject to different rules and approval criteria.

TIF was created in Vermont under 24 V.S.A Chapter 53, subchapter 5. This legislation permitted municipalities to establish

#### Box 1: Definitions of TIF Terms

**Taxable Value:** The assessed value of property that is subject to state, municipal, or other taxes.

**Original Taxable Value:** The base taxable value of the property before the establishment of a TIF district.

**Increment:** The difference between a property's current value and original taxable value.

**Tax increment (incremental revenue):** The difference between the property taxes due on the current taxable value and the property taxes due on the original taxable value.

**Related costs:** Expenses incurred and paid by the municipality to finance and construct new infrastructure.

**Retention period:** The period of time a municipality is entitled to capture a portion of the total tax increment to finance infrastructure improvements.

<sup>6</sup> Randall O'Toole, Cato Institute, Crony Capitalism and Social Engineering: The Case Against Tax Increment Financing, 18 May 2011.

TIF districts and set up basic parameters for their formation. Four TIF districts were established under the rules set by this legislation: Burlington Waterfront, Milton's Husky and Catamount district (now combined to form the Milton North and South TIF district), Winooski, and Newport (now inactive). Since no formal State program existed for these districts at their formation, the project criteria and tax increment split were decided on a district-by-district basis.

In 1998, the Vermont Economic Progress Council (VEPC) was delegated the authority to review and approve new TIF districts. Currently, VEPC is charged with approving and administering the TIF program in Vermont. After Act 60 of 1997 created a statewide education property tax, TIF districts became eligible to retain two revenue sources: the statewide education property tax increment and the municipal property tax increment. Since statewide revenues were being used, a statewide body (VEPC) was charged with reviewing, approving, and overseeing TIF districts.

Act 60 greatly increased State involvement in the program by providing an additional revenue source for municipalities. Recognizing this, the Legislature passed Act 184 of 2006 which, in addition to capping TIF districts at 10, laid out new approval criteria for VEPC:

- Limits on the split of tax increment: For the statewide education property tax increments, a municipality could retain only 75% of the tax increment for TIF debt, remitting 25% of it to the State. The municipal property tax increment was also set at 75/25; 75% of the tax increment would be kept to repay TIF debt, while 25% went to municipal general funds.
- New approval criteria: VEPC was required to review whether the development would have happened without the tax incentive ("but-for" evaluation). It was also now responsible for reviewing town projections for property growth, tax increments, and tax increment splits.
- New location criteria: A new TIF district would now only be approved if it were in one of the following areas: a high density or compact area, an approved downtown or growth center, or an economically distressed area.
- New project criteria:<sup>7</sup> A new TIF district must include at least three of the following five criteria:
  - The development must require substantial public investment beyond normal municipal operating or bonded debt expenditures
  - The development includes new affordable housing for residents in the municipality
  - The development includes the remediation of a brownfield site

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<sup>7</sup> Henceforth in this report, "project criteria" will refer to the rules governing what types of development are eligible for TIF. "Location criteria" will refer to the areas of the State that are eligible to use TIF.

- The development includes at least one entirely new business or the expansion of an existing business within the district
- The development will increase transportation by improving traffic flow or creating new public transit systems
- TIF district lifespan: Any new district was eligible to retain property tax increments for not more than 20 years.

Five of Vermont's ten active TIF districts fall under these Act 184 of 2006 legislative criteria.

The next major TIF legislation to be passed occurred in 2013 in Act 80. The legislation prohibited VEPC from approving new TIF districts other than the ones already created, delegated the rulemaking authority to VEPC, and clarified how tax increments could be used.

The most recent major change to TIF legislation was Act 69 of 2017 which created clearer but also stricter criteria for new districts. In addition to grandfathering the rules for existing districts, major updates included:

- New districts are now entitled to keep only 70% of the statewide education property tax increment, rather than the previous 75%.
- Municipalities are required to commit at least 85% of the municipal property tax increment for the funding of TIF district debt, effectively increasing the share municipalities bear for their own development.
- New TIF applicants must meet two of the three aforementioned (see page 8) location criteria, rather than one.
- Definitions are clarified for what constitutes an economically distressed area.

Act 69 capped the creation of new districts at six, which could be increased by Emergency Board approval. Bennington is the only TIF district that has been approved under these rules. A complete list of statutory changes can be found in Appendix Table A1.

## **II. Report Analysis**

Per Act 69 of 2017, this report is charged with examining Vermont's TIF program. It aims to study four specific areas of the program:

A. Operational Evaluation: How well does Vermont define and administer its TIF program relative to other states and cities?

B. Fiscal Impacts: What are the positive or negative fiscal impacts of the TIF program on the State?

C. Economic Impacts: Has the TIF program created real economic benefit for the State?

D. Geographic Diversity: Does the current program promote geographic diversity of TIF districts in the State?

**A) Operational Evaluation: An examination of Vermont’s statutory definitions and administrative performance relative to other states and cities.**

In order to examine Vermont’s TIF program from an operational perspective, JFO studied the effectiveness of the program on two levels.

Statutory perspective: This section will examine how well Vermont’s TIF statute is defined and how well it sets limits on potential downsides to TIF.

Administrative perspective: This section focuses on how well Vermont monitors whether the program is meeting the goals set out in statute, and how easy it is for a member of the public to obtain information on Vermont’s TIF districts.

Below is a summary of JFO’s findings in these areas:

- **Statutorily, the design, definitions, and limits of Vermont’s TIF program help limit the downside risks associated with the uncertainty of TIF in a way that exceeds most other state or city TIF programs.**
  - The types of taxes eligible for TIF: Because Vermont statute limits TIF to municipal and State education property taxes (and not sales, income, meals and rooms taxes or other revenue sources), TIF district revenue flows are exposed to less downside risk and volatility compared to other states.
  - The portion of the tax increment eligible for TIF: By capping new TIF districts to 70% of the statewide education property tax increment retention, the State realizes some potential fiscal benefits to property value growth while preventing TIF municipalities from incurring overly large debt burdens. Those states that allow for 100% increment capture will see significantly less fiscal benefit and could encourage more municipal borrowing.
  - The types of projects eligible for TIF funds: Vermont’s specific project criteria attempt to ensure that TIF is being used for developments that enhance the public good within a TIF municipality. Vague definitions of project eligibility in



- other states have led to TIF overuse with unclear public benefits at the municipal or state level.
- The length of time a TIF is entitled to retain tax increment: Limiting TIF lifespans to 20 years allows Vermont TIF districts to have more credible forecasts of taxable value and tax increment. Additionally, the shorter lifespan equates to a lower fiscal cost to the State and curbs municipal debt burdens for TIF. The exceptions to this are Burlington’s Waterfront and Milton North and South TIF district where the retention period was extended. However, if incremental tax revenues from a TIF exceed TIF debt service, Vermont municipalities are not required to repay their debt early, which would shorten the retention period.
  - Voter approval and public hearings: Vermont’s requirement that TIF establishment have a public hearing and that TIF debt be approved by voters acts as a check on TIF’s overuse.
- **Despite TIF financing occurring in large part through statewide education property tax revenues, statute does not require a cost-benefit analysis from a statewide perspective as part of the approval process.<sup>8</sup> Moreover, unlike the Vermont Economic Growth Incentive Program (VEGI), analysis of potential economic benefits from TIF is not subject to a quantitative analysis through an economic model.**
  - **Administratively, Vermont’s program excels in being transparent relative to other states but could improve its systems to make TIF districts more accountable for results.**
    - Transparency: Vermont provides more easily accessible information on its TIF districts relative to other states. This includes application information and annual reports. The need for transparency in TIF is important because the fiscal impact of TIF is “off-budget,” meaning the money diverted to finance TIF district projects is neither appropriated nor estimated as part of the budgetary process.
    - Accountability: Vermont’s TIF districts set objectives at their creation but these objectives are only partially monitored by VEPC. VEPC has little recourse should a TIF district not meet economic development objectives.

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<sup>8</sup> 32 V.S.A. § 5404a.

## **i. Statutory: Evaluation of how well Vermont's statute limits the potential downsides to TIF**

Evaluating the statutory definitions of Vermont's TIF program requires comparing Vermont's TIF legislation with other states. While all states except Arizona have some form of TIF statute, there is substantial variation in the characteristics of TIF laws across the country. This makes direct state-to-state comparisons difficult.

However, six parameters of TIF are common to all TIF programs across the country. These parameters are:

- The types of taxes eligible for TIF: While every TIF program allows for the retention of incremental tax revenues, states vary on the types of taxes (property, sales, income, other revenues) that are eligible for paying TIF debt.
- The portion of the tax increment eligible for TIF: When incremental tax revenues are generated, they are split: some percentage is used to pay TIF debt and some percentage flows to the municipality or state. States vary on this division of revenues.
- The types of projects eligible for TIF funds: Across the country, incremental tax revenues from a TIF district could be used to finance a variety of projects: infrastructure, new housing, retail buildings, and office complexes. States have different laws specifying the types of projects eligible for these funds.
- The length of time a TIF is entitled to retain tax increment: In most states, a TIF district is entitled to collect incremental tax revenues for only a certain period of time. Once that time period is over, all incremental tax revenue flows to the municipality and/or state.
- Voter approval and public hearings: When a potential TIF district's application is under review, states may hold public hearings on the plan. Moreover, some might require that voters approve the district or the debt a municipality incurs for its TIF district.
- Feasibility tests or cost-benefit analyses: Before approving a new TIF district, a municipality or state may want some level of justification for using the incentive, either by examining whether it is likely to generate incremental tax revenues and/or by determining whether the project will bring new economic growth and public benefit.

Table 2 reviews Vermont's statute around these parameters. It compares Vermont's statute to the practice in other states. Next, it outlines why strong statutory definitions around these parameters help mitigate the potential disadvantages to using TIF. Finally,

it provides an evaluation of how well Vermont's statutory rules and definitions limit the negative consequences of using TIF.

**Table 2: Evaluation of Vermont's TIF Statute Relative to Other States**

<b>TIF Parameter</b>	<b>What is in Vermont statute?</b>	<b>What is the practice in other states?</b>	<b>Why is strong statute important?</b>	<b>Evaluation of Vermont's program</b>
The types of taxes eligible for TIF	<ul style="list-style-type: none"> <li>The State allows for the capture of two types of property taxes: the municipal property tax and the statewide education property tax. (24 V.S.A. § 1894)</li> </ul>	<ul style="list-style-type: none"> <li>TIF in all states allow for municipal property taxes to be retained.</li> <li>15 states allow sales tax increments to be retained.<sup>9</sup></li> <li>3 allow for income taxes to be retained.</li> <li>Some other states allow for other revenue streams: PILOTS, parking fees, payroll taxes.<sup>10</sup></li> <li>No other state retains a statewide property tax for TIF districts.</li> </ul>	<ul style="list-style-type: none"> <li>Restricting the number of revenue sources could limit the amount of debt a municipality can incur.</li> <li>Limiting this debt mitigates potential downside risks to TIF. If actual tax increments fall short of what was initially projected, a municipality may need to divert resources from other areas of its budget.<sup>11</sup></li> <li>Limiting TIF revenue to property tax increments provides a less volatile revenue stream.</li> </ul>	<ul style="list-style-type: none"> <li><b><u>Vermont's statute helps prevent TIF downsides better than other states.</u></b></li> <li>Vermont's TIF statute, limiting a TIF district to property taxes, ensures a more stable revenue source for TIF debt.</li> <li>By curbing the amount of debt a municipality can take on, it limits the amount of fiscal pressure a municipality could face if actual tax increments miss projections.</li> </ul>
The portion of state tax increments permitted to be captured for TIF debt	<ul style="list-style-type: none"> <li>TIF district is entitled to retain up to 70% of the State education property tax increment, and a municipality must commit at least 85% of its municipal property tax increment.</li> <li>This only applies to new districts; most Vermont TIF districts have a limit of 75% State education property tax increments and 75% of municipal property tax increments. (24 V.S.A. § 1894)</li> </ul>	<ul style="list-style-type: none"> <li>Varies from state to state.</li> <li>In general, most states allow municipalities to retain 100% of the municipal property tax increment.</li> <li>In those states that allow other types of statewide tax increments (state sales, income, etc), the portion the TIF district is permitted to retain varies.</li> </ul>	<ul style="list-style-type: none"> <li>Restricting the amount of revenue available to finance TIF debt limits the amount of debt a municipality can incur.</li> <li>Limiting the amount of debt a municipality can incur mitigates downside risk if actual tax increments fall short of projections.</li> </ul>	<ul style="list-style-type: none"> <li><b><u>Vermont's statute is well-defined and has clearer objectives, relative to other states</u></b></li> <li>The 70/30 split for education property taxes allows the Education Fund to see potential fiscal benefits even during the life of the TIF, as opposed to governments that allow 100%.</li> <li>Vermont's unique 85% floor on the municipal property tax encourages municipalities to take greater ownership of their TIF districts and may help limit fiscal downside to the State.</li> </ul>

<sup>9</sup> Even if a state tax is not involved in TIF, for those states that provide state aid to municipalities for education, they may be indirectly bearing a fiscal cost because of TIF. See Box 2 in the Appendix for further explanation.

<sup>10</sup> Kerth, Rob and Baxandall, Phineas. "Tax Increment Financing: The Need for Increased Transparency and Accountability in Local Economic Development Subsidies." U.S. Public Interest Research Group. 2011.

<sup>11</sup> For an example of the potential downside fiscal risks, see Box 3 in the Appendix on Louisville, Kentucky.

Table 2 continued

TIF Parameter	What is in Vermont statute?	What is the practice in other states?	Why is strong statute important?	Evaluation of Vermont's program
The types of projects eligible for TIF funds	<ul style="list-style-type: none"> <li>The funds must be used for infrastructure or related costs.</li> <li>TIF districts will be approved only if the proposed district includes three of five project criteria: Substantial public investment required, affordable housing, transportation improvements, new businesses, and the cleanup of a brownfield. (32 V.S.A. § 5404a)</li> </ul>	<ul style="list-style-type: none"> <li>The requirement that TIF funds only be used for infrastructure exists in some but not all states.</li> <li>Some states, like California<sup>12</sup> and Iowa,<sup>13</sup> require that a certain percentage of TIF funds be used for affordable housing.</li> <li>Many states (including but not limited to Kentucky<sup>14</sup>, Iowa<sup>15</sup>, New Jersey<sup>16</sup>, and Oklahoma), simply require that the project create new economic activity in a previously blighted area.</li> </ul>	<ul style="list-style-type: none"> <li>Helps ensure that state or municipal priorities are being fulfilled and the public benefits from the TIF district,</li> <li>Prevents unchecked overuse of TIF. As an increasing percentage of a municipality or state's tax base is frozen because of TIF, the fiscal impacts become greater.</li> <li>If the only criterion for TIF district approval is showing that new development will create new economic activity for the municipality or state, then all new projects could be eligible for a TIF incremental revenues.</li> </ul>	<ul style="list-style-type: none"> <li><b><u>Vermont's statute helps to prevent excessive use of TIF and may lead to more publicly beneficial projects.</u></b></li> <li>The benefits of these project criteria are evident. TIF districts in Vermont almost always include some public improvement project such as a park or affordable housing. For example, TIF has been used to create public space and improve traffic flow in Winooski and construct a bike path along the Burlington Waterfront.</li> <li>The restricted project criteria prevent TIF from being used for any private development, an issue in other states.</li> </ul>
Length of time a TIF district is entitled to retain tax increments	<ul style="list-style-type: none"> <li>Municipalities are entitled to up to 20 years of tax increment retention from the date the first debt is incurred to build infrastructure. (32 V.S.A. § 5404a)</li> <li>Two of the ten active TIF districts have received extensions.<sup>17</sup></li> </ul>	<ul style="list-style-type: none"> <li>The majority of states limit TIF district lifespans to between 20 and 30 years. However, some allow TIF districts to retain tax increments for greater than 30 years.<sup>18</sup></li> </ul>	<ul style="list-style-type: none"> <li>Shorter retention periods allow for more accurate forecasts of property values or economic activity.</li> <li>Longer retention periods enable a municipality to incur more debt for their TIF districts, exacerbating potential downside fiscal risks.</li> <li>Longer retention periods freeze municipal and state property tax bases for a longer period of time, increasing potential fiscal costs.</li> </ul>	<ul style="list-style-type: none"> <li><b><u>Vermont's shorter retention period results in more accurate projections and less potential downside risk compared to other states.</u></b></li> <li>Allows municipalities to finance debt over a longer period, but also could result in more accurate projections of their revenue flows (albeit still with considerable uncertainty).</li> <li>Curbs larger debt burdens.</li> <li>Also likely lessens the fiscal costs to the State and municipality.</li> </ul>

<sup>12</sup> California Assembly Bill 2492 of 2016.

<sup>13</sup> Iowa House File 2460 of 2012.

<sup>14</sup> KRS 154.30 040, 050, and 060.

<sup>15</sup> Iowa House File 2460.

<sup>16</sup> New Jersey Economic Stimulus Act of 2009.

<sup>17</sup> 10 years for Milton's North and South and 20 years for Burlington's Waterfront.

<sup>18</sup> Kerth, Rob and Baxandall, Phineas. "Tax Increment Financing: The Need for Increased Transparency and Accountability in Local Economic Development Subsidies." U.S. Public Interest Research Group. 2011.

**Table 2 continued**

TIF Parameter	What is in Vermont statute?	What is the practice in other states?	Why is strong statute important?	Evaluation of Vermont’s program
<p>Voter approval and public hearings for TIF districts</p>	<ul style="list-style-type: none"> <li>• Municipalities are required to hold a public hearing on the proposed TIF district. (24 V.S.A. § 1892)</li> <li>• Voters are required to approve debt for a TIF district. (24 V.S.A. § 1904)</li> </ul>	<ul style="list-style-type: none"> <li>• 36 states require a public hearing for TIF district approval,</li> <li>• Many do not require public approval for a TIF district to incur debt.<sup>19</sup></li> </ul>	<ul style="list-style-type: none"> <li>• Locally, TIF districts can shape the development and use of land for an entire community, so public involvement is important.</li> <li>• The public should at least be informed of fiscal impacts of TIF (debt service and potentially forgone tax revenues).</li> <li>• Voter approval of debt can provide a check on TIF expansion because residents could veto a district if they deem it would negatively infringe upon the quality of municipal services.<sup>20</sup></li> </ul>	<ul style="list-style-type: none"> <li>• <b><u>Public involvement in Vermont’s TIF approval could help slow TIF expansion and ensures TIF creates public benefit.</u></b></li> <li>• TIF districts have not spread in Vermont as they have in other states, due at least in part to this public involvement.<sup>21</sup></li> <li>• TIF districts in Vermont also almost always include some publicly beneficial project beyond new economic activity, in part because the public has a voice in their approval.</li> </ul>
<p>Feasibility studies and analysis of but-for claims</p>	<ul style="list-style-type: none"> <li>• VEPC’s reviews whether the development at the municipal level would have occurred, or occurred in a significantly different way or timeline, without the use of TIF.<sup>22</sup></li> <li>• VEPC requires municipalities to produce projections of development, property value growth, tax increment, and debt repayments. (32 V.S.A. § 5404a)</li> </ul>	<ul style="list-style-type: none"> <li>• 18 states specifically require a but-for test; however, these are difficult in most cases to implement meaningfully.</li> <li>• 23 other states require a feasibility study or a cost-benefit analysis, although it is not always clear what parameters these cost-benefit analyses attempt to measure.<sup>23</sup></li> </ul>	<ul style="list-style-type: none"> <li>• Without meaningful but-for analyses, there is no way to determine whether the project is a fiscal cost or not.</li> <li>• A feasibility test forces municipalities to create projections of future property growth, tax increments, and debt service payments and determine how likely they are to be achieved.</li> <li>• If there is state participation in TIF, a cost-benefit analysis examines whether TIF is providing statewide benefit.</li> </ul>	<ul style="list-style-type: none"> <li>• <b><u>Statute could be improved to ensure that TIF developments will create statewide benefit, not only municipal benefits.</u></b></li> <li>• Because State revenues are involved, any TIF district would need to show it provides statewide economic benefits.</li> <li>• Use of a quantitative model, such as the VEGI Cost-Benefit model, could help inform the approval process by showing which projects are likely to yield statewide benefits.</li> </ul>

<sup>19</sup> Kerth, Rob and Baxandall, Phineas. “Tax Increment Financing: The Need for Increased Transparency and Accountability in Local Economic Development Subsidies.” U.S. Public Interest Research Group. 2011.

<sup>20</sup> For an example of how voter approval can curb rapid TIF expansion in a state, see Box 4 on California’s Redevelopment Authorities in the Appendix.

<sup>21</sup> There are other statutory limits that checks TIF expansion. These include placing a cap on the number of new districts (6) and project and location criteria.

<sup>22</sup> Only the post-2010 TIF districts were required to meet a but-for test (four out of the 11 TIF districts established in Vermont).

<sup>23</sup> Ibid

## **ii. Administrative: Evaluation of the level of transparency and accountability of Vermont's TIF districts**

Statute sets the limitations of TIF upon approval. However, once a district is approved, examination should be given to whether these programs are serving the public benefit. This section examines the degree to which TIF districts' operations in the State are:

Transparent: How easy is it for a member of the public to obtain information about Vermont's TIF districts and their performance?

Accountable: Once the district is created, how well does Vermont monitor the district and evaluate whether it is achieving the objectives set out in statute and in its application?

### a) Transparency: An analysis of how easy it is to obtain information on Vermont's TIF districts

Current TIF District information disclosure: VEPC's website contains a wealth of information on Vermont TIF districts. This includes general information on the basics of TIF and the TIF district application process. One can easily find information on all existing TIF districts within VEPC's annual report, including projected growth in original taxable value, tax increments, and development within each TIF district. The reports also outline the goals of each district and how well the district has moved toward them. Finally, the website contains each district's application. These applications include information related to projected development, justifications for the use of TIF, and data on tax increment projections and future property value growth.

Benefits to providing easy-to-access information to the public: Providing all available information on public programs generally is a practice of good government. TIF is no exception.

Providing information on TIF districts to the public is a way of increasing oversight for the program, beyond what the State or municipality requires. Providing public information on the types of projects involved in a TIF district plan can help ensure that these projects provide some level of public benefit. Moreover, the public can provide an additional oversight role to ensure that districts are following through on the promises made in their applications.

Finally, while TIF is not an outlay of the government, it is a tax expenditure that affects the Education Fund tax base. A portion of incremental growth in property taxes is no longer being remitted to the government but instead is used to finance TIF debt.

Because the program involves public money, the public should have easy access to information on the program.

#### Evaluation of Vermont's access to information:

In Vermont, the amount of publicly available information available surpasses nearly every other state examined by JFO. Research completed by JFO found that most states do not track data on their TIF districts since they are mostly municipal programs without direct state involvement. Even for those states that do have involvement (by permitting the retention of state taxes), few provide the level of easily accessible information that Vermont does. While some states provide information on existing districts, as well as information about the total incentive size, JFO could not find easy access to other states' TIF district applications. Among cities, the degree of transparency in the administration of TIF districts varies significantly. Some cities, such as Chicago, release a significant amount of data on their website. However, the majority of cities simply list active TIF districts and a basic TIF explainer on their websites. Numerous critiques of TIF have highlighted this lack of transparency.<sup>24</sup>

While Vermont provides a significant amount of information to the public on its TIF districts relative to other states, there is some minor room for improvement. Statute requires annual reporting of TIF districts, updating VEPC on realized development and tax increments for each year, expenditures for debt and related costs, and new economic activity such as jobs created.<sup>25</sup> The municipalities provide this detailed information to the State; however, much of it is not easily accessible online for a member of the public. VEPC's annual TIF report contains some of the data, but they are often aggregated and do not contain all the information provided by the municipality.

Easily accessible online information about TIF districts is more limited at the municipal level. The City of Burlington provides some information about its TIF districts (basic information about the district, some data on new property value growth, maps of the district). Other municipalities contain only TIF primers and maps of their districts. This lack of information is, at least in part, mitigated by the fact that VEPC provides most of the municipal information as part of its oversight role.

#### b) Accountability: an analysis of Vermont's system of oversight and evaluation of TIF district performance.

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<sup>24</sup> Examples include Chicago's 2011 Task Force Report on TIF, Bieri and Kayanan (2014), and Kerth and Baxandall (2011).

<sup>25</sup> 24 V.S.A. § 1901.



Current TIF district oversight and evaluation in Vermont: Administering a TIF district in Vermont is largely the responsibility of the municipality: the town assesses all properties each year, taxes the properties, calculates tax increments, and services the debt of the TIF district. While many towns hire a consultant to help prepare their applications for TIF approval, none uses consultants to administer their programs.

In addition to VEPC's initial role in approving the districts, VEPC also assumes an ongoing monitoring role. Districts are required to submit annual reports to VEPC, including information on development progress, incremental revenues, jobs created, and other performance measures.

In addition to VEPC's ongoing monitoring role, in 2012, the Office of the State Auditor reviewed the operational performance of four pre-2010 TIF districts (Burlington Waterfront, Milton North and South, Newport, and Winooski).<sup>26</sup> The audits found that the municipalities generally complied with statutes when establishing TIF districts, but made errors when calculating incremental taxes. The audits also found that TIF districts collectively owed \$6 million in taxes to the State Education Fund due to incorrect calculations of tax increments.

These audits helped spur meaningful legislative action that provided clearer TIF definitions and required more accountability. Examples of changes to legislation since these audits include<sup>27</sup>:

- Clearer definition of "original taxable value," the base value of all parcels in the district and used for calculating property tax increments.
- Clarifications around the length of time a district is eligible to retain TIF funds.
- Requirement that TIF districts submit annual reports to VEPC by February 15 of each year.

The State Auditor's Office is required in statute to conduct performance audits of Vermont's TIF districts in the future. The schedule of these audits depends on when they were established and are different for the pre-2010 and post-2010 TIF districts.

The reports provided to VEPC each year provide data regarding tax increments, investments, and jobs created. They also provide a way for the State to track where TIF funds were being spent. However, unlike the audits, these reports do not verify if tax increments were properly calculated or if statute is being followed.

Benefits to a strong monitoring and evaluation framework for TIF districts: Because TIF is a public program designed to incentivize economic development within high-density

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<sup>26</sup> <http://auditor.vermont.gov/sites/auditor/files/files/reports/performance-audits/Tax-Increment-Financing-Capstone-Report-12.31.12.pdf>

<sup>27</sup> For a full list of legislative changes, please see Appendix Table A1.

or downtown areas and create public benefit at the municipal level, there are advantages to monitoring and assessing regularly how well TIF is achieving that goal.

Monitoring ensures that the rules set out in statute are being followed. State statute mandates that any approved TIF district include certain projects (the location criteria). Regular monitoring determines the extent to which a municipality has completed the projects proposed in its application and that these projects conform to the location criteria. Monitoring TIF districts also would help ensure that each municipality is remitting the statutory percentage of property tax increment to the State.

Monitoring also allows the State or municipality to track the TIF district's financial health. If the State and municipality regularly monitor TIF districts' financial performance, it would allow them to act early at the first sign of shortfalls in tax increment, rather than acting when the situation is more urgent.

Finally, performing in-depth and comprehensive evaluations of TIF district performance is necessary to determine whether the State and municipality are receiving returns on their investment, both from fiscal and economic activity perspectives. These evaluations could also help inform legislators and VEPC about the success of the program at achieving statutory goals but also about potential tweaks to legislation to make the program more effective.

Evaluation of Vermont's oversight and evaluation system: JFO finds that, generally, VEPC's oversight and evaluation of TIF districts exceed the levels in most states. The current annual reporting requirements contained in VEPC's Annual Report exceed those in many other states. Some, but not all, states require statewide reports (Missouri, Nebraska, and Ohio, to name a few). Municipalities in other states produce annual reporting on their TIF districts, regardless of whether there is a state statute to do so. These reports range from a simple overview of the balance sheet of a TIF district to a full analysis of new economic activity. In addition, VEPC regularly works with approved TIF districts on an ongoing basis to help them determine whether their proposed projects follow VEPC's TIF Adopted Rules.

Moreover, Act 80 of 2013 established an audit schedule for both pre- and post-2006 TIF districts which are completed by the State Auditor's Office. The State Auditor's Office also helped establish the procedures used by independent auditors hired by the municipalities. This oversight helps ensure that tax increments are being properly calculated and remitted to the appropriate funds.

However, JFO finds that Vermont's TIF program could benefit from improved evaluation of whether the program is meeting economic development objectives, particularly at the State level. During the approval process, JFO finds that statute and VEPC are primarily focused on the benefits TIF could create for the individual municipality, not the State as

a whole. Furthermore, JFO could not find evidence of regular, independent evaluation of economic benefits.

One of the State Auditor's findings in 2012 was that municipalities did not establish meaningful performance objectives or track TIF district progress toward any objectives they did create. The requirement that TIF districts provide annual reports to VEPC has improved this; however, JFO believes that these annual reports are not sufficient for evaluation of economic benefits to the State.

JFO believes that VEPC's Annual Report provides more of a reporting function rather than an evaluation function. The Annual Report provides data on property values, tax increments, and debt profiles. While this is useful information, the report does not provide a deeper analysis or evaluation of whether the program is providing the statewide benefits necessary to justify the use of the statewide education property tax revenue. Just because individual TIF municipalities experience economic growth does not mean that the entire State benefits from the program (see Section C: Economic Impact sections for further discussion). Making use of a quantitative economic model, similar to VEGI's Cost-Benefit model, might help provide insight in this regard.

Another type of evaluation that could improve the report is a comparison of actual property value growth and incremental tax revenues compared to what the municipalities expected in their applications. This information could be valuable to inform legislators about the financial viability of the TIF districts. For example, if a municipality had bonded against incremental tax revenues that fall short of projections, the Legislature would be informed of this well in advance. (This exercise is performed in Section C: Economic Impacts.)

Moreover, an important argument for TIF is that TIF indirectly creates economic benefits associated with downtown, dense development. VEPC's Annual Report does not contain any information on these economic benefits, nor could JFO find any estimates of the benefits completed by VEPC or the municipalities.

On the municipal level, there does not appear to be monitoring by municipalities to determine whether TIF is achieving the goals set out at the application (if there were any clearly defined) outside what they report to VEPC. Additionally, like shortcomings at the State level, there do not appear to be deeper municipal analyses of whether the economic development impacts are directly attributable to the use of TIF.

In sum, JFO concludes the TIF program's evaluation process could be improved by requiring independent, regular (every 5 to 7 years) examination of statewide economic benefits. This could be completed by an independent consultant or as a supplement to the State Auditor's performance audits. Requiring these independent evaluations would

inform legislators whether the program is providing the necessary statewide economic benefits to justify the use of statewide education property tax revenue.

## **B) Fiscal Impacts: Estimating Costs and Benefits of TIF using JFO Model**

This section estimates the fiscal impact on the State's Education Fund. The framework for these estimates is a model constructed by JFO using assumptions for TIF district property value growth and assumptions for property value growth absent the use of TIF.

### **i. Summary of fiscal impact estimates**

To estimate the fiscal impacts of TIF on the State's Education Fund going forward, JFO constructed a model that compared the revenues to the Education Fund for a TIF district against the revenues to the Education Fund of a hypothetical baseline scenario with no TIF. The difference between these two scenarios was the cost/benefit to the Education Fund; if the TIF district provided greater revenues than the baseline scenario, it was positive net benefit. If the baseline scenario provided greater revenues than the TIF scenario, then it was net cost to the Education Fund. This methodology was also used to calculate the fiscal impacts on municipal general funds, in aggregate.

This methodology for estimating fiscal impacts differs from both VEPC's and the Legislative Economist's. VEPC's estimates of fiscal impacts to the Education Fund assume that no growth would have occurred within the TIF district for 20 years absent the use of TIF (0% baseline growth). The Consensus Administration/JFO Education Fund Outlook estimates assume that all the growth that occurs within a TIF district would have occurred anyway and therefore any diverted tax increments represent a fiscal cost (baseline and TIF district growth are always equal). The full fiscal cost of the program to the State Education Fund is estimated by the Consensus Administration and JFO Education Fund forecast as part of the Education Fund outlook. These estimates are shown in Table A3 in the Appendix.

For JFO's estimates, the following mid-range assumptions were made:

- JFO assumed future nominal growth in TIF district property value of 6% year-over-year, which is similar to what Vermont's TIF districts predicted their growth would be in their applications, on average. This growth assumption was applied for the first ten years of a TIF district's lifespan. Thereafter, the TIF district's county average growth rate over the past 20 years was applied.
- For the baseline, no-TIF scenario, the 20-year county average grand list growth rate plus or minus 50 percentage points was applied to the original taxable value for every year. For non-Chittenden County TIF districts, this growth rate was

reduced by 50 percentage points. For Chittenden County, this growth rate was increased by 50 percentage points.

- Vermont's ten active TIF districts will incur all the debt projected in their applications. This assumption is based upon conversations with municipalities and VEPC.
- State education property and municipal property tax rates are assumed to be flat going forward. This is the assumption TIF applicants now use in their applications.
- JFO also examined fiscal impact estimates using VEPC and the Legislative Economist's assumptions: that no growth would have occurred absent the use of TIF (0% baseline growth) or that all development would have occurred anyway (baseline and TIF district growth are equal).

Depending on the assumptions used, the fiscal impacts on the State Education Fund could vary significantly. JFO also examined fiscal impact estimates using VEPC's (0% baseline, no-TIF growth) and the Legislative Economist's (baseline and TIF district growth are equal) estimates in the Appendix (Tables A3 to A6). In nearly all instances, with the exception of VEPC's assumptions (0% baseline, no-TIF growth), TIF represented a fiscal cost to the State Education Fund. Although the cost of TIF is small relative to the overall size of the Education Fund, this cost puts the TIF program as one of the largest economic development programs the State offers (in dollar terms), and the largest program for municipal urban development.

**Using JFO's mid-range assumptions, the model estimated the following fiscal impacts:**

- **Between 2017 and 2023, the TIF program represents a negative cost to the Education Fund of between \$3 million and \$6 million (in nominal dollars) per year. The five additional TIF districts that have not been identified but approved by the Legislature in 2017 are not included, and if included, would likely increase this loss.**
- **From 2023 to 2028, the net negative cost to the Education Fund fluctuates between \$6 million and \$7 million (nominal dollars) per year and decreases thereafter.**
- **From 2017 to 2030, based upon only active TIF districts and assuming no new districts will be created, TIF will cumulatively cost the Education Fund approximately \$68 million (in nominal dollars).**

- For municipal general funds in Vermont, on aggregate, from 2017 to 2030, TIF will cost an additional \$2 to 5 million per year, and nearly \$43 million over the entire period (in nominal dollars).
- Using an alternative scenario that assigned a uniform 3.3% baseline growth rate for non-TIF growth to all TIF districts (based upon the latest Education Fund forecast for 2017-2023), the cost decreases to between \$1 million and \$4 million annually until 2023, and \$31.6 million cumulatively from 2017 to 2030 (in nominal dollars).
- For the purposes of calculating education property tax rates each year and the size of TIF's cost as a tax expenditure, JFO continues to support using the methodology and estimates from the Consensus Administration and JFO Education Fund Outlook (\$5 to \$10 million per year). These estimates are discussed more completely in Appendix Table A3.
- On average, using nominal dollars, it will take more than 50 years from the beginning of a TIF district for cumulative revenues to the Education Fund from a TIF district to break even with the revenues from the same area without a TIF. Using inflation-adjusted dollars, this break-even point is pushed even further into the future.
- Regarding TIF district debt outstanding, using a future TIF property growth of 6% annually for the first 10 years and historical county growth rates for the next 10 years, six of the ten active TIF districts will be able to repay their TIF debt by the end of their retention periods.

## **ii. Current and Future Debt Obligations for Vermont TIF districts**

Since the inception of TIF in the late 1990s, the combined 11 TIF districts have incurred \$88,375,773 in debt to fund infrastructure improvements. Of the 11 TIF districts, only Newport has fully repaid its debt and become inactive.

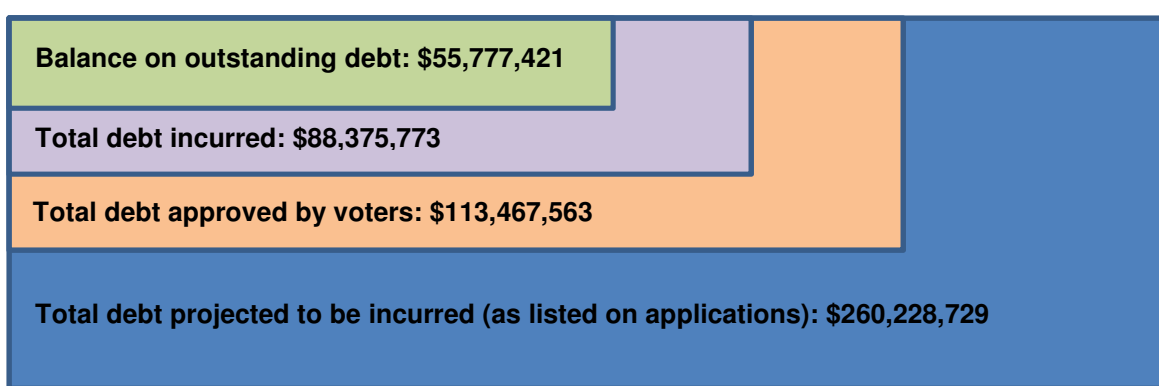
Of this \$88,375,773 TIF debt, \$55,777,421 is still outstanding and \$32,598,242 has been repaid by TIF districts (see Figure 1).

Although Vermont's TIF districts have incurred only \$88,375,773 in debt, voters have approved up to \$113,467,563 to be incurred. This means that although some municipalities have asked voters to approve debt for a TIF district, they have yet to borrow the fully approved amount. For instance, for the St. Albans TIF district, voters have approved up to \$16,000,000 in TIF debt, but the city has only formally borrowed

\$12,400,000. In Vermont, municipalities tend to borrow as they build; a municipality will not borrow money until the project is shovel-ready.

According to TIF district applications, the sum of all projected borrowing for the 11 total districts is \$260,228,729 over all TIF lifespans. The difference between this \$260,228,729 and the \$113,467,563 amount that voters have approved is explained by the fact that some districts have had their applications approved but have not had any votes on new debt (South Burlington) or that districts plan on returning to voters for additional debt approval sometime during the lifespan of the TIF. Figure 1 summarizes the current and projected debt for Vermont's TIF districts.

**Figure 1: Current and Future Debt Obligations of Vermont TIF Districts**



Source: 2017 Annual Report on TIF Districts in Vermont, VEPC

The financing for infrastructure projects comes from various sources. The majority of the time, municipalities bond through the Municipal Bond Bank. This being said, municipalities may use other sources of debt finance for their projects. This includes private financing (banks) and other types of federal and state loan programs. In Vermont, unlike many TIF districts around the country, TIF debt is rarely financed as a revenue bond (where a municipality bonds against tax increments directly). In Vermont, if a municipality issues bonds to pay for infrastructure, TIF is usually just one of a suite of revenue sources to repay that debt.

This method of financing has both advantages and disadvantages. By not linking debt repayment directly to the bonds themselves through a revenue bond, a municipality can repay debt using many revenue sources. The use of many revenue sources might also help mitigate downside risk if future tax increments do not materialize as planned. On the other hand, this mix of financing makes it difficult to determine whether a TIF district is achieving expectations of future tax increments; one indicator of a successful TIF district is being able to generate enough tax increments to finance its debt; that the TIF development “pay for itself.”

**For these reasons, it is difficult to determine whether the amount of debt incurred and projected offsetting revenues are sustainable.** The ability to pay off debt during the life of the TIF (also known as the retention period) will depend on the growth in each TIF district and the amount of non-TIF revenues (outside sources of funds; State and federal grants, for example) available to the municipality going forward.

**Assuming that there will be no non-TIF revenue used to repay debt going forward, and that TIF district property value growth is 6% year-over-year until the end of their debt voting period, six of the ten active TIF districts will be able repay their debt before the end of the retention period using incremental tax revenues alone.** However, it should be stressed that these repayment schedules vary significantly depending on the future property value growth of the TIF districts. Moreover, it should be noted that a municipality need not repay all debt by the end of its retention period. It could simply use normal tax revenues in the post-retention period to service debt.<sup>28</sup>

The debt situation plays into the fiscal impact that TIF has on the State and municipality in two ways:

- For any given TIF district, the sooner it is able to repay its debt, the sooner the State and municipality will benefit from the full tax benefit of new development in the TIF district. Early repayment of debt is not required in statute or VEPC's TIF Adopted Rules.
- Although this has not occurred in Vermont, if tax increments fall significantly short of projections, putting pressure on a municipality's ability to make debt payments, municipalities will be forced to use other sources of municipal revenue. This situation would represent a negative fiscal impact, potentially with consequences on statewide municipal borrowing.

### **iii. Introduction to the JFO fiscal impact model**

Determining the fiscal impact of TIF hinges upon the strength of the but-for condition.

The but-for condition states that no comparable development would happen in the proposed TIF district area if not for the use of the incentive. If examining fiscal impacts at the State level, then the but-for condition states that no comparable development would have occurred anywhere else in the State. If this but-for condition is correct, then TIF would never be a net fiscal cost to the State or the municipality under current statute. In other words, even if the State or municipality would not receive the full

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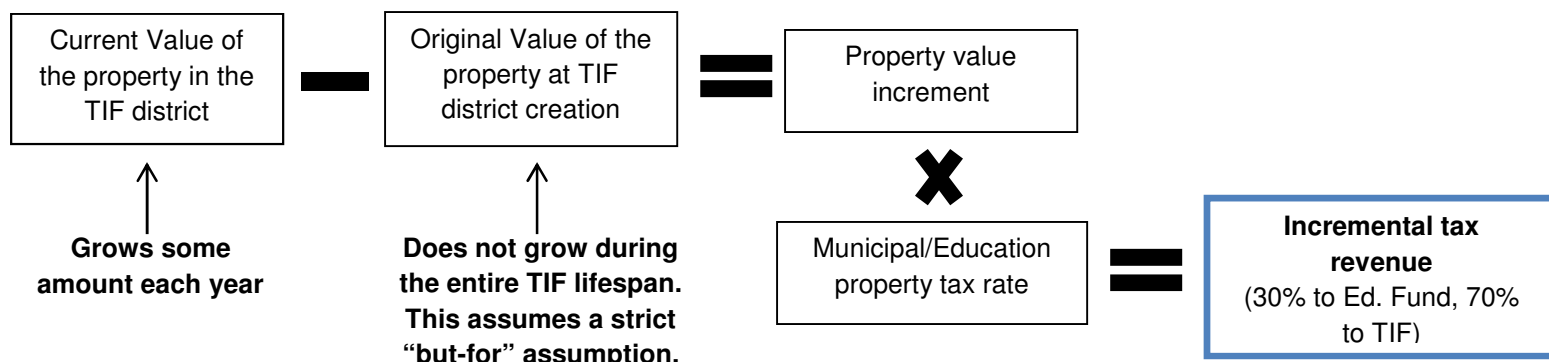
<sup>28</sup> These estimates assume that the TIF district will incur all the debt projected in their application. It is unclear how likely this is to occur in Vermont's TIF districts. Each district is required to incur debt within five years of the approval of their application. Once the district incurs the first debt, it has an additional ten years to incur any additional debt. However, once the municipality incurs that first debt, it has 20 years to retain statewide property tax increments.



amount of new tax revenues from new property development in a TIF district, the portion it does receive would always be more than what it would have received if no development occurred.

**Currently, in Vermont’s TIF program (and all other programs nationwide), incremental tax revenues are calculated from the assumption that the base value of the property in the TIF district would not grow at all (0% year-over-year), but for the use of TIF.**<sup>29</sup> To calculate incremental revenues, a municipality takes the difference between the value of property in a given year (current taxable value) and the value of the property when the TIF was established (base value). The base value in this calculation does not experience any growth over the course of the TIF lifespan. As the value of the property grows, the size of the incremental tax revenue grows. Figure 2 illustrates this calculation.

**Figure 2: Current calculation of incremental tax revenue**



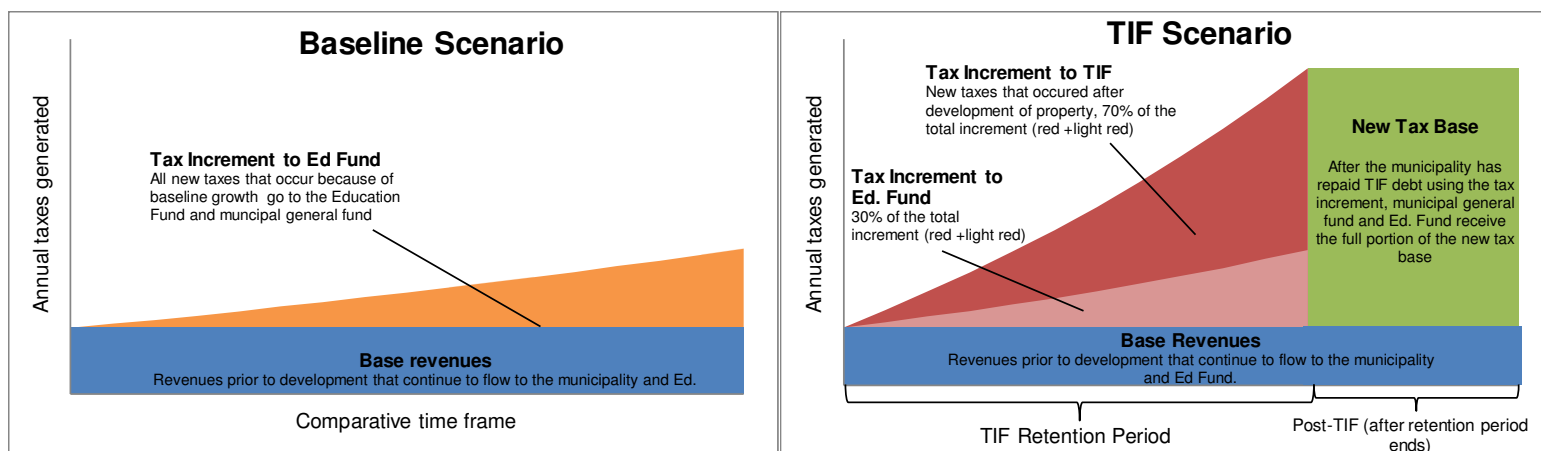
**JFO’s model, instead of keeping the base value of the property flat into the future, assumes positive baseline growth; that some growth would have occurred absent the use of TIF.** The model creates a baseline scenario, where TIF was not used. In this scenario, rather than assuming zero growth, the model assumes that the value of property would have grown to some extent absent the use of TIF. However, under this scenario, because there is no TIF, the municipality and Education Fund receive the full portion of any tax increment, rather than forgoing 70% to 75% of it to finance TIF debt. It is important to note that for estimates of Education Fund costs/benefits, this non-zero baseline growth could mean that growth would have occurred either in the TIF district geographic area or somewhere else in the State.

**This model estimates costs by comparing the revenues to the Education Fund and municipal general funds under a TIF versus those revenues without TIF but the value of the land grows by some baseline growth assumption.** JFO’s model

<sup>29</sup> See 24 V.S.A. § 1896.

estimates the net cost or benefit to using TIF by taking the difference in these respective revenues. If the baseline, no-TIF scenario provides greater revenues to the Education Fund than using TIF, then using TIF is a cost. If TIF provides greater revenues, the difference in the tax revenues to the Education Fund under a TIF and the baseline scenario is the fiscal benefit of using TIF. Figure 3 illustrates this calculation:

**Figure 3: Comparing Baseline vs. TIF Scenarios**



Under the baseline scenario, with no TIF, the orange portion is the amount of tax revenue the Education Fund would receive under a baseline growth assumption. In the TIF scenario, the light red portion represents the return to the Education Fund; however, it is only 30% of the total tax increment (the dark and light red combined). If the orange portion is larger than the light red portion, it is a hypothetical fiscal loss to the State over that time period.

The estimates the model produces will depend highly upon two important assumptions:

- The baseline growth assumption: the assumption on how much property value growth would have occurred if TIF was not used.
- The TIF growth assumption: the assumption for what kind of property value growth occurs in the TIF district once TIF is used.

The JFO fiscal model makes various assumptions around these two parameters:

- **The baseline growth assumption is the TIF district's respective county average growth rate over the past 20 years, plus or minus 50 percentage points depending on whether the district was in Chittenden County.** This assumption was used because it covers a long-duration, recent peak-to-peak real estate cycle. Using the average of the past ten years would include the Great Recession, which saw large drops in property values. The assumption also provides flexibility among different areas of the State. Each TIF district will have its own baseline growth assumption based upon its county average. Moreover, this assumption attempts to account for differences in property value growth

throughout the State. Chittenden County property values have grown at a much faster rate than other parts of the State so baseline growth assumptions in Chittenden County were shaded upward. Other areas of the State have grown slower so their growth rates were shaded downward.<sup>30</sup>

- **The TIF growth assumption is assumed to be 6% year-over-year.** This assumption is based upon the growth rates assumed in TIF district applications. This growth rate is roughly in line with the compound annual growth rates that Vermont TIF districts assumed in their application, on average. The actual growth assumptions they used varied from 2% to 9%.

The JFO model uses these assumptions for each of the ten active TIF districts in Vermont (including Bennington) and estimates their fiscal impact. It then aggregates them to create a statewide cost to the Education Fund and municipal general funds. JFO excluded five of the recently approved, but not yet active, TIF districts. Inclusion of these additional TIF districts could add additional cost to the program and the estimates outlined herein. JFO also compiled alternative estimates for the Education Fund based upon differing assumptions of baseline growth. These estimates can be found in the Appendix (Tables A3 to A6). Tables A3 and A4 show the Consensus Administration/JFO and VEPC estimates respectively.

This model assumes that property tax rates (statewide education homestead, statewide nonresidential and municipal rates) going forward will be equal to what they were in FY2018. To calculate statewide incremental taxes, since most TIF districts are composed of non-homestead parcels, the non-homestead rate was used. In those TIF districts where homesteads were a significant portion of total parcels, homestead and non-homestead rates were applied. According to VEPC, this flat-growth property tax rate assumption is what municipalities will be using in their applications going forward.<sup>31</sup>

It is important to note that these estimates represent only costs to the Education Fund and municipal general funds resulting from property taxes, not other tax types. Advocates of TIF, including VEPC, believe that these incremental taxes are indeed generated by the use of TIF. On the other hand, the Consensus Revenue Estimates of State revenues do not include any incremental growth in these tax types.<sup>32</sup> JFO's model

<sup>30</sup> The assumption of 20-year average growth or any assumption of a particular growth rate is at best hypothetical. Real estate growth is not consistent and can vary tremendously. Also given the small geographic areas that TIF districts encompass, the ability to project growth is all the more difficult. The JFO model approach is done in full awareness that such assumptions are difficult at best. Instead, it offers one way to understand the comparative issues at play.

<sup>31</sup> Property tax rate growth is a function of municipal and State education spending, as well as the growth in the grand list. Non-homestead property tax rates have fluctuated over the past 20 years, rather than growing consistently every year (See Chart A1).

<sup>32</sup> The Education Fund Outlook reports Education Fund revenues diverted because of tax increment financing as an expense on the Fund. See <http://www.leg.state.vt.us/jfo/education/EF%20Outlook%20-%20FY2017%20Closeout%20and%20Revenue%20Update.pdf> for more information.

does not attempt to estimate fiscal impacts relating to income, sales, or meals and rooms taxes. The use of TIF could conceivably create other incremental tax revenues that could offset some of the potential costs to the Education Fund or municipal general funds. However, research for this report found that while TIF projects could be producing municipal benefits, it is less likely that they are producing net statewide benefits outside those from denser, downtown development (see Section C: Economic Impacts). Any estimates that could be made for these other tax types would be methodologically questionable and need to be compared to a statewide hypothetical baseline, no-TIF scenario.

#### **iv. Estimates of annual net fiscal impacts to the Education Fund**

This section offers an overview of the main results of the JFO model. In general, the model finds that using the assumptions above, TIF represents a net cost to both the State's Education Fund and municipal general funds.

It is important to note that these estimates of fiscal impacts sensitive to the assumptions made around the level of growth which will occur in the TIF district and what might have occurred absent the use of TIF. For example, if baseline growth is projected to be 0% for the entire 20-year TIF lifespan, TIF districts provide positive returns to both the Education Fund and municipal general funds. On the other hand, if the baseline growth is assumed to be the same as the TIF district growth assumption (in other words, that any TIF district growth that occurs would have happened anyway), the fiscal impacts are even less than what JFO estimates. These estimates are shown in Tables A3 and A4 in the Appendix.

Using the two mid-range assumptions specified above, the JFO model estimates the following for the Education Fund (Table 3):

- **TIF represents a cost to the Education Fund of approximately \$3 million to \$6 million per year from 2017 through 2023 (in nominal dollars). Including the additional five districts authorized by the Legislature, but not yet approved by VEPC, would likely increase the size of this cost.**
- **From 2023 to 2028, the negative fiscal impact to the Education Fund fluctuates between \$6 million and \$7 million (nominal dollars) per year. After 2028, once most currently active TIF districts have repaid their debt, the cost decreases to roughly \$3 million per year for the ten active TIF districts only**

- From 2017 to 2030, based upon only the ten active TIF districts and assuming no new districts will be created, TIF will cumulatively cost the Education Fund approximately \$68 million (in nominal dollars).
- Using these assumptions, cumulative revenues to the Education Fund from Vermont TIF districts will not break even with cumulative revenues from that same area without a TIF district for 56 years, on average, in nominal dollars.

<b>Table 3: Fiscal Impacts to the State Education Fund</b> (Using baseline growth of 20-year county average growth +/- 50 percentage points <sup>a</sup> )			
	What it receives under TIF	What it receives under no TIF	Difference (Negative=cost)
2017	\$9,816,447	\$12,816,992	-\$3,000,545
2018	\$10,017,410	\$13,475,088	-\$3,457,678
2019	\$10,923,772	\$14,871,639	-\$3,947,867
2020	\$11,154,097	\$15,615,939	-\$4,461,842
2021	\$11,391,001	\$16,396,504	-\$5,005,503
2022	\$11,629,197	\$17,215,131	-\$5,585,934
2023	\$11,855,820	\$18,073,709	-\$6,217,889
2024	\$12,093,655	\$18,974,219	-\$6,880,564
2025	\$12,719,116	\$19,918,743	-\$7,199,627
2026	\$14,955,666	\$20,909,468	-\$5,953,802
2027	\$15,959,226	\$21,948,690	-\$5,989,464
2028	\$16,450,459	\$23,038,822	-\$6,588,364
2029	\$21,162,518	\$24,182,397	-\$3,019,879
2030	\$24,542,225	\$25,382,076	-\$839,851
<b>Total</b>	<b>\$194,670,610</b>	<b>\$262,819,417</b>	<b>-\$68,148,808</b>

<sup>a</sup> If the district was in Chittenden County, 50 percentage points were added. If it was not, 50 percentage points were subtracted

To check the sensitivity of these results to changes in assumptions, a second, alternative approach was used. Rather than using the 20-year historical average grand list growth rates for the TIF district's county plus or minus 50 percentage points for the baseline scenario, a uniform 3.3% baseline growth rate was applied. This baseline scenario was based on average projected statewide grand list growth from 2017 to 2021 from the October 2017 Education Fund Forecast. The TIF district growth assumption was kept the same as before (6%). The fiscal impacts on the Education Fund are shown in Table 4.

<b>Table 4: Fiscal Impacts to the State Education Fund</b> (Using baseline growth of 3.3% from the October 2017 Consensus Forecast)			
	What it receives under TIF	What it receives under no TIF	Difference (Negative=cost)
2017	\$9,815,848	\$11,205,400	-\$1,389,553
2018	\$10,016,161	\$11,601,183	-\$1,585,022
2019	\$10,909,888	\$12,718,049	-\$1,808,161
2020	\$11,121,446	\$13,162,300	-\$2,040,854
2021	\$11,321,774	\$13,621,212	-\$2,299,439
2022	\$11,500,369	\$14,095,268	-\$2,594,899
2023	\$11,656,889	\$14,584,968	-\$2,928,079
2024	\$11,818,969	\$15,090,828	-\$3,271,859
2025	\$11,986,815	\$15,613,382	-\$3,626,566
2026	\$12,265,899	\$16,153,179	-\$3,887,281
2027	\$14,480,403	\$16,710,790	-\$2,230,387
2028	\$15,060,449	\$17,286,802	-\$2,226,354
2029	\$15,364,180	\$17,881,823	-\$2,517,643
2030	\$19,255,758	\$18,496,479	\$759,279
<b>Total</b>	<b>\$176,574,847</b>	<b>\$208,221,664</b>	<b>-\$31,646,818</b>

The annual estimates of costs to the Education Fund improve under this methodology. From 2017 through 2026, the cost to the Education Fund is approximately \$1 million to \$4 million annually. The cumulative 2017 to 2030 cost of TIF under these assumptions is roughly \$31.6 million in nominal dollars, less than one-half the cost of using a baseline assumption based upon the 20-year county historical average growth rates. The decrease in costs for this methodology is driven by the lower baseline assumptions in Chittenden County; 6 of the 10 districts and the majority of TIF funds originate from this higher-growth area.

These Education Fund fiscal impact estimates (\$3 million to \$6 million per year) are relatively small, representing less than one-half of 1% of the total annual revenues to the Education Fund and would have only marginal impact on statewide property taxes. This puts TIF at nearly the same cost as the State's largest economic development incentive, the Vermont Economic Growth Incentive (VEGI), which costs the State approximately \$5 million per year.<sup>33</sup> The TIF program is also considerably larger (in terms of annual costs to the State) than comparable town incentives the State offers (downtown and village tax credits, and the Downtown Transportation Fund).<sup>34</sup>

Finally, using the same assumptions as above (20-year historical average growth rates as the baseline growth assumption and 6% for TIF district growth), JFO also estimated the costs to municipal general funds. The results are shown in Table 5:

<sup>33</sup> Vermont Employment Growth Incentive Program. Annual Report 2017  
[http://accd.vermont.gov/sites/accdnew/files/documents/DED/VEPC/VEGI/2017\\_VEGI\\_AnnualReport-Final.pdf](http://accd.vermont.gov/sites/accdnew/files/documents/DED/VEPC/VEGI/2017_VEGI_AnnualReport-Final.pdf)

<sup>34</sup> The Vermont Community Development Block Grant program is a program that provides grants for community development. The money for this program, however, originates at the federal level from the Department of Housing and Urban Development. The program itself is not entirely funded by State money.

<b>Table 5: Fiscal Impacts to Municipal General Funds</b> (Using baseline growth of twenty year county average growth +/- 50 percentage points <sup>a</sup> )			
	What they receive under TIF	What they receive under no TIF	Difference (Negative=cost)
2017	\$5,041,260	\$6,996,882	-\$1,955,622
2018	\$5,129,709	\$7,359,471	-\$2,229,762
2019	\$5,700,324	\$8,232,662	-\$2,532,339
2020	\$5,796,926	\$8,646,019	-\$2,849,093
2021	\$5,898,712	\$9,079,147	-\$3,180,434
2022	\$5,999,145	\$9,533,011	-\$3,533,867
2023	\$6,088,246	\$10,008,626	-\$3,920,380
2024	\$6,181,511	\$10,507,056	-\$4,325,545
2025	\$6,409,554	\$11,029,416	-\$4,619,862
2026	\$7,752,073	\$11,576,880	-\$3,824,807
2027	\$8,336,454	\$12,150,678	-\$3,814,223
2028	\$8,566,025	\$12,752,101	-\$4,186,076
2029	\$11,682,678	\$13,382,507	-\$1,699,828
2030	\$13,394,808	\$14,043,318	-\$648,510
<b>Total</b>	<b>\$101,977,426</b>	<b>\$145,297,774</b>	<b>-\$43,320,349</b>

<sup>a</sup> If the district was in Chittenden County, 50 percentage points were added. If it was not, 50 percentage points were subtracted

TIF also represents a net loss to municipal general funds, on aggregate. This cost is between \$2 million and \$5 million annually between 2017 and 2030, in nominal dollars. Over that same time period, it is estimated that TIF will cumulatively cost municipal general funds approximately \$43 million statewide, in nominal dollars.

Combining costs to the Education Fund and municipal general funds, TIF represents a total cost to the State and municipalities of between \$5 million and \$10 million per year over the 2017 to 2030 period, in nominal dollars. Cumulatively, from 2017 to 2030, this cost is over \$111 million, in nominal dollars.

The fiscal cost estimates shown here assume that there may be some statewide and municipal benefits to using TIF. This assumption is difficult to make with certainty, especially at the State level. **For the purposes of calculating budgetary resources for the Education Fund, however, JFO does not take the position that estimated TIF costs should be offset by uncertain benefits and concludes that it is more appropriate and conservative to use the estimates of fiscal costs from the Consensus Administration and JFO Education Fund Outlook (\$5 million to \$10 million per year, see Appendix Table A3).**

## v. Other considerations for estimating fiscal impacts

**The JFO model did not attempt to estimate the fiscal costs associated with the downside risk that tax increments do not materialize as projected.** The failure of tax increments to hit their projected targets could result in both the State and municipality incurring additional fiscal loss. Furthermore, if increments continue to fall

short of projections, then the town will be forced to repay the debt through other resources in its budget.

This has occurred nationwide and even in Vermont. The Milton North and South TIF district was projected to create \$100 million in additional property values by the end of its increment retention period but had only generated \$36 million. Despite being at the end of the retention period, the town still owed \$21 million in debt related to the TIF district. To mitigate this problem, in 2006, the Legislature allowed the district to retain tax increments for an additional ten years. As a result, the State and municipality will continue to incur fiscal costs longer than projected.

**Some of these costs to the Education Fund or municipal general funds could potentially be offset by any TIF benefit to other tax types or the longer-term economic effects of denser economic development.** As mentioned earlier, JFO did not attempt to estimate the fiscal impacts related to increases in sales, income, or meals and rooms taxes. Although the evidence is mixed as to whether TIF creates new revenues from these sources (see Section C: Economic Impacts), if TIF in Vermont is creating new economic activity that would not have occurred elsewhere, the fiscal impacts from these tax types might offset the fiscal costs to the Education Fund and municipal general funds.

It is also possible that the costs to the respective funds could be offset from the benefits of increased density in downtown areas. If TIF district growth causes more people to move to TIF municipalities, the school districts in these municipalities may benefit from economies of scale resulting from greater student populations, generating positive effects for the Education Fund. Another potential benefit to density is higher worker productivity.<sup>35</sup> To the extent that higher productivity leads to higher wages, the State would benefit through higher income taxes.

## **C) Economic Impacts: Analysis of Economic Impacts Attributable to Vermont TIF**

### **i. Summary of economic impact conclusions**

Vermont's TIF program is relatively unique compared to other states, largely because it requires TIF districts to be located only in downtown areas. Because of this, TIF is effectively a tool used to finance downtown infrastructure and downtown economic development.

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<sup>35</sup> Glaeser, Edward L., José A Scheinkman, and Andrei Shleifer. "Economic growth in a cross-section of cities." *Journal of Monetary Economics* 36.1 (1995): 117-143.



Examining the economic benefits of using TIF in Vermont requires studying the extent to which TIF generates positive economic activity through two channels:

- The extent to which downtown economic development (facilitated by TIF), as opposed to sprawl, generates positive economic benefits.
- The extent to which TIF's incentive creates *new, net positive* economic activity that would have otherwise not occurred in the State *and* the municipality by using public funds to leverage private investment.

To the question of whether downtown development (in part driven by the use of TIF) generates positive economic benefits, **JFO concludes there may be economic benefits to encouraging development in downtown areas, and TIF may be beneficial in this regard. This is for the following reasons:**

- Recent academic research has found that increased density is associated with enhancements to productivity and wages.
- The use of TIF to drive development to downtowns is consistent with the theory of "Smart Growth" for urban centers, which has been found to provide a number of economic benefits to communities. These include more efficient public services and less of an environmental impact.
- Requiring TIF to be located in downtowns is also consistent with other policies implemented at the State level, namely Act 250.

To the question of whether TIF creates economic growth, **JFO concludes that it is uncertain whether TIF's incentive itself is creating *new, net positive* economic activity in the State *and* the municipalities. This is for the following reasons:**

- It is unclear whether the size of TIF's incentive in Vermont is large enough to tip a private developer's decision to construct a new development. In other words, it is difficult to determine whether the investments would have occurred absent the use of the TIF incentive.
- Vermont's TIF program likely causes some substitutability of economic activity from one area of the State to the select downtown/high density TIF districts.
- Research on the economic benefits created directly by TIF is mixed, although more recent literature has found little to no economic benefit from using TIF.

Finally, JFO also analyzed the extent to which TIF districts in Vermont have achieved the expected development laid out in their applications and made the following findings:

- **Vermont's TIF districts have largely achieved their projections of taxable property growth.**

- **However, on aggregate, actual incremental tax revenue has fallen considerably short of projections, missing 70% of the time and with a median miss of 42%. This is largely due to towns projecting higher property tax rates than what actually occurred.**
- **As of year-end-2016, total actual private real property investment in Vermont TIF districts has been less than one-half of what was projected in their applications.**

## **ii. Does TIF's promotion of downtown development create indirect benefits?**

Because Vermont requires TIF districts to be located in downtown or dense areas, TIF is effectively an incentive to promote development in downtown areas. Even if the development would have happened elsewhere without TIF or TIF is creating demand substitution, TIF could still be a useful incentive if the State and/or municipality are seeking to promote economic development within their downtowns as opposed to elsewhere.

Economic development to promote more population density is one of the tenets of "Smart Growth" for urban centers. Smart Growth, which is promoted by the American Planning Association<sup>36</sup> and the Environmental Protection Agency<sup>37</sup>, advocates for compact urban development, reducing sprawl, varying housing choices, and creating walkable communities.<sup>38</sup>

Advocates of Smart Growth point to numerous benefits that could result from building more compact communities. These include:

- Increased housing options for residents: in sprawling communities, zoning restrictions may be putting restrictions on the types of multi-family housing.
- Transportation benefits: these include less money spent on transportation by residents, improved fitness, and reduced traffic incidents.
- More efficient provision of public services: utilities, roads, and emergency services cheaper to provide in denser communities.

<sup>36</sup> <https://www.planning.org/policy/guides/adopted/smartgrowth.htm>

<sup>37</sup> <https://www.epa.gov/smartgrowth/about-smart-growth>

<sup>38</sup> "APA Policy Guide on Smart Growth." Updated April 14, 2012.  
<https://www.planning.org/policy/guides/adopted/smartgrowth.htm>

- Environmental benefits: less need for cars results in fewer vehicles emitting pollution and fewer impervious surfaces.<sup>39, 40</sup>

There is also a body of academic literature that has found that increased density leads to increases in productivity, wages, and innovation.<sup>41</sup>

At the State level, directing development to downtown areas is also coherent with policies regarding land use it has enacted (namely, Act 250 of 1970) and other ACCD tools that promote downtown development.

**JFO concludes that TIF may help generate these indirect benefits by requiring that TIF districts be located in downtown areas.** These effects are likely to be longer-term. TIF is used in conjunction with other policies to promote denser development. One such policy is land use policy at the State and municipal level. Because TIF is not the only tool creating Smart Growth benefits, it is difficult to measure which of these benefits is directly attributable to TIF.

### **iii. Does the TIF incentive itself create new, positive economic activity that would not have occurred in the State *and* municipality?**

#### a) Economic Theory of TIF's Benefits

In order for TIF to be an effective development incentive, it must produce *new* economic growth. This section analyzes whether Vermont's TIF program creates *new* economic growth by determining whether the characteristics of Vermont's TIF districts meet two specific criteria:

- **TIF's incentive to private developers was truly large enough to tip their decision to build.** In other words, was the infrastructure financed by TIF revenues too costly for private developers to do themselves? Without the incentive, would the development have been completed anyway by the developer?
- **The demand for the new goods and services created in the TIF district was location-specific.** In other words, did these new developments need to occur within such a limited geographic area as a TIF district or could they have been

<sup>39</sup> Robert Burchell, et al. (2002), The Costs of Sprawl 2000, TCRP Report 39, Transportation Research Board ([http://onlinepubs.trb.org/onlinepubs/tcrp/tcrp\\_rpt\\_74-a.pdf](http://onlinepubs.trb.org/onlinepubs/tcrp/tcrp_rpt_74-a.pdf))

<sup>40</sup> Todd Litman (2008), Understanding Smart Growth Savings: What We Know About Public Infrastructure and Service Cost Savings, And How They are Misrepresented By Critics, Victoria Transport Policy Institute ([www.vtpi.org/sg\\_save.pdf](http://www.vtpi.org/sg_save.pdf)).

<sup>41</sup> Glaeser, Edward L., José A Scheinkman, and Andrei Shleifer. "Economic growth in a cross-section of cities." *Journal of Monetary Economics* 36.1 (1995): 117-143.

built outside the district and been just as successful at creating economic growth for the municipality or State?

Was TIF a large enough incentive to tip private developers' decision to build?

TIF's use in Vermont is based upon the idea that the infrastructure in a geographic area is insufficient for major private development to occur. In order to make this land usable, either the municipal/state government or the private developer would need to construct new infrastructure. TIF's but-for argument (that no development would occur but for the use of the incentive) suggests that the developers would not build this infrastructure themselves; if they did build it themselves, it would be too costly, rendering the whole project unprofitable. Only once the municipality and State step in and agree to use TIF to finance the cost of the infrastructure will the project be profitable for the developer.

JFO attempted to analyze whether the cost of infrastructure was truly too large for developers to bear themselves and was preventing them from moving forward with developments. **JFO finds that the degree to which this is true in Vermont TIF districts is uncertain.** This is because of the following reasons:

- It is difficult to determine if the cost of building infrastructure is critical to a developer's decision to build without understanding the developer's financial position at the time of application. This information was not available to JFO.
- It is unclear who the primary users of the infrastructure are in Vermont's TIF districts. Multiple users of the infrastructure complicate the question of how much any developer would be expected to contribute toward the infrastructure's cost.

In some cases in Vermont, the infrastructure being built by the city was being utilized by numerous new developments, such that the cost potentially could have been split. For instance, in the Barre TIF district, structured parking was expected to be utilized by all nine developments projected to be built. At a projected cost of \$4,462,500, this would imply a cost of \$495,833 per user, if they all used the garage equally. However, because the developments were scheduled to be built at different times, it may have been difficult to come to an agreement with all developers to finance a certain portion. In these cases, TIF was used to solve this coordination problem. In these cases of multiple users, it may be worth further review to determine why construction or user fees were not used to finance this infrastructure.

Is the demand for the goods and services in a TIF district location-specific?

TIF would only create *new* economic activity if the forthcoming demand for the new development is geographically limited. If it is not, then TIF simply moves economic

activity from one geographic area to another. This phenomenon is called “demand substitution.”

If the projects being built in a TIF district do not rely on geographically limited demand, then economic growth for the city or State becomes a zero-sum game.<sup>42</sup> New economic activity in one area comes at the expense of another; the net result is zero new economic growth. If development from TIF is effectively a zero-sum game, then it represents a potential cost to both the municipality and the State; forgone tax revenues are not creating any *new net* economic growth. This is a major concern for TIF; research has shown that growth within TIF districts can come at the expense of growth in other parts of cities.<sup>43</sup>

JFO attempted to analyze the degree to which TIF is causing economic demand substitution in Vermont. **JFO finds that Vermont’s TIF program likely creates some level of demand substitution, at both the city and State level, but it is difficult to determine the extent to which this occurs.**

Applications often do not provide enough information to determine if the demand for the type of development is location-specific. For instance, many projects are described as “retail” developments, which is ambiguous whether such a product or service has substitutes in the city. In some cases with known tenants, the demand for the goods or products they offer is arguably not specific to the geographic area of the TIF district. In Barre, one of the developments was a new bank branch, which competes with numerous banks outside the TIF district. In St. Albans, a new hotel in its downtown TIF district is in direct competition with at least four other hotels located within the city.

#### b) Research on the economic impacts directly attributable to TIF

Because the use of TIF has exploded since the late 1970s and early 1980s, a large amount of economic research examines whether TIF has had positive economic impacts on a blighted area. This includes academic research, as well as other examinations by other states and research institutions. It is important to note, however, that the research on TIF has been conducted on other state TIF programs. Because Vermont’s program is different in some aspects (namely its location and project criteria), using these same methodologies specifically to analyze Vermont’s TIF may yield different results.

**Some academic research found that, controlling for other economic factors, areas with TIF experienced greater property value growth and a slightly bigger**

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<sup>42</sup> This zero-sum game has been demonstrated for numerous other types of tax credits, including R&D tax credits (Wilson, 2009) and investment and corporate tax rates (Chirinko and Wilson, 2008).

<sup>43</sup> Dye, Richard F., and Merriman, David, “The Effects of Tax Increment Financing on Economic Development,” *Journal of Urban Economics*, Volume 47, Issue 2, 2000, Pages 306-328.

**increase in jobs than those without.**<sup>44, 45, 46</sup> These studies were conducted in Indiana and Michigan. In addition to this, there has been some recent research on Chicago TIF districts that found the use of TIF generated faster property value appreciation than areas without it, depending on the level of blight in the TIF district compared to the surrounding area.<sup>47, 48</sup>

**Recent academic research finds that TIF does not create new economic activity, and in some cases, causes slower economic growth in TIF municipalities overall.**

Much of this literature has been produced within the past 20 years and relies on a different methodological approach from earlier studies. Newer studies now account for the idea that cities with faster economic growth could be more likely to adopt TIF than slower-growth cities. This is because where the opportunity exists to capture another entity's tax revenues (such as the State), if the municipality knows the development is going to occur, it can use a TIF to increase its revenue stream.

A summary of this literature can be found in Table 6.

**Nonacademic research has generally been critical of TIF or found that it creates little to no new economic growth.** A 2011 report by the U.S. Public Interest Research Group (PIRG) criticized a lack of transparency and accountability for results in TIF districts nationwide. The Lincoln Institute for Land Policy has also written extensively on TIF. One of its studies found TIF introduces long-term volatility in municipal budgets.<sup>49</sup> Another paper criticized municipalities for not properly accounting for TIF debt as municipal debt, raising accountability and repayment concerns.<sup>50</sup>

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<sup>44</sup> John E. Anderson. "Tax Increment Financing: Municipal Adoption and Growth." *National Tax Journal*. Vol. 43, No. 2 (June, 1990), pp. 155-163.

<sup>45</sup> Man, J.Y. 1999. "Effects of tax increment financing on economic development." *Journal of Public Budgeting, Accounting & Financial Management*, 11(3): 417-430.

<sup>46</sup> Man, Joyce Y., and Mark S. Rosenstraub. "Tax increment financing: Municipal adoption and effects on property value growth." *Public Finance Review* 26.6 (1998): 523-547.

<sup>47</sup> Smith, B. C., "Economic Depreciation of Residential Real Estate: Micro Level Space and Time Analysis". *Real Estate Economics*, 2004, 32:1.

<sup>48</sup> Smith, B.C.. "If you promise to build it, will they come? The interaction between local economic development policy and the real estate market: Evidence from tax increment finance districts". *Real Estate Economics*. 37(2): 209-234. 2009.

<sup>49</sup> Dye, R., Merriman, D.. "Tax Increment Financing: A Tool for Local Economic Development." Lincoln Institute of Land Policy. January 2006.

<sup>50</sup> Youngman, Joan. "TIF at a Turning Point: Defining Debt Down." Lincoln Institute of Land Policy. May 2011.

**Table 6: Summary of Academic Research**

Year	Author(s)	Location of study	Major finding(s)
1990	John Anderson	Michigan	TIF-adopting cities saw greater property value growth
1998	Joyce Man, Mark Rosenstraub	Indiana	Home values were higher in TIF-adopting cities than in non-TIF cities
1999	Joyce Man	Indiana	Cities with TIF created 4% more jobs than non-TIF cities on average
2000	Richard Dye and David Merriman	Chicago	TIF-adopting cities' growth was slower than in non-TIF cities
2003	Rachel Weber, Bhatta Sauav & David Merriman	Chicago	In industrial TIF districts, parcels sell for less than their non-TIF counterparts
2010	Paul Byrne	Illinois	Retail TIFs have a negative effect on employment while industrial ones have a positive effect
2010	Mark Skidmore and Russ Kashian	Wisconsin	TIF affects tax rates of those municipalities just outside the TIF-adopting municipality
2010	Susan Mason and Kenneth Thomas	Missouri	Adopting a TIF made neighboring municipalities 2.5 times more likely to adopt as well. Some evidence that TIF may contribute to economic inequality between municipalities.
2015	Michael Hicks, Dagney Faulk, Pam Quirin	Indiana	Adoption of TIF is associated with a decline in employment levels and business establishments. No impact on sales tax revenues.
2015	Charles Swenson	California	RDAs were associated with minimal economic impacts

Aside from other state annual reports, which are similar to VEPC's annual report, JFO found few comprehensive analyses of TIF by other states. In 2015, the Indiana Legislative Services Agency completed an in-depth econometric analysis of Indiana TIF districts and found minimal economic impact of using TIF.<sup>51</sup> Another comprehensive report by the California Legislative Analyst's Office in 2011<sup>52</sup> on Redevelopment Authorities (RDAs) concluded that while RDAs were a flexible tool for local governments and helped fund some affordable housing, there was no evidence that RDAs increased regional or statewide economic development. The report recommended dissolution of all RDAs in California, per the Governor's proposal at the time.

To summarize the research on TIF's economic impacts, while the results are somewhat mixed, more recent literature has found that using TIF does not create new economic growth in a municipality, and in some cases, may cause negative growth because of

<sup>51</sup> Landers, J. and Gossard, A. "2015 Indiana Tax Incentive Evaluation." Office of Fiscal and Management Analysis, Indiana Legislative Services Agency. [https://iga.in.gov/static-documents/6/d/e/c/6dec6072/indiana\\_tax\\_incentive\\_review\\_2015\\_annual\\_report.pdf](https://iga.in.gov/static-documents/6/d/e/c/6dec6072/indiana_tax_incentive_review_2015_annual_report.pdf)

<sup>52</sup> Taylor, Mac. "Should California End Redevelopment Agencies?" California Legislative Analyst's Office. February 9, 2011.

demand substitution. Research conducted by other states' research offices has drawn similar conclusions.

#### **iv. Analysis of actual TIF district performance versus projections**

Using data provided by VEPC in each of the TIF district annual reports, JFO analyzed year-by-year how actual taxable property values and incremental tax revenues performed relative to the projections made in their applications.

In order to justify the use of TIF, a municipality needs to demonstrate that the use of TIF will create new economic growth. In their applications, each TIF district in Vermont made projections about the level of economic growth that its TIF district would generate. However, even if municipalities hit their projections completely, this does not necessarily imply that there is *new, net positive* economic impact for the State and municipality, for all the reasons discussed above (demand substitution, the development could have happened without the use of TIF).

It is important to point out that property value growth and incremental tax revenues could miss their projections for a number of reasons that have little to do with slow property value growth in the TIF district or incorrect assumptions by municipalities. Construction and permitting delays are a significant reason for delays. However, if construction is delayed, because the TIF retention period lasts 20 years, it shortens the amount of time a municipality can retain incremental tax revenues (generated by the development) to pay TIF debt. Furthermore, if the construction of the infrastructure is completed upfront and there are construction delays in private development, it delays the revenue flow of tax increments to repay the debt on the infrastructure.<sup>53</sup> The data included in these annual reports often contain large swings for both measures from year to year. This is because a new development could cause an abrupt increase in taxable value and incremental tax revenue. In years where there was either no actual or projected taxable value or incremental tax revenues, the year was excluded.

The results are listed below in Table 7. **JFO's key findings are:**

- **Municipalities' projections of taxable property growth are quite accurate. The median percentage miss was very close to zero (using the average, the actuals are 6% higher than projections).**

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<sup>53</sup> Often in Vermont, to prevent this from occurring, municipalities will secure written agreement from developers to start their construction either during or after the construction of the infrastructure by the municipality.



- On incremental tax revenues, municipalities have fallen short of their projections 70% of the time, missing by a median amount of 42% (29% on average).
- Using data that were available, \$10.6 million of total tax increment was projected, but only \$5.45 million had been realized, a miss of over 50% (Table 7).

	<b>Taxable Value</b>	<b>Tax Increment</b>
<b>Median Percentage Miss</b>	0%	42%
<b>Average Percentage Miss</b>	-6%	29%
<b>Cumulative Projected</b>	N/A	\$10,608,907
<b>Cumulative Actual</b>	N/A	\$5,447,900

Note: Excludes data from Burlington Waterfront TIF district

Source: TIF district annual reports to VEPC

Since tax increment revenues and taxable values are linked, it should be expected that if taxable property values achieve their projections, so would incremental tax revenues. The divergence is likely caused by inaccurate estimates of property tax rates, in aggregate. For three TIF districts (St. Albans, Milton Town Core, and South Burlington), there is data on their projections of tax rates in their applications, shown in Table 8. For 2017, all three TIF districts predicted non-homestead tax rates that were higher than the statewide actual rate.

	<b>Statewide Actual</b>	<b>South Burlington</b>	<b>Milton Town Core</b>	<b>St. Albans</b>
2011	\$1.35		\$1.35	
2012	\$1.36		\$1.36	
2013	\$1.38		\$1.39	\$1.53
2014	\$1.44		\$1.43	\$1.60
2015	\$1.55		\$1.48	\$1.67
2016	\$1.54		\$1.53	\$1.75
2017	\$1.54	\$1.57	\$1.58	\$1.82
2018	\$1.54	\$1.60	\$1.65	\$1.91
2019		\$1.63	\$1.73	\$1.99
2020		\$1.67	\$1.81	\$2.08
2021		\$1.70	\$1.91	\$2.18
2022		\$1.74	\$1.99	\$2.27
2023		\$1.77	\$2.07	\$2.38
2024		\$1.81	\$2.15	\$2.48
2025		\$1.74	\$2.23	\$2.59
2026		\$1.88	\$2.32	\$2.71
2027		\$1.92	\$2.41	\$2.83
2028		\$1.95	\$2.50	\$2.96
2029		\$1.99	\$2.59	
2030		\$2.03	\$2.69	
2031		\$2.07		
2032		\$2.11		
2033		\$2.16		
2034		\$2.20		
2035		\$2.24		
2036		\$2.29		

Source: TIF District Applications, data provided by VEPC

In addition to these districts, based upon the numbers provided in VEPC's 2017 Annual TIF Report, many TIF districts assume a statewide combined homestead and non-homestead education tax rate of over \$2.00 by the end of their retention period (See Table 8).

	<b>Final year of Increment Retention</b>	<b>Total Taxable Value Projected</b>	<b>Total Education Tax Revenue Projected</b>	<b>Effective Education Tax Rate</b>
<b>Barre</b>	2035	\$74,387,220	\$1,577,291	\$2.120
<b>Burlington Downtown</b>	2036	\$252,408,208	\$6,776,694	\$2.685
<b>Burlington Waterfront<sup>a</sup></b>	2035	\$136,823,716	\$2,382,325	\$1.741
<b>Hartford</b>	2034	\$94,282,261	\$1,444,069	\$1.532
<b>Milton North and South<sup>b</sup></b>	2019	\$61,342,520	\$923,605	\$1.506
<b>Milton Town Core</b>	2031	\$250,622,150	\$6,095,226	\$2.432
<b>South Burlington</b>	2037	\$202,023,960	\$7,522,211	\$3.723
<b>St. Albans</b>	2033	\$197,615,250	\$6,190,495	\$3.133
<b>Winooski</b>	2024	\$114,351,720	\$1,752,880	\$1.533

<sup>a</sup> Burlington Waterfront TIF District's retention period ends in 2035, but the data here represent the 2015 data

<sup>b</sup> Milton North and South TIF District's retention period ends in 2019, but the data here represent 2015 data

Source: 2017 Annual Report on Tax Increment Financing Districts in Vermont, VEPC

This analysis underscores the need for accurate growth assumptions for both future property values and tax rates. These growth assumptions are critical to estimating the size of infrastructure projects a municipality can plausibly support with TIF. If a municipality is incurring debt against overly optimistic growth assumptions, it will have to seek other revenue sources to make up for shortfalls in TIF revenue.

**Finally, JFO finds that TIF districts in Vermont have received less than one-half of the total projected private investment.** At the time of application, as of the end of 2016, TIF district applications cumulatively projected over \$431 million in real private property investments. Based on the data provided by each TIF district's annual reports, only \$214 million has materialized. As stated earlier, this could be the result of construction and permitting delays. Continued shortfalls in investment could result in misses for both future taxable value and tax increments. However, this would only be a concern if municipalities are borrowing against the tax increments. To the extent that the municipalities borrow smaller amounts for each individual project (rather than borrowing a large amount for multiple projects), it would reduce the downside risk to the municipality if tax increments are falling short of projections.

#### **v. Other Economic Impact Considerations: The use of non-TIF revenue in TIF districts**

Linking economic growth directly to the use of TIF is even more difficult if TIF is used in conjunction with other sources of economic development funds. In Vermont, TIF is rarely used as the sole instrument for funding infrastructure improvements; rather, it is

one tool in a suite of other available funds. These funds include grants and loans from the State and federal government.

Relying on non-TIF revenue can be advantageous to a municipality because it diversifies revenue streams. Some of the major pitfalls of TIF can be avoided by ensuring that TIF debt can be financed using multiple sources of revenue. However, the use of non-TIF revenue blurs the direct link between new economic activity and the use of TIF.

**After examining the total amount of revenues that TIF districts have generated thus far, JFO finds that many Vermont TIF districts make heavy use of non-TIF revenues.** In some cases (Winooski, Barre, Hartford), non-TIF revenues have so far represented over 80% of total revenue in the TIF district. Others, such as the TIF districts in Milton, have relied almost entirely on TIF incremental revenues.

Table 10: Comparisons of TIF District Revenue Sources, as of end-2016

	Barre	Burlington Waterfront	Hartford	Milton North and South	Milton Town Core	St. Albans	Winooski
<b>Total Revenue</b>	\$3,196,859	\$24,942,271	\$286,885	\$534,157	\$1,240,065	\$2,239,799	\$83,275,710
<b>of which: TIF Revenue</b>	\$313,299	\$22,231,913	\$48,938	\$529,549	\$1,240,065	\$1,464,589	\$11,707,609
<b>of which: Non-TIF Revenue</b>	\$2,883,560	\$2,710,358	\$237,947	\$4,608	0	\$775,210	\$71,568,101
<b>Percentage Non-TIF Revenue</b>	90.20%	10.87%	82.94%	0.86%	0.00%	34.61%	85.94%
<b>Percentage TIF Revenue</b>	9.80%	89.13%	17.06%	99.14%	100.00%	65.39%	14.06%

Note: Data for South Burlington and Downtown were unavailable

Source: Individual TIF district annual reports

Because of this frequent mixing of TIF and non-TIF revenues to finance infrastructure improvements, it is difficult to establish a measurable direct link between growth in property values or economic activity in a TIF district and the use of TIF itself.

## **D) Ensuring Geographic Diversity of TIF Districts in Vermont**

As requested in the statutory charge, this section examines how well Vermont's TIF program ensures geographic diversity of TIF districts.

### **i. Summary of findings**

JFO finds that Vermont's TIF statute does not guarantee geographic diversity of TIF districts for primarily three reasons:

- **Research has found that municipalities that have some level of underlying economic demand will apply for TIF districts, rather than those municipalities that are economically distressed.**<sup>54</sup>

<sup>54</sup> Economically distressed areas are defined in statute as: a municipality in which the area is located has at least one of the following: (i) a median family income that is not more than 80 percent of the statewide median family income; (ii) an annual average unemployment rate that is at least one percent greater than the latest annual average statewide unemployment rate; or (iii) a median sales price for residential properties under six acres that is not more than 80 percent of the statewide median sales price for residential properties under six acres. See 32 V.S.A. § 5404a.

- **The location criteria in Vermont’s statute do not require that an area be economically distressed to be eligible for a TIF district.<sup>55</sup>**
- **The complexity of TIF as an economic development tool, both in applying and administering, may limit TIF to municipalities with greater staff capacity and expertise.**

## **ii. Municipalities with more economic demand are more likely to establish TIF districts**

Act 69 of 2017 stated that the Legislature has a role to play in supporting downtown development, “particularly in distressed communities.”<sup>56</sup> This would imply that one of TIF’s goals is to promote development in these communities.

Although TIF is often used as an economic development tool to bring investment to economically distressed communities, research has found that those municipalities that are experiencing stronger growth are more likely to adopt TIF.

Most research on TIF adjusts for a phenomenon called “selection bias.”<sup>57</sup> When a municipality establishes a TIF district, the usual claim is that it does so to increase the property values in economically distressed areas. However, it is also possible that it adopts TIF because it expects that property values are going to increase anyway, and therefore, establishing a TIF district is a way to capture tax revenues from another government entity (such as the State government or a local fire district). Selection bias suggests that direction of causality could flow in two directions:

Creating a TIF district → Growth in property values

Expected growth in property values → Create a TIF district to capture new taxes

The research on TIF has generally found that this dual-causality exists for TIF districts. This suggests that TIF districts are more likely to locate where there is sufficient underlying demand. Rather than being used to spur growth in economically distressed communities, TIF is more likely to be used in growing municipalities to develop previously undeveloped tracts of land.

There is some evidence that this is occurring in Vermont. For the more recent, post-2006 TIF districts, all are located in counties with higher-than-State-average 20-year grand list growth. Bennington, which is in a slower-than-average growth county, has been recently approved for a TIF district. At present, of the ten active TIF districts in the

<sup>55</sup> 32 V.S.A. § 5404a.

<sup>56</sup> Act 69 of 2017.

<sup>57</sup> See Dye and Merriman (1999) and Anderson (1990).

State, six of them are located in Chittenden County, which is one the fastest-growing counties in the State.

In a State where a municipality is eligible to capture another entity's tax revenues, geographic diversity of TIF districts in Vermont may be limited by this self-selection phenomenon.

### **iii. Current statute does not guarantee TIF district geographic diversity**

Vermont's TIF statute does lay out certain geographic constraints on new TIF districts, although JFO finds that these may not guarantee that economically distressed municipalities will establish TIF districts.

Current statute forces some geographic diversity by stating that no municipality that currently has a TIF district will be eligible for an additional one.<sup>58</sup> This rules out new TIF districts in some of the fastest growing municipalities in the State, namely Burlington and some of the surrounding municipalities in Chittenden County.

Current location criteria also require that TIF districts be placed in denser, downtown areas.<sup>59</sup> These criteria rule out TIF being used for industrial construction or expansion in rural areas. Because much of the State is rural, they also prevent large parts of the State from using TIF for economic development.<sup>60</sup>

Finally, statute requires that a TIF applicant meet at least two of the following three location criteria:<sup>61</sup>

- The development is i) compact; and ii) high density or located in or near an existing industrial area.
- The development is located within an approved growth center or designated downtown or village center.
- The development is located in an area that is economically distressed, as defined by various criteria.

Thus, new TIF applicants need not be economically distressed communities exclusively.

JFO concludes that if the State's goal is to use TIF to boost economic activity in economically distressed municipalities around the State, statute cannot guarantee that this will occur. In fact, any TIF district that is established in a faster-growth area will be

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<sup>58</sup> 32 V.S.A. § 5404a.

<sup>59</sup> 32 V.S.A. § 5404a.

<sup>60</sup> TIF has generally been confined to urban areas nationwide. JFO could not find any research on the suitability for TIF in rural areas.

<sup>61</sup> 32 V.S.A. § 5404a.

financed, in part, by economically distressed communities through higher statewide property tax rates.

**iv. The complexity of TIF may preclude towns with less staff capacity and expertise from taking up the program.**

Another consideration that may limit geographic diversity of TIF in Vermont is the expertise and staff capacity required to apply and administer a TIF district. Applying for a TIF district requires making accurate projections of property value growth and incremental tax revenues. It also requires a substantial amount of effort from a municipality; for example, taking stock of all parcels in the proposed district and meeting with private developers to discuss plans for investment. Administering a TIF district, at a minimum, requires the staff capacity to annually calculate incremental tax revenue and complete annual reports for VEPC. The State Auditor's reports in 2012, which found errors in assessing and calculating tax increments, highlighted the complexities of administering a TIF program.

VEPC's TIF rules have taken strides to mitigate this concern. Consultant costs for the preparation of the applications are now considered a "related cost," and thus eligible for TIF funds.<sup>62</sup> However, this presents a potential conflict of interest as consultants are paid for the applications they complete. They are not accountable for inaccurate tax increment or taxable value projections, nor are they monetarily motivated to advise a municipality against using TIF.

Notwithstanding the concerns with using consultants, this statutory change only affects the application for TIF, not the administration. For municipalities with limited staff and expertise, the complexity of completing an application and administering TIF once it is established may preclude them from taking advantage of the program.

Finally, because State statute currently states that TIF applicants will be considered in the order they are received,<sup>63</sup> towns with less capacity may be less prepared to complete the application process with expediency.

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<sup>62</sup> See VEPC's Tax Increment Financing Districts Adopted Rule, adopted May 2015. Page 15.

<sup>63</sup> 32 V.S.A. § 5404a.

### **III. Considerations for Legislators**

JFO recognizes the State's desire to play a role in economic development in Vermont municipalities. In light of the above findings, this section puts forth some considerations for legislators regarding the use of TIF and economic development around the State.

#### **1) Legislators may want to consider requiring municipalities to repay TIF district debt as incremental tax revenues accrue, rather than solely the required bond payment.**

Current statute and TIF Adopted Rules by VEPC do not explicitly state what a municipality is to do with incremental tax revenues that exceed the required debt service payment. Instead of allowing municipalities to maintain funds with surplus revenues, legislators may want to consider requiring municipalities to use these surplus incremental tax revenues to prepay debt. However, this requirement should only apply if there are small or no prepayment penalties on the debt. Moreover, there should be a strong degree of certainty that future tax increments will be able to cover debt service payments.

The main reason why early repayment of debt is advantageous is that the sooner the municipality pays off TIF debt, the sooner the TIF district begins to remit the full 100% of incremental property tax revenue to both the municipality and the State. In JFO's fiscal impact estimates, once debt was repaid, the fiscal impact became positive because any boost in growth provided by TIF was no longer split between the Education Fund and TIF debt; the Education Fund received 100% of the growth in property taxes.

Another advantage of repaying TIF debt early is that the municipality is less exposed to the risk of uncertainty surrounding future tax increments. Future tax increments are subject to a considerable amount of uncertainty stemming from real estate cycles and fluctuations in the economy. It may be advantageous for a municipality to use the unexpected windfall during good times to pay off debt, rather than hoping that those windfalls continue into the future.

If a TIF district is generating surplus tax increments and there is reason to believe that they will continue, there are fiscal benefits to requiring municipalities to use these windfalls for early debt repayment. The quicker debt is repaid, the quicker the State can see a quicker return on its investment.

**2) Legislators may want to consider whether the current system of approval, monitoring and evaluation ensures TIF district accountability for results.**

JFO finds that the current system of approval, monitoring, and evaluation could be improved to ensure that the TIF program is providing *statewide* benefits, not just municipal ones.

Beginning with the approval process, JFO found that applications focused largely on the benefits TIF will provide to the municipality. As part of VEPC's review of a municipality's but-for claims, it examines the following items:

- Analysis of infrastructure cost and debt assumptions, real property development, and property tax revenue generation assumptions.
- Availability of other sources of revenue.
- Analysis of revenues generated through property taxes, grants received, other sources, and ability to service debt.
- Analysis of existing stock and marketability and absorption of proposed development.
- Availability of market studies.

JFO agrees with VEPC that these are important aspects to examine when approving a TIF district.

**However, the process could be improved by analyzing the degree to which new development within the TIF district is causing demand substitution within the municipality *and* around the State.** Consideration should be given to the type of development (retail, mixed-use, residential). Use of a formal economic model, such as VEGI's Cost-Benefit model, could also help inform the decision.

**Once a TIF district is established, VEPC's Annual Report should provide information on the level of statewide economic benefits, in addition to the value created within TIF districts themselves.** The report could also show estimates of benefits from Smart Growth that are due to TIF. In this way, the report could provide legislators with a better sense of whether the program is worthy of its cost to the Education Fund.

Moreover, the Annual Report could also report whether incremental tax revenues are meeting projections and whether investment in the TIF districts is meeting the plans laid out in their applications. This information could help inform legislators and VEPC first, whether the TIF district is achieving the development it projected in its applications, and second, whether any municipality is at risk of fiscal stress due to lagging tax increments.



**With respect to evaluation of TIF districts, VEPC may be in a difficult position to provide independent evaluation of the program.** VEPC may not have the staff resources to carry out time-intensive, in-depth evaluations given its other responsibilities. Also, negative evaluation could risk the program's future. Because VEPC is concerned with development in both individual Vermont municipalities and the State as a whole, evaluating whether TIF is creating new economic activity again puts VEPC in a difficult position. If VEPC completed an evaluation of a specific TIF district and found that the TIF is benefiting the municipality but not the State as a whole, then the program would be achieving one of its mandates but not the other.

**The evaluation process could be improved by requiring an independent estimation of statewide economic benefits every 5 to 7 years.** This evaluation could be done as a supplement to the State Auditor's regular performance audits or conducted by an outside consultant.

**If a municipality bonds against TIF incremental tax revenues, should these tax increments not materialize as projected because of delays in private investment, legislators should consider creating recourse for VEPC and the municipality so that the fiscal health of both the State and municipality are protected.** There currently exist some frameworks for municipalities in Vermont to protect against a situation where private investment does not occur even after the construction of infrastructure using public money. Some municipalities obtain promises from developers that they will indeed make their investments if the municipality builds the necessary infrastructure. However, if a municipality builds the infrastructure up front and there are private construction delays, there is currently no recourse available for the municipality; no increments occur and the debt service for the infrastructure will need to come from the municipal budget. Legislators may want to consider legislation that would either not allow a municipality to construct the infrastructure without guarantees from private developers or make developers liable for part of the shortfall in tax increments if there are construction delays.

### **3) Consideration should be given to whether TIF is the most effective way to achieve infrastructure development in downtowns.**

TIF is one economic development tool that could be used to fund infrastructure in downtown areas. Given the potential downside risks and the administrative and application complexities unique to TIF, policymakers should weigh the unique benefits of TIF against these disadvantages, and determine whether other economic development tools could achieve the same goal without these disadvantages. This recommendation extends to the 5 remaining TIF districts available as part of Act 69 of 2017, and any future approvals of new TIF districts. Vermont's current TIF statute

contains location criteria that effectively limit the use of TIF to downtown areas.<sup>64</sup> Two of the three location criteria are related to downtowns or dense areas, meaning that no TIF district will be approved unless it is in either a downtown or a densely populated area. Furthermore, because TIF funds are largely constrained to funding infrastructure improvements, this means that TIF in Vermont can be thought of as an incentive to fund downtown infrastructure. Table 11 provides a brief overview of some other economic development tools that could achieve the same goals as TIF.

**TIF has some advantages over other economic development tools that would help finance infrastructure improvements in downtowns.** One advantage of TIF is that it could be used to draw in other types of outside funding. In many cases, TIF district designation has led to an influx of non-TIF-related revenue. These funds are used to make additional improvements within the TIF district. Another advantage is that TIF creates linkages between public improvements and private investments; TIF municipalities in Vermont often do not construct infrastructure without guarantees from private developers.

**Administratively, TIF requires specific staff capacity and expertise.** The application process requires accounting for all parcels within a district, creating a base taxable value, working with developers, and then making accurate projections of both taxable property value and incremental tax revenues generated from the district. Once approved, the municipality needs to assess new developments in the district each year, calculate incremental tax revenues, and service debt. As mentioned earlier, the complexity and staffing requirements of TIF may preclude some smaller municipalities in Vermont from using the program.

**In addition to this, the downside risks associated with TIF are unique relative to other economic development tools.** Because TIF relies so heavily on projections of property value and economic growth, projections that fall short can have significant fiscal consequences at the municipal and State levels. If the development would have occurred in some form without the use of TIF, the municipality has frozen its property tax base needlessly for many years. Moreover, the difference between the actual incremental tax revenues and the debt service requirements will need to be made up with other municipal resources, putting pressure on other areas of the municipal budget.

If the goal of the Legislature is to increase development in its downtowns, the positives and negatives of TIF should be weighed against other economic development tools that could achieve the same goal.

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<sup>64</sup> 32 V.S.A. § 5404a.

**Table 11: Alternative Downtown Infrastructure Development Tools**

<b>Financing Tool</b>	<b>What is it?</b>	<b>Pros</b>	<b>Cons</b>	<b>U.S. Examples</b>
Metropolitan Area Projects (MAPS)	Multiple development projects submitted by citizens via request for proposals. Funded by a limited term sales tax increase.	Projects are funded without debt and are citizen-driven	State restrictions on sales tax uses	Oklahoma City
Tax Credits or Abatements	Exemptions on local or state taxes for development	Versatile and varied. Can be used for many types of projects	Companies may divest once the credits end. Discontent over preferential treatment. Difficult to evaluate.	Washington D.C. Baton Rouge, LA Tucson, AZ
Business Improvement Districts (BID)	Property owners in a specific area vote to initiate and manage supplemental services via a common area based on an assessment formula	Citizen-driven. Has been shown to increase property values in New York City.	Smaller BIDs are unlikely to make a major impact on overall economic development in a city	Philadelphia New York City Denver Madison, WI San Diego
Public Private Partnerships (PPP)	Contractual agreement between public agency and a private partner to support construction, development, ongoing operations, and/or maintenance of a public asset or function	Potential reduction in operating or construction costs. Can be used for many types of public projects or functions.	Some PPPs can be complex and require constant monitoring	30 states have some form of PPP legislation. However, more than one-half of all PPP projects have occurred in only 8 states.
Revolving Loan Funds (RLF)	Provides at or below market rate financing to fund projects in downtown areas or for specific developments	Provides competitive interest rates and flexible terms versus conventional lending. Lowers overall risk for other participating partners.	Loans must be able to generate enough of a return to replenish the fund. Requires an initial amount of capital.	Georgia: Downtown Development RLF Minneapolis, Two Percent RLF
Gap Financing	Funds that fill a gap in traditional funding for business, entrepreneurial, or commercial real estate development projects	Flexible; many types of development projects/costs are eligible. Reduces overall risk for other development partners.	Gaps in financing may be large. Incentive for other partners to reduce their funding share.	Florida Municipal Loan Council
Infrastructure Bank	Assists public and private entities in the construction or redevelopment of transit facilities	Low rate, fixed-term loans at favorable terms	Has not yet been fully proven as an effective tool for municipalities	Chicago
Targeted matching grants	State provides a matching grant to the municipality for use in building infrastructure	State has a clear understanding of the cost of the program	Subject to an annual appropriation, which could change with government priorities. May favor towns with higher capacity to complete grant applications.	

Source: Larkins, Stephanie. "Financing Downtown Redevelopment." Harvard University Data-Smart City Solutions. 5 March, 2014. <http://datasmart.ash.harvard.edu/news/article/financing-downtown-redevelopment-408>

#### **4) The combination of Vermont's statewide property tax system and TIF raises equity issues among municipalities.**

JFO estimates that the TIF program is a net cost to the Education Fund. Legislators need to be mindful of the incidence of this cost and consider, as with other State programs, whether TIF is providing statewide economic benefits, not just benefits to the TIF municipalities.

**The net cost to the Education Fund implies that non-TIF municipalities are financing improvements in the TIF municipalities.** About two-thirds of Vermont's Education Fund is funded using statewide education property taxes.<sup>65</sup> In Vermont's TIF program, districts are entitled to retain up to 70% of the incremental tax revenues that would otherwise go to the Education Fund. If any development would have occurred anyway, then infrastructure improvements in one municipality come at the expense of municipalities statewide. This is because the incremental education property tax revenues that would have flowed to the Education Fund are now being diverted to finance TIF debt. This loss of revenue to the Education Fund will result in higher property taxes statewide.

JFO estimates that to make up this difference, the average homestead and nonresidential property tax rates are roughly one-half of a penny higher per year than if the State allowed no TIF districts. This tax increase is borne by all the municipalities in the State, not only TIF municipalities.

This being said, the use of statewide taxation to fund local projects is not unique to TIF. Gasoline taxes statewide are used to fund State roads running through specific municipalities. The property tax, however, is a historically local form of taxation that Vermonters may link to education funding and municipal services in their town. In other words, the benefits that the tax provides are expected to accrue where the tax originates. TIF breaks down this link because property tax revenues in non-TIF municipalities are used to fund infrastructure in other municipalities. Legislators should be aware of this before approving new TIF districts beyond the six approved in Act 69 of 2017.

**Because of TIF's cost to the Education Fund, legislators may also want to consider whether the benefits of new infrastructure and economic growth in a TIF municipality provide statewide benefits.** Under the current structure, the benefits that TIF districts provide to non-TIF municipalities would need to exceed between \$3 million and \$6 million per year to represent a positive return on the State's investment in TIF. To determine whether this is the case, consideration needs to be given to the types of

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<sup>65</sup> Another 20% comes from Vermont's General Fund consisting largely of income taxes, and another 13% comes from General Purpose Taxes, such as sales taxes and fees.

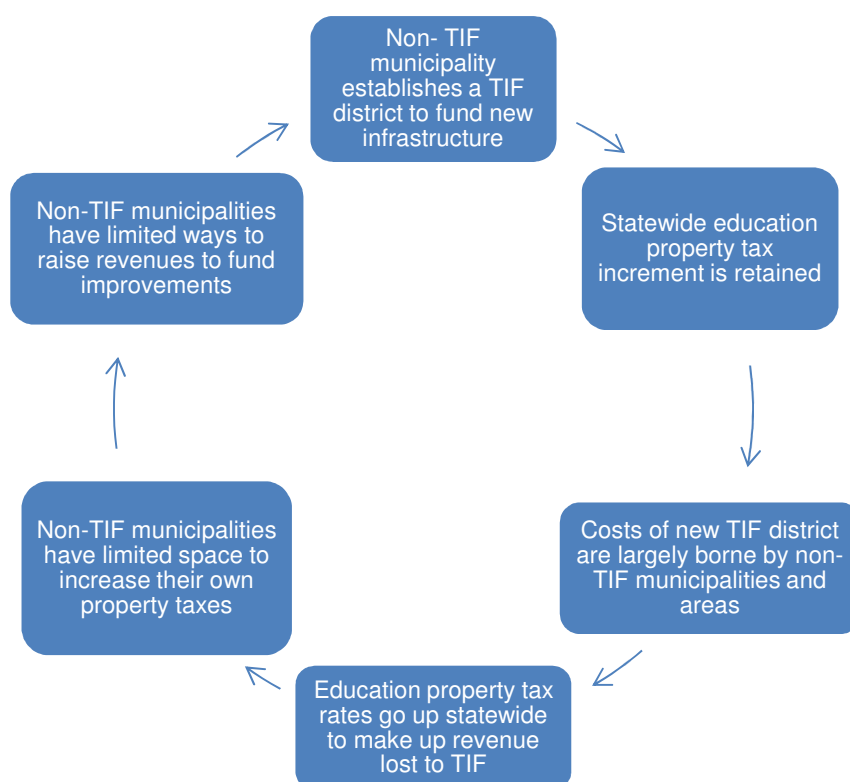
new developments a TIF district facilitates. If the benefits of the development are particularly town-specific, then the TIF may not be providing a statewide benefit.

**5) Because TIF allows municipalities to retain State education property tax revenues to fund their own infrastructure, there could be an incentive for nonparticipating municipalities to establish TIF districts.**

Where there are overlapping government entities, each with their own taxes, legislators should be mindful that there is an incentive for a municipality to use TIF to finance any improvements for two reasons:

- TIF creates a new revenue stream: In an economically distressed area, a municipality may have limited space to increase property taxes. Funding an infrastructure improvement requires diverting resources from another area of its budget. TIF allows such a municipality to retain State property taxes in addition to its own to pay for this infrastructure, without creating the fiscal pressures of funding it on its own.
- More TIF districts increase the cost burden on the non-TIF municipalities, motivating them to establish TIF districts: As the number of TIF districts increases in a state, the cost that non-TIF municipalities bear for the infrastructure in TIF municipalities grows. In Vermont, as this cost becomes greater, the need for statewide education property taxes to make up the Education Fund funding difference will grow. This increase in statewide education property tax rates puts pressure on non-TIF municipalities not to raise their own municipal tax rates. In order to fund infrastructure improvements, this further limited fiscal space will make TIF more appealing. Thus, although TIF currently presents a small budgetary cost to the State, this incentive structure could lead to rapid expansion of TIF and rapid escalation of costs to the State. Figure 3 illustrates this cycle.

**Figure 3: Statewide TIF Expansion Cycle**



The extent to which this is occurring in Vermont is uncertain. However, research on TIF, as well as other states' experiences, particularly those where state revenues are eligible for TIF districts as in Vermont, have shown that this is a possibility in Vermont.

The case of California's Redevelopment Agencies (RDAs) (see Box 4 in the Appendix) is an example. Because RDAs were entitled to retain not only municipal increment tax revenues, but also overlying county and school district taxes, TIF presented a way for municipalities to increase revenues despite Proposition 13 which limited property tax growth. As a result, the use of TIF exploded and the costs to the State ballooned. Maine offers another example (see Box 2 in the Appendix). Since Maine provides state aid for education, using TIF allows a municipality to make improvements that increase property values (but freeze its property tax revenues) without a commensurate drop in its state school district funding. This results in an increased state share of the cost burden of funding schools. This advantageous outcome is one factor that has led to rapid TIF expansion in the State. Academic literature has also shown this incentive exists and needs to be considered when studying economic impacts of TIF.<sup>66</sup>

<sup>66</sup> Dye, Richard F., and Merriman, David, "The Effects of Tax Increment Financing on Economic Development," *Journal of Urban Economics*, Volume 47, Issue 2, 2000, Pages 306-328.

Recent changes to legislation have attempted to address this incentive. Municipalities are now required to pledge at least 85% of their municipal tax increments to TIF district debt. However, the incentive still exists because in most municipalities in Vermont, the education tax rate is higher than the municipal one. The wider the difference in education tax rates and municipal tax rates, the greater the revenue to be captured from the State and the greater this incentive.

Legislators might want to be mindful of these incentives. Approval of additional districts will potentially have a compounding effect on the incentives for non-TIF municipalities to establish TIF districts. If these incentives lead to districts, the cost to the State Education Fund will grow. Legislators might also want to discuss the appropriate level of State-municipal cost-sharing to limit the growth in this incentive.

### **6) Legislators need to be mindful that TIF involves considerable uncertainty.**

The success of a TIF district relies on events in the future, namely its ability to spur new investment, generate future property value growth, and incremental tax revenues. The scale of infrastructure improvements a municipality can undertake is dependent on the amount of debt it can afford, which is in turn, dependent on the amount of future incremental tax revenues a TIF district could generate. Basing any development or policy decisions on future events is inherently risky; TIF is no different.

**TIF districts could be subject to upside opportunities.** If the amount of development exceeds what was expected, then excess tax increments present a windfall to the municipality (but not necessarily the State) it could use to pay off debt sooner. Furthermore, any unexpected development could create new economic activity, providing other benefits to a municipality, such as higher wages and higher non-property tax revenue (if the municipality has a local option sales tax). Establishing a TIF district may also draw in other types of funding, such as federal or State loans and grants.

**TIF also involves downside risks and fiscal consequences.** The main downside risk is that future property value growth and tax increments fall short of their projections. If a municipality has incurred debt against these tax increment projections, it could put significant fiscal pressure on the municipality. If a municipality is unable to repay debt obligations because of missed tax increment projections, the State may be forced to extend the increment retention period (such as with the Milton North and South TIF district), prolonging costs to the Education Fund. While no municipality in Vermont has

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John E. Anderson. "Tax Increment Financing: Municipal Adoption and Growth." National Tax Journal. Vol. 43, No. 2 (June, 1990), pp. 155-163.

yet to miss a debt payment on TIF debt to date, actual tax increments have regularly missed projections. Legislators may want to be mindful of the potential consequences of these missed projections.

**Moreover, there is uncertainty surrounding but-for claims.** JFO has attempted to provide a framework for estimating costs to the Education Fund using various baseline assumptions. However, because it is impossible to know what might have occurred absent the use of TIF, these estimates cannot be made with complete accuracy.

In sum, legislators need to be mindful that no estimates of future property growth, tax increments, or but-for claims can be made with certainty. Understanding the upside and downside consequences of this uncertainty, and weighing the probability that they will occur, will help inform the TIF approval and evaluation process.

One consequence of this uncertainty is that it is difficult to have a full understanding of what TIF's costs will be going forward, and as such, gives policymakers little control over its costs. Legislators need to be mindful that the only way to have full control of the costs of the program is to place limits on the number of TIF districts in the State.



## Boxes

### **Box 2: Indirect State Funding of TIF Districts**

Vermont's TIF program allows a TIF district to capture a State tax (the education property tax) in addition to municipal property taxes. Because of this, Vermont's program, at first glance, may seem more generous than those states where only municipal property taxes are retained. However, in those states where the state is responsible for providing some level of funding for local education, if the municipality uses TIF and freezes its property tax base, the state could bear the indirect cost of making up the gap in education spending and municipal funding.

Consider the case of Maine, where municipalities receive state education aid. Normally, when there is an increase in property values, the amount of state education aid is reduced because a municipality can now afford to pay more toward its schools than before, resulting in a higher municipal share of the school district budget. However, by using TIF, the municipality is able to protect itself against this drop in state aid; the school district does not receive any additional property tax from new property value growth so the state maintains the same level of education aid as before. The City of Portland alone estimated this "savings" to be \$715,000 in FY2016.

Source: City of Portland, Maine, Economic Development Department. "Tax Increment Financing, Fiscal Year End 2016 Annual Report." October 2016.

<http://www.portlandmaine.gov/DocumentCenter/Home/View/14871>

### **Box 3: City of Louisville, Yum! Center TIF District**

In early 2006, the city of Louisville, Kentucky, together with the University of Louisville, announced the construction of a new multipurpose arena in the heart of downtown Louisville. The primary tenant of the arena was to be the University's basketball teams, although other events (concerts, shows) would use the arena as well. The total investment for the arena was \$435 million, of which \$265 million was expected to be paid through the use of TIF.

The city established a 2.45 square mile TIF district around a large portion of downtown. Property, sales, and wage tax increments were entitled to be retained for a period of 20 years. The city then bonded against these tax increments, creating a revenue bond. The debt payments relied on an economic analysis that stated that the tax increment would be \$4.5 million in the first year (2010), and then increase to up to \$10 million in subsequent years. Economic analysis projected that the arena would create \$4.6 billion in economic activity.

Almost immediately, tax increments were short of projections. In the first year, increments were \$615,000 (versus \$4.5 million projected). Second year increments were \$2.1 million (versus \$6.6 million projected). As of the end of 2016, the arena had produced \$35 million less incremental tax revenue than projected. The economic benefits of the arena as of 2015 were estimated at \$580 million, which were \$36 million short of what was initially projected. An audit of the projections done for the arena's tax increments showed that those projections were improperly calculated and inflated.

The shortfall in tax revenue, and the prospect of default, produced significant fiscal pressure on the city, the arena, and the state. In March 2017, the state agreed to a package to extend the increment capture period from 20 to 45 years. The city of Louisville increased its annual payment to the arena authority by \$4 million (up to \$10.8 million). The city also renegotiated with the University to pay larger lease payments.

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### **Box 4: California and Redevelopment Agencies**

California pioneered the use of tax increment financing in the 1950s when the legislature established the ability for a city or county to declare an area as blighted and use the growth of future property taxes to fund development in the area. The authority over this area would be called a Redevelopment Agency (RDA). For the first 30 years, take-up of the program was slow and those cities and counties that did use it limited it to smaller areas.

Two important events changed the program in the 1970s. The first was the passage of Chapter 1406 by the legislature. This statute guaranteed a certain level of funding to school districts if there were local revenue shortfalls because of lower property values. The second was the passage of Proposition 13 in 1978. The new constitutional amendment, passed by voter initiative, significantly reduced a city and county's ability to raise new taxes in two ways. First, it capped property taxes at one percent of full cash value of the property at the time of acquisition. Second, any increase in property taxes had to be approved by two-thirds of voters.

These two policy changes instantly made RDA more appealing to cities. First, because of the revenue limits, if they established an RDA, the state would now be responsible for making up any shortfalls in revenue that resulted from the diversion of tax increments. Second, it allowed a city to increase its property tax revenue at the expense of other entities in the state.

Under an RDA, a city could designate a special district for redevelopment. The area within this district would then be entitled to not only municipal property tax increments, but also those of the county, and other special district taxes. Capturing these other entities' tax increments did not require their approval, nor did establishing an RDA or incurring new debt require voter approval. By doing this, cities and counties could work around the property tax caps set by Proposition 13, while at the same time because of Chapter 1406, avoiding any fiscal harm to their school districts from diverting tax revenues.

The result was explosive growth of RDAs. Entire cities would establish themselves as RDA districts. RDA districts would often span 20,000 acres or more. By 2011, the state was responsible for making up 12% of forgone property tax increments to school districts, costing over \$2 billion annually.

During a budgetary crisis in 2011, Governor Jerry Brown proposed closing down all RDAs in the state. To do this, the state would collect all RDA tax increments, totaling \$5.7 billion in 2012. \$2.2 billion of this would be used to pay down existing RDA debt while \$3 billion would be funneled to local governments. Going forward, existing RDAs would be required to pay down their debts and remit excess tax increments to local governments.

In June 2011, the California legislature passed Assembly Bills 26 and 27 during a special session; AB 26 dissolved all RDAs in the state while AB 27 outlined a process where RDAs could continue to exist if they offset state payments to school districts by remitting tax increments to local governments. The California League of Cities and the California Redevelopment Association immediately challenged the bills in court. In December 2011, the Supreme Court of California upheld AB 26 but struck down AB 27. As such, all RDAs were subject to the dissolution terms in AB 26.

TIF has returned to California since 2011. It now has two programs: Enhanced Infrastructure Financing Districts (EIFDs) and Community Revitalization and Investment Authorities (CRIAs). EIFD is exclusively used to finance new infrastructure, while CRIAs are most similar to the RDAs. However, with CRIAs, municipalities are now only entitled to capture their own tax increments (unless they gain approval from other entities), and the approval process requires three public hearings. Moreover, property owners and residents have the power to veto its approval. Since their establishment, take-up of both programs has been much slower than those of the RDAs.

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## Appendix

<b>Table A1: TIF Districts – Legislative History</b>	
<b>Act No.</b>	<b>Overview of Legislation</b>
1985 Acts and Resolves No. 87	<ul style="list-style-type: none"> <li>• First TIF-enabling legislation</li> <li>• Burlington (waterfront) authorized under this legislation in 1996, and the city voted to expand the TIF in 1997</li> <li>• Newport TIF authorized under this legislation in March 1997</li> </ul>
1997 Acts and Resolves No. 60	<ul style="list-style-type: none"> <li>• Changes in education financing to statewide property tax</li> <li>• TIF districts in Burlington (waterfront) and Newport grandfathered to allow for utilization of the new State education property tax</li> </ul>
1998 Acts and Resolves No. 71	<ul style="list-style-type: none"> <li>• Authorizes VEPC to approve additional TIFs as part of the Economic Advancement Tax Incentive program (requiring job creation)</li> <li>• Milton (North and South) TIF district approved under this authority</li> </ul>
2000 Acts and Resolves No.159	<ul style="list-style-type: none"> <li>• Creates a TIF district in Winooski through special legislation</li> </ul>
2003 Acts and Resolves No. 68	<ul style="list-style-type: none"> <li>• Amendment to Winooski TIF district relating to calculation of “excess valuation” of property</li> </ul>
2006 Acts and Resolves No.184	<ul style="list-style-type: none"> <li>• Sets out VEPC approval process and framework for new TIF districts</li> <li>• Caps TIF districts at 10 and not more than 1 per town for a five-year period, ending June 30, 2011</li> <li>• Milton (town core), Burlington (downtown), Colchester, Hartford, St. Albans, and Barre approved under this authority and subject to VEPC process</li> </ul>
2008 Acts and Resolves No. 190	<ul style="list-style-type: none"> <li>• Caps TIF districts at 6</li> <li>• Limits not more than 1 TIF per town for a five-year period, ending June 30, 2013</li> <li>• Changes what type of financing available</li> <li>• Inserts reporting/auditing requirements</li> <li>• Changes when debt can be incurred</li> <li>• Retroactively approves type of debt used for Burlington</li> </ul>
2009 Acts and Resolves No. 54	<ul style="list-style-type: none"> <li>• Reopens Burlington (waterfront) TIF for debt purposes</li> <li>• Applies different requirements to Milton (town core) TIF district, including different types of financing available and length of time increment can be retained</li> </ul>
2011 Acts and Resolves No. 45	<ul style="list-style-type: none"> <li>• Changes audit requirements</li> <li>• Treats Milton (North and South) TIF as one district for auditing and reporting requirements</li> <li>• Amends Burlington’s formula for payment to the Education Fund</li> </ul>

2013 Acts and Resolves No. 80	<ul style="list-style-type: none"> <li>• Prohibits VEPC from approving additional TIF districts other than the following: Burlington (Downtown), Burlington (Waterfront), Town of Milton (North and South), City of Newport, City of Winooski, Town of Colchester, Town of Hartford, City of St. Albans, City of Barre, and Town of Milton (Town core)</li> <li>• Permits the approval of the City of South Burlington if approval granted by December 31, 2013</li> <li>• Delegates rulemaking authority to VEPC</li> <li>• Imposes certain information reporting and auditing requirements</li> <li>• Clarifies how tax increment may be used</li> <li>• Permits the City of Burlington to incur indebtedness in its waterfront TIF district for an additional five years, beginning January 1, 2015</li> <li>• Various technical amendments</li> </ul>
2014 Acts and Resolves No. 174	<ul style="list-style-type: none"> <li>• Various technical amendments, including removing a redundant reporting requirement for the Burlington TIF, clarifying when related costs may be taken, clarifying the listing practices for calculating original taxable value, and clarifying who calculates the increment and how it is accounted for at the municipal level</li> <li>• Clarifies what information must go into an audit report and amends the schedule for audits to harmonize the timing for all districts</li> </ul>
2015 Acts and Resolves No. 57	<ul style="list-style-type: none"> <li>• Removes certain special assessments in a municipal charter from the property tax for the purpose of assessing property values and tax increment in a TIF district</li> </ul>
2016 Acts and Resolves No. 134	<ul style="list-style-type: none"> <li>• Delays the audit of the Milton Town Core district by one year</li> <li>• Extends the time period that the City of Burlington can incur debt on certain parcels in the Burlington Waterfront TIF district and the time period that Burlington can retain municipal and education tax increment</li> </ul>
2017 Acts and Resolves No. 69	<ul style="list-style-type: none"> <li>• Requires annual JFO report on TIF districts</li> <li>• Changes education property tax increment split to 70% from 75%</li> <li>• Requires municipalities to send not less than 85% of the municipal property tax increment to TIF district related costs</li> <li>• Caps the number of TIF districts at six but Emergency Board can increase</li> <li>• Stricter location and project criteria</li> <li>• Grandfathers all TIF districts approved before 2017 under 2013 Act 80 statutory guidelines</li> </ul>

<b>Table A2: Historical Growth Rates of Vermont's Grand List</b>			
	<b>Average Annual Growth Rate Over The Past...</b>		
	<b>5 Years</b>	<b>10 Years</b>	<b>20 Years</b>
<b>Addison</b>	0.1%	3.6%	4.3%
<b>Bennington</b>	-1.7%	1.9%	3.5%
<b>Caledonia</b>	-0.4%	3.5%	3.6%
<b>Chittenden</b>	1.9%	3.6%	4.7%
<b>Essex</b>	-1.7%	2.7%	2.6%
<b>Franklin</b>	1.3%	3.4%	4.3%
<b>Grand Isle</b>	-0.4%	3.5%	4.8%
<b>Lamoille</b>	-1.0%	3.1%	5.1%
<b>Orange</b>	-0.7%	2.9%	3.7%
<b>Orleans</b>	0.6%	4.3%	4.6%
<b>Rutland</b>	-2.5%	1.5%	2.9%
<b>Washington</b>	0.2%	3.4%	4.3%
<b>Windham</b>	-0.1%	2.4%	3.1%
<b>Windsor</b>	-1.6%	1.8%	4.1%
<b>Statewide Average</b>	-0.1%	2.9%	4.0%

Source: Department of Taxes, Division of Property Valuation and Review Annual Reports

### **Tables A3 to A6: Alternative Estimates of Fiscal Impacts**

<b>Table A3: Consensus Forecast Estimate of Fiscal Costs to the Education Fund Due to TIF</b>		
	<b>Exemptions from the Statewide Grand List due to TIF</b>	<b>Fiscal Impact on the Education Fund</b>
2017	\$338,000,000	-\$5,200,000
2018	\$370,000,000	-\$5,692,308
2019	\$415,000,000	-\$6,384,615
2020	\$476,000,000	-\$7,323,077
2021	\$528,000,000	-\$8,123,077

Note: Excludes the Bennington TIF district

Source: Consensus Forecast, Education Fund Outlook

Note: The estimates above assume a baseline growth assumption equal to the TIF growth assumption. That is, all the development that occurred within Vermont's TIF districts would have occurred without the use of TIF. Beyond 2021, the cumulative cost of TIF to the Education Fund is projected to be over \$100 million, using this methodology and these assumptions. From 2017 to 2030, the cumulative cost is greater than \$135 million.



<b>Table A4: VEPC Estimate of Fiscal Impact on the Education Fund</b>		
	Incremental Education Property Taxes Generated	Fiscal Impact on the Education Fund
2017	\$7,479,260	\$1,180,640
2018	\$8,917,792	\$1,540,273
2019	\$9,857,661	\$1,775,273
2020	\$11,687,484	\$2,232,696
2021	\$14,330,861	\$2,893,540
2022	\$14,912,530	\$3,038,958
2023	\$15,597,061	\$3,210,090
2024	\$16,400,867	\$3,411,042
2025	\$15,669,899	\$3,542,538
2026	\$14,297,764	\$3,574,441
2027	\$14,673,942	\$3,668,486
2028	\$15,062,060	\$3,765,515
2029	\$15,462,549	\$3,865,637
2030	\$15,875,854	\$3,968,963

Note: Excludes the Bennington TIF District

Source: 2017 VEPC TIF District Annual Report

Note: The estimates above assume baseline growth equal to 0%. That is, no development would have occurred over this period absent the use of TIF. The TIF district growth assumptions in these estimates originate from the individual TIF applications. Cumulatively from 2017-2030, the fiscal benefit to the Education Fund using this assumption and methodology is approximately \$42 million.

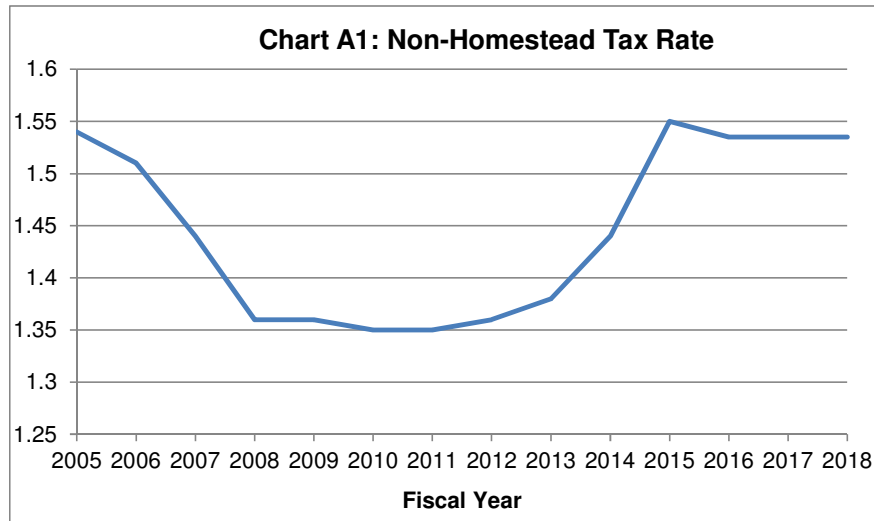
<b>Table A5: Fiscal Impacts to the State Education Fund (Using baseline growth of ten-year county average growth)</b>			
	What it receives under TIF	What it receives under no TIF	Difference (Negative=cost)
2017	\$9,815,942	\$11,416,892	-\$1,600,950
2018	\$10,016,357	\$11,841,377	-\$1,825,020
2019	\$10,912,075	\$12,979,806	-\$2,067,730
2020	\$11,126,562	\$13,447,110	-\$2,320,548
2021	\$11,332,580	\$13,930,647	-\$2,598,067
2022	\$11,517,863	\$14,430,987	-\$2,913,124
2023	\$11,682,677	\$14,948,720	-\$3,266,043
2024	\$11,853,644	\$15,484,457	-\$3,630,813
2025	\$12,031,005	\$16,038,831	-\$4,007,826
2026	\$12,263,672	\$16,612,497	-\$4,348,826
2027	\$14,256,402	\$17,206,135	-\$2,949,733
2028	\$15,246,344	\$17,820,445	-\$2,574,102
2029	\$15,576,423	\$18,456,156	-\$2,879,733
2030	\$18,778,135	\$19,114,020	-\$335,885
<b>Total</b>	<b>\$176,409,679</b>	<b>\$213,728,079</b>	<b>-\$37,318,400</b>

Note: The estimates above assume baseline growth equal to the TIF districts' ten-year average growth rate of the county's grand list. The TIF district growth assumption is 6% year-over-year.

Table A6: Fiscal Impacts to the State Education Fund, in Real Dollars (Using baseline growth of 20-year county average growth +/- 50 percentage points <sup>a</sup> )			
	What it receives under TIF	What it receives under No TIF	Difference (Negative=cost)
2017	\$9,642,875	\$12,590,365	-\$2,947,490
2018	\$9,656,806	\$12,990,015	-\$3,333,209
2019	\$10,324,060	\$14,055,190	-\$3,731,130
2020	\$10,335,039	\$14,469,243	-\$4,134,204
2021	\$10,347,595	\$14,894,598	-\$4,547,003
2022	\$10,356,836	\$15,331,608	-\$4,974,772
2023	\$10,351,631	\$15,780,635	-\$5,429,003
2024	\$10,352,246	\$16,242,052	-\$5,889,807
2025	\$10,674,161	\$16,716,246	-\$6,042,085
2026	\$12,305,023	\$17,203,612	-\$4,898,589
2027	\$12,873,254	\$17,704,558	-\$4,831,305
2028	\$13,009,312	\$18,219,506	-\$5,210,194
2029	\$16,407,541	\$18,748,887	-\$2,341,347
2030	\$18,654,771	\$19,293,149	-\$638,378
<b>Total</b>	<b>\$165,291,148</b>	<b>\$224,239,664</b>	<b>-\$58,948,516</b>

<sup>a</sup> If the district was in Chittenden County, 50 percentage points were added. If it was not, 50 percentage points were subtracted

Note: This estimation deflates the fiscal impact estimates from Table 3 by the Personal Consumption Expenditure (PCE) deflator. This methodology decreases the annual cost of TIF to the Education Fund but pushes the break-even point even further in the future.






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**Vermont Economic Progress Council**

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**Agency of Commerce and  
 Community Development**

January 17, 2018

Stephen Klein  
 Chief Fiscal Officer  
 Legislative Joint Fiscal Office at the Vermont General Assembly  
 One Baldwin Street  
 Montpelier, VT 05633  
 802.828.5768

Dear Mr. Klein,

On January 15, Vermont's Joint Fiscal Office (JFO) released a report examining the use of Tax Increment Financing (TIF) in Vermont. As Chair of the Board and Executive Director of the Vermont Economic Progress Council, we are writing to ensure balance and clarity and, in part, to express our concerns as this report is considered by legislators.

At the heart of the report's findings are two conclusions that we are concerned may be based on incomplete analysis and inaccurate research: first, that TIF districts represent an investment for which the report does not foresee a return; and, second, though costs are shared by all, the benefits of TIF districts will be unevenly shared across the state. We disagree with these conclusions.

TIF districts are indeed an investment, and a long-term one at that. But measuring the "return" on that investment – the economic impact of a TIF district – is not so easy as counting dollars in and out of the Education Fund, as done in the report. Investing in the infrastructure of Vermont's rural downtowns, encouraging density, discouraging sprawl, and giving our communities some control over their economic futures will make our development sustainable, protect our environment, and make more of our State livable for years to come in ways that cannot be quantified by an economist. That does not mean, however, those impacts should be discounted – though we are concerned that this report does just that.

And make no mistake, the impacts will be felt statewide. We all benefit from good roads throughout the state, regardless of whether our car drives on every mile of asphalt, because it is the network that supports the state economy. Everyone's property taxes go to the Education Fund, regardless of whether one has or will have children in Vermont schools, because we all agree that investing in education strengthens the state. The same is true with our downtowns. No matter where they live, all Vermonters would benefit from vibrant downtowns across the state that attract new families, promote walkability, create new housing stock, bring in and spread around tourism dollars, and give seniors opportunities to downsize while still staying in the communities they've been a part of for years. A Vermont with growth in not just Burlington but also in Bennington, St. Albans, and other towns is a stronger state than one with growth in one place and stagnation or depopulation everywhere else.

Opponents of the use of TIF have responded to the points above by saying that these developments are happening anyway (and indeed, the conclusions in the report rest on such an assumption). The trends in

our downtowns are clear, even if some economists believe otherwise. Since the establishment of a TIF district in St. Albans, the average annual increase in the grand list values within the district has been more than \$10 million, while the annual average, city-wide, before the TIF was \$1.3 million. If that astounding increase alone doesn't convince you that the assumptions in this report are incorrect, talk to anyone who walked around downtown St. Albans in 2010: they would agree that such development would not have occurred without the TIF.

When the Vermont Economic Progress Council approved Bennington's TIF district, space downtown above the first floor was mostly vacant. No significant commercial investment had been made in downtown Bennington in the previous seven years – save a bed and breakfast and a dollar store, the latter of which is generally considered an indicator of financial anxiety, not growth. If you heard the testimony of community members in Bennington, as they described what TIF would enable them to accomplish where nothing could be done before, you would understand that the reality of Bennington's challenge was different from the 3% annual growth rate the report assumes the town would have anyway.

We recognize the difficulty in making projections and measuring impact in these situations, which is why we agree with the report's finding that our system for monitoring and evaluating TIF districts could be improved. Specifically, we suggest that future TIF districts conduct independent and professional impact evaluations, and that evaluation design be taken into account before construction begins – a best practice when conducting such evaluations. What we learn from thorough impact evaluations can help inform future policy choices, based on observed facts measured against criteria established ahead of time, instead of relying on arbitrary assumptions and incomplete data, data which is cherry-picked after-the-fact to support a preexisting view.

The fact that Vermont's TIF statute is more responsible and risk-averse than other states – another point on which we are in agreement with the report – only strengthens this position. We have adopted best practices learned from decades of TIFs in other jurisdictions and from our own experience, and as a result Vermont's TIF program is the gold standard nationally.

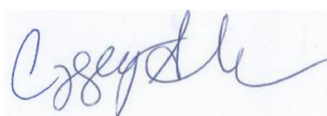
Yet despite that fact, the report relies on research on other states' programs to reach questionable conclusions about what we can achieve in Vermont. Applying an analysis of other states' mistakes – mistakes that we have already learned from – to make projections in Vermont does not help us understand anything about our own program.

We will continue to evaluate this report and make suggestions for further and future assessment of TIF successes and impacts. At this stage we would not advise any changes be made to the TIF statute. TIF one of the best tools we have for revitalizing our downtowns. Let's give our existing policies and program time to work, take time to do balanced and accurate assessments of its efficacy, and set in motion future plans to subject it to well-designed evaluations.

Sincerely,



Stephan Morse  
Chair, VEPC Board



Casey Mock  
Executive Director, VEPC

## I. Summary

The TIF program has generated \$2 million for the Education Fund through 2016 and is projected to contribute a total of \$257.5 million to the Education Fund during the life of the TIF districts active through 2016, contrary to this report's claim that TIF is a net cost to the Education Fund.

In the time available for review, a detailed analysis of the model, a point-by-point commentary, and detailed review of the literature cited in the report were not feasible. The discussion herein will focus on the following major areas, many of which are cross-cutting and recur throughout the report:

1. The report does not evaluate TIF in the context of other economic development tools, as required by statute. It is our view that no superior alternative to financing downtown revitalization across Vermont exists, and nothing in the report rebuts that view. We urge legislators to take into consideration the lack of a comparison to other tools in weighing the utility of the report's findings.
2. Several claims made throughout the report rely on literature that is either biased or inapplicable. This undermines the findings throughout the document, but such a result was also inevitable because no research has been done on a TIF program that resembles Vermont's. The paucity of relevant literature also supports our suggestion for an independent monitoring and evaluation program.
3. The report's methodology for calculating the cost of TIF relies on so many assumptions as to make the figure arbitrary and unhelpful for directing policy, especially absent comparisons to other tools. We also fundamentally disagree with several of the assumptions in the model, any one of which would substantively change the outcome of the analysis, and several of which are based on inapplicable research.
4. The report includes several suggestions for improving VEPC's approval and monitoring and evaluation mechanism. We agree with some of these suggestions and disagree with others. Notably, we do not believe "a cost-benefit analysis" as suggested in the report would be additive, and a thorough comparison of Vermont's practice to other states makes that clear. We do agree that monitoring and evaluation could be improved and have a specific proposal for doing so that takes into account internationally recognized best practices.
5. The report's claim that TIF creates equity issues among municipalities is an attempt to create controversy where none exists. Much as public education and roads are public goods that benefit all regardless of use, we believe that healthy, vibrant downtowns across the state are a statewide public good and benefit all Vermonters. No evidence to suggest otherwise is presented in the report.

While we disagree on many of the details, we look forward to working with JFO and other stakeholders on ensuring effective outcomes in Vermont's TIF districts.

**II. The report does not evaluate TIF in the context of other economic development tools, as required by statute.**

JFO's statutory charge in 24 V.S.A. § 1892, as amended by the Legislature in Act 69 of 2017, states that the report was to include a comparison of Vermont's TIF program to other economic development tools:

- (f) The report shall include:
- (1) a recommendation for a sustainable statewide capacity level for TIFs or *comparable economic development tools* and relevant permitting criteria;
  - (2) the positive and negative impacts on the State's fiscal health of TIFs *and other tools*, including the General Fund and Education Fund;
  - (3) the economic development impacts on the State of TIFs *and other tools*, both positive and negative;
  - (4) the mechanics for ensuring geographic diversity of TIFs *or other tools* throughout the State; and
  - (5) the parameters of TIFs *and other tools* in other states. (emphasis added)

The repetition of “other tools” in each entry makes clear that the legislative intent was for the report to evaluate TIF in the context of a discussion of other economic development tools. It is our view that no superior alternative to financing downtown revitalization across Vermont exists, and nothing presented in the report rebuts that view. We urge legislators to take into consideration the lack of a comparison to other rural downtown development tools in weighing the utility of the report's findings.

Of the report's 66 pages, only page 52 contains a response to this part of the statutory charge. The table on that page lists alternatives to TIF for funding downtown infrastructure development. Although the table includes columns for “pros” and “cons,” the report does not explicitly discuss how these tools would work in Vermont, how well they would work compared to TIF, or what the impacts would be on the state's fiscal health. Instead, we have only a partial analysis without context.

This missing context is fundamental, as it would have provided a yardstick by which to measure the report's other findings. If someone tells you the cost of a gallon of gasoline is \$2.00, that alone does not reveal anything about whether that is cheap or expensive gas, or whether you are receiving value for your money or wasting it. Only after you know the price is something more like \$2.50 down the street – or that \$2.00 gas is your only option and the alternatives are jet fuel and rubbing alcohol – can you fairly evaluate that \$2.00 cost.

We believe that an in-depth analysis of other rural downtown infrastructure financing tools would have revealed the situation at hand to be more like the analogy above, in that the only other options – like putting jet fuel or rubbing alcohol in your gas tank – would not be the right fit for Vermont, ineffective, costly, or even counterproductive. Among the alternatives presented on page 52, each has obvious limitations: either (1) requiring a major appropriation and administrative infrastructure (in the case of targeted matching grants); (2) needing scale beyond what is possible in Vermont to be effective (in the case of business improvement districts, public private partnerships, and infrastructure banks); (3) not meeting Vermont's needs (in the case of

revolving loan funds and gap financing; we already have VEDA, and it's generally easy for developers to access loan capital); or (4) not appropriate for Vermont's tax system (as with metropolitan area projects, which are funded by local sales tax increases – which are limited in Vermont, regressive in practice, and on a small scale not effective at raising large sums of money).

If big city options aren't realistic for Vermont's towns, what is there available for smaller downtowns? Not much that isn't federal in origin. Simple Google searches for “rural downtown infrastructure financing,” “small town revitalization funding,” and other related terms reveals a theme: federal funding, through USDA and community development block grants, are the major component to most small-town revitalization efforts across the country. Vermont already makes use of these resources, and in fact CDBG grants are often effectively paired with the use of TIF. What else is clear from cursory searches is that these Federal resources are under threat, with huge cuts to these programs proposed by the current administration in Washington. No single, easy solution exists, and at best, small communities looking to revitalize their downtowns across the country cobble together funding from a mix of federal grants and programs like TIF.

Any objective evaluation of Vermont's TIF program against other downtown revitalization tools would reveal that our program, when compared against other options, is designed to maximize positive impact on the state while minimizing risk. We recommend the alternatives be considered before any changes are made to Vermont's TIF statute.

### **III. The report relies on literature that is either inapplicable or biased.**

Underlying the approach to evaluating TIF in the report as well as several of its specific claims like demand substitution (discussed herein in Section IV.B) and TIF “expansion” (p. 54) are theories derived from academic and non-academic literature that is at best irrelevant to Vermont and at worst biased. The reliance on irrelevant academic literature calls the findings of the report into question, since these theories are relied upon throughout and are fundamental to the modeling assumptions therein. We recommend legislators read the report with skepticism of these assumptions and theories insofar as they originate with the cited literature.

The table provided on page 40 provides a helpful tool with which to evaluate the relevance of the literature cited in the report. To summarize: out of twelve academic sources and state evaluations of TIF programs, four evaluated TIF in Indiana, three evaluated Illinois, two evaluated California, and one each evaluated Wisconsin, Michigan, and Missouri. For the sake of brevity, we will only highlight aspects of the more frequently evaluated states' programs – California, Illinois, and Indiana – but given the uniqueness of Vermont's TIF statute, we expect the same to be true of the other three states.<sup>67</sup>

*California's* redevelopment agency program (RDAs), the first TIF statute nationally, has also been one of the most problematic by any objective measure. TIF was abolished in 2012 (though a new program was later reinstated), as the

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<sup>67</sup> We believe the summary herein is representative, but this limited survey is all that was possible to compile in the five days allowed ACCD and VEPC to compose a response to the final draft of the report.

unique nature of California's proposition 13 – which added a measure to the California constitution that made it difficult for municipalities to raise property taxes – created a perverse incentive for municipalities to make up for lost revenue through a proliferation of TIF districts.<sup>68</sup> California originally permitted districts to last 50 years, did not have a state-level approval authority, and had only vague location requirements for the use of TIF.<sup>69</sup>

TIF in *Illinois* is so widespread that it has its own industry lobbying association.<sup>70</sup> Illinois, like California, has only a vague “blight” requirement for location – which has led to TIF subsidizing big box stores and greenfield developments more than downtown revitalization. Illinois has no state-level approval authority for the establishment of a TIF district and allows municipalities to tap into sales tax revenue in addition to property tax revenue.

*Indiana* only added a “but-for” requirement to its statute in 2014, and only required bond issues be subject to referendum in 2008. Similar to Illinois and California, Indiana has a vague blight requirement that permits development if it simply promotes employment or attracts new businesses, leading to sprawl and greenfield builds. Like California, property tax caps enacted in 2008 provided a perverse incentive for municipalities to use TIF to increase revenue, and as a result the number of TIFs doubled in 10 years – diverting more than \$320 million *annually* in property taxes by 2016.<sup>71</sup>

What makes Vermont unique is that our legislators had the opportunity to learn from many of the mistakes summarized in the report's cited literature. The changes Vermont made to its TIF program between 2006 and 2013 were made after most of the academic evaluations cited in the report (all but two are from 2010 or earlier), and Vermont's statute adopted several best practices that emerged from those studies:

- Having a state-level approval authority rather than allowing municipalities to establish districts *sua sponte* (to discourage proliferation);
- Having strict location requirements (to prevent sprawl and discourage proliferation);
- Requiring TIF be used for public infrastructure (preventing the use of it for mere revenue generation or sending benefits directly to companies or developers); and
- Instituting a but-for requirement which is reviewed by an independent, state level authority (to evaluate whether the use of TIF is necessary in a given case).

It's no coincidence that the ills that Vermont's policies were designed to address correspond very closely to the “risks” identified in the report and the assumptions underlying its model (see Section IV). There is a type of circular reasoning at work here: first, the report cites academic

<sup>68</sup> Pg. 54, and Box 4, pg. 58.

<sup>69</sup> For basic information on California and other states, see the 2008 TIF Report by the Council of Development Finance Agencies, the most comprehensive survey of TIF in every state, available at <https://www.cdfa.net/cdfa/tifmap.nsf/index.html>.

<sup>70</sup> See the association website, available at <http://www.illinois-tif.com>.

<sup>71</sup> See, e.g., “Report Says TIF Districts Are Net Loss For Local Governments,” WFYI Indianapolis, February 9, 2016. Available at <https://www.wfyi.org/news/articles/reports-says-tif-districts-are-net-loss-for-local-governments>



studies of TIF in other jurisdictions that identified problems with TIF as used in those jurisdictions; second, those identified problems are, in turn, used as a basis for the theories in this report that undergird the model; and third, that model predictably produces results that are consistent with the cited academic theories. But the model does not correct for the fact that those same academic studies produced best practices which informed the design of Vermont's current TIF statute, which would have broken the circle and led to different results. So not only are the academic sources the report relies on irrelevant, but they also lead the report to conclusions that are the inverse of what would be expected.

The non-academic sources cited in the report are also problematic. Many of them rely on the research above, some come from advocacy groups rather than objective institutions, and none of them specifically address impacts in Vermont. The piece cited in footnote 5, for example, comes from the Cato Institute. The Cato Institute is a partisan institution that pushes a set of radical libertarian, anti-tax policies, and is funded by Charles and David Koch of Koch Industries.<sup>72</sup> Papers from such an institution should not be relied upon in a serious legislative report without some caveat about the credibility of the source.

We note that, due to Vermont's uniqueness, there is no study of TIF that has been done that would be applicable or informative, and so without a thorough analysis of how Vermont is different from the states which have been studied, the result here was inevitable. We suggest that the paucity of available, relevant data strengthens our claim in Section V below for an independent impact evaluation of future TIF districts. Such a study will generate the information that is lacking here.

**IV. The report's methodology for calculating the cost of TIF relies on so many assumptions as to make the figure unhelpful for directing policy, especially absent comparisons to other tools.**

On page 24 is a list of four explicit assumptions: that future growth in TIFs would proceed at 6% year-over-year for ten years; that a modified twenty-year county average grand list growth rate was applied to account for growth that the report assumes would occur anyway; that all projected debt would be incurred; and that property tax rates would be flat. Although each of these assumptions is defensible, alternative assumptions are equally defensible. As a result of these variables, the figure that the model returns is arbitrary and tells us nothing – absent the comparisons to other programs that Section II above notes are missing.

This last point is in fact made in the report (albeit in a footnote – footnote 29):

The assumption of twenty-year average growth or any assumption of a particular growth rate is *at best hypothetical*. Real estate growth is *not consistent* and can *vary tremendously*. Also given the small geographic areas that TIF districts encompass, the ability to project growth is all the more difficult. The JFO model approach is done for in full awareness that such assumptions are difficult at best. *Instead, they offer one way to understand the comparative issues at play.* (emphasis added)

<sup>72</sup> See, e.g., Mayer, Jane. *Dark Money: The Hidden History of the Billionaires Behind the Rise of the Radical Right*, 2016.

The footnote above was in reference to the calculation of background growth (more on that in Section IV.D), but it is relevant here as it supports our proposition: the model is based on artificial assumptions, and so it is only useful insofar as it is used comparatively. But as has been noted, no comparison was made in the report, and so we are left with an arbitrary set of numbers that should not be taken as fact and are meaningless on their own.

In this section, for brevity's sake, we will discuss only two of the report's four explicit assumptions. But first, we should comment briefly on two *implicit* assumptions that affect the outcome of the report: first, that other benefits of TIF are "uncertain" (pg. 34) and second, that growth would have occurred elsewhere anyway (p. 28, 38).

**A. The exclusion of a spectrum of economic benefits from the model makes its analysis incomplete.**

Excluded from the model are the impacts of downtown development and smart growth on anything besides the Education Fund (pg. 34). We understand that these impacts are difficult to measure (see Section V), and that the report discounts these impacts not just due to that difficulty but also as a result of the problematic literature relied upon (see Section III). Yet by not taking these factors into account, a significant portion of the expected "outputs" of TIF are ignored. As noted in 24 V.S.A. § 1893:

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.* (emphasis added).

In effect, only one of the four expected outputs of Vermont's TIF program – improving and broadening the tax base – are modeled in the report. Thus, the result is no less incomplete than it would have been had the report modeled the cost of planting a seed in the ground – plus the cost of the water and fertilizer that nourishes the seed and makes it grow – before reaching the conclusion that the plant was a net financial loss. Of course, the obvious thing missing from such a model would be the value of the plant's fruits – and so it is the case here.

While it is our expectation that TIF will have positive effects in all four areas identified by statute, we should note that the expected outputs, as worded in the statute, are disjunctive, in that they are connected by an 'or', rather than with 'and'. Vermont's TIF program would be meeting its statutory purpose if it had only one of the four required effects – three of which are not addressed in the report. Had the full impact of TIF on our towns and the state economy been modeled, we believe it would be positive and significant.

**B. Unsupported claims about demand substitution skew the results.**

Underlying the baseline growth assumption discussed in Section IV.D is the claim that TIF is simply moving "economic activity from one area to another" (pp. 28, 38-39). The report relies on

inapplicable academic literature to make this point (see Section III) and does not otherwise support the claim with data.

Academic literature and data aside, such a claim is also not supported by logic. When a developer chooses a specific project, the fact that a choice was made implies a difference in value and that the option foregone provides lower value – a lower value which, in turn, would have been reflected in lower net property value gains for the state. This is particularly true when a greenfield development replaces a downtown development: the property values for similar buildings are lower in remote locations than they are in downtowns, and so if a one-for-one substitution is made, the state would receive less property tax revenue from the more remote building.

This claim also contains an implicit assumption that developers with a choice are only choosing between sites in Vermont, as if Vermont were walled off from the region. Any development presumed to have been likely to happen anyway elsewhere could very well occur outside of Vermont, in which case none of the “background growth” property value would be available for the Vermont Education Fund. In either case, it is impossible to estimate the proportion of property value that is either reduced in value, developed outside of the state or not developed altogether. None of these issues are considered in the report.

Finally, any actual demand substitution would only occur from the perspective of the tax base: even if one believes that a hotel could presumably have the same taxable value wherever it is built in the state, this still assumes a one-for-one substitution in all respects and ignores the other externalities at play. A hotel in a downtown that provides walkability to other tourist destinations, restaurants, or businesses has a much different set of downstream impacts than a hotel built in a cornfield by the Interstate. The first location will meet more of the development goals of the statute, and so any full accounting of “growth” would take that into account – not just the taxable value. This is not addressed in the report.

This claim substantially affects which baseline growth rate is applied in the model (see Section IV.D) and prejudices the analysis throughout.

**C. The assumption of 6% year-on-year growth in TIF districts is arbitrary and not based on in depth analysis – but has a substantial effect on the outcome.**

The 6% assumption in the report relies on a percentage that is “similar to what Vermont’s TIF districts predicted their growth would be in their applications, on average.” This figure has a huge impact on the output of the model: the difference between a 6% growth rate and an 8% growth rate (in the model as of the preliminary draft in December) is the difference between a \$32 million cost to the Education Fund and a \$10 million net *gain* by 2030. Just for clarity, a difference of 2% in this one variable results in a more than \$40 million swing, with a totally different outcome.

Vermont’s TIF districts are each unique, and several of them have come into existence through different means and under different statutory regimes and economic conditions. A detailed look at the infrastructure investment and subsequent growth in grand list values year-by-year, district-by-district, would reveal that any attempt at averaging would misrepresent what has happened on

the ground. TIF district development tends to occur in fits and starts. A flat average composed of an extremely small sample size does not reflect reality. But our point here is not to quibble about the validity of the figure used in the report, but rather to point out that it is an arbitrary choice that has an outsize impact on the results.

In sum: assuming TIF district growth to be an average percent year on year misrepresents how these developments occur, and even a small change to the assumption has outsize effects on the model. We believe this caveat should be more strongly stated throughout the report, and such a caveat lends credence to our position that the analysis conducted in the report is not useful on its own but only in comparisons to similar evaluations of other tools.

**D. The assumption of a baseline growth rate above 0% not is based on any facts or data.**

The analysis on page 32 further illustrates the point made in Section IV.C – that an arbitrary, small change in the percentage applied results in an outsize impact on the results. But in the case of the background growth rate, the mathematical difference between applying any percentage of assumed growth without the TIF and applying 0% – which assumes development is because of the TIF – is huge.

The note on page 23 is worth emphasizing: “In nearly all instances, *with the exception of VEPC’s assumptions (0% baseline, no-TIF growth)*, TIF represented a fiscal cost to the Education Fund.” In other words, if the assumption that none of the development taking place in the TIF district would have occurred absent the TIF investments (See Section IV.B above) were applied, the impact on the Ed Fund *would be positive* by several million dollars. No data is provided to support why a 0% baseline was not used. Instead, such claims rest on the academic literature discussed in Section III and the unsupported claims discussed in Section IV.B.

We urge legislators to be skeptical of the report’s assumptions on this issue. Indeed, some numbers tell quite a different story. Since the establishment of a TIF district in St. Albans, the town has seen a 41% increase in property values within the district – compared to no growth in the six years prior to the formation of the TIF district. Yet the report assumes in its background growth calculation that more than \$20 million would have occurred between 2006 and 2012 and another \$15 million between 2012 and 2016. Meanwhile, throughout the rest of the state, including ski areas and greenfield retail development, total commercial and industrial property values increased at a little more than 2% annual rate between 2012 and 2016. And yet, it is a background growth of almost 4% from which the report derives the calculated “cost” to the Education Fund, with no strong data to support this choice.

We believe that a 0% baseline should have been applied, which as the report notes, would have resulted in a net gain to the Education Fund.

**V. JFO makes several suggestions for improving VEPC’s approval and monitoring and evaluation mechanism. We agree with some of these suggestions and disagree with others.**

Among the “considerations for legislators” discussed in the report is the finding that legislators may want to consider whether the current system of approval, monitoring and evaluation is

sufficient. On the issue of approval, the report recommends that VEPC adopt a quantitative “cost-benefit” model when considering applications (pp. 22, 49). On monitoring and evaluation, the report recommends that an independent evaluation be done every 5-7 years (pg. 23). We address each of those in turn below.

**A. A quantitative “cost-benefit” analysis would not be as effective as suggested in the report.**

For government programs generally, quantitative cost-benefit analyses can be helpful. In the report’s cited example of the Vermont Employment Growth Incentive (VEGI), the cost-benefit analysis conducted in that case is based on specific verifiable investments in a single business resulting in a reportable and verifiable level of new hiring and wages. ACCD and technical working groups have worked hundreds of hours to link those specific changes to changes in the Vermont economy and tax revenues, and the resulting analysis is easy to do and understand, and is useful in the process.

In the case of TIF, however, specific infrastructure construction leads to large dollar value private sector property investment, which in turn leads to increased commercial and residential activity. That increased activity has ripple effects within the TIF district. The impacts of private sector development, business growth, and improved property values in a background of global and regional economic changes are difficult to model during the application stage and difficult to monitor after project implementation – as demonstrated by the lack of such data in the model used in this report. The only evidence provided to suggest such analysis would be useful is the fact that other states do it (see pg. 18).

In fact, even though other states conduct what they call a “cost-benefit” analysis in reviewing TIF applications, Vermont’s existing review process is still more quantitatively rigorous than any state surveyed. According to the 2008 state-by-state TIF report published by the Council of Development Finance Agencies (CDFA), the most comprehensive and up-to-date summary available of every state’s TIF program, eleven states require a cost-benefit analysis be conducted prior to the establishment of a TIF.<sup>73</sup> Of those eleven, only two TIF programs require both a cost-benefit analysis and an independent, state level review, like the report suggests Vermont adopt: New Mexico and West Virginia. New Mexico’s state-level “review” lacks teeth, in that its statute only requires that the governing authority of the municipality or county that adopts TIF to notify the state secretary of finance and administration and the director of the legislative finance committee of the action establishing the TIF within ten days, not providing for any review or veto power by the state.<sup>74</sup> West Virginia, in its TIF handbook, openly states it in practice defers to local governments.<sup>75</sup>

Despite the fact that Vermont has stronger state level controls than both of these states, it is also illustrative to consider how the cost-benefit reviews are actually done in these states. Information from Albuquerque City Council Meetings suggests that, at least in Albuquerque’s case, a “cost-benefit” analysis simply meant adopting the fiscal projections prepared by consultants,

<sup>73</sup> Available at <https://www.cdfa.net/cdfa/tifmap.nsf/index.html>

<sup>74</sup> New Mexico Statutes Chapter 5. Municipalities and Counties § 5-15-4(F).

<sup>75</sup> Available at <https://revenue.wv.gov/Documents/tifhandbook.pdf>

verbatim.<sup>76</sup> A detailed review of the West Virginia Development Office TIF handbook reveals the same is true in that state. Applicants need only submit high level data about infrastructure costs and job creation on a form, with their own projections, and in their own formats, as an attachment.<sup>77</sup>

Lest the sample of states with a cost-benefit analysis be considered too small, we can also evaluate states that have a cost-benefit analysis reviewed by local institutions:

*Wisconsin* doesn't require a state review but has a local board review TIF applications. In the example of Stoughton's TIF district, a "cost-benefit" analysis simply meant that the town claims in its resolution that "the economic benefits of the redevelopment projects within the proposed Tax Incremental District . . . as measured by increased employment, business and personal income and property values, are sufficient to compensate for the cost of the improvements; and the benefits of the proposed tax incremental district outweigh the anticipated deferral in tax revenues of the overlying taxing jurisdictions."<sup>78</sup> In fact, the state provides no guidance on how to conduct such an analysis, only providing a checklist for municipalities to indicate that the projects are feasible.<sup>79</sup>

*Montana*, another state listed by CDFA as requiring a cost-benefit analysis but with a review by a local "urban renewal authority," requires only that the approving municipality state that "a sound and adequate financial program exists for the financing of said project."<sup>80</sup>

Let us compare this with the review conducted by VEPC. VEPC provides a data workbook to all applicants for TIF that standardizes the information requested and the format. An economic analyst and VEPC staff review this information for realism, coherence, and completeness before this data is presented to the VEPC Board, who then conduct the following reviews:

- Analysis of infrastructure cost and debt assumptions, real property development and property tax revenue generation assumptions.
- Availability of other sources of revenue.
- Analysis of revenues - generated through property taxes, grants received, other sources - and ability to service debt.
- Analysis of existing stock and marketability and absorption of proposed development.
- Availability of market studies.

<sup>76</sup> See, e.g., materials available at <https://cabq.legistar.com/LegislationDetail.aspx?ID=2256078&GUID=0133FC73-8DC7-463C-A371-EAC8BE0F3785>; <https://www.cabq.gov/dfa/documents/investor-documents/tax-increment-development-district-applications-1-of-3.pdf/@download/file/tax-increment-development-district-applications-1-of-3.pdf>; <https://www.cabq.gov/dfa/documents/investor-documents/tax-increment-development-district-applications-2-of-3.pdf/@download/file/tax-increment-development-district-applications-2-of-3.pdf>

<sup>77</sup> See FN 9.

<sup>78</sup> Materials available at <https://static1.squarespace.com/static/54ac5e65e4b0b6dc3e27cc0c/t/55afcbdc4b09decf8bde4ca/1437584348206/TIF+7+Creation+Packet.pdf>

<sup>79</sup> Checklist available at <https://www.revenue.wi.gov/DORForms/pe-222.pdf>

<sup>80</sup> Manual available at <https://comdev.mt.gov/Portals/95/shared/CTAP/docs/.../TIF%20Manual%202014.pdf>

VEPC's analysis of financial and market viability are clearly more formal and quantitatively rigorous than any other observed state's cost-benefit programs.<sup>81</sup> The basic fact that we require objective data presented in a standard way itself puts Vermont above any other state reviewed, and ensuring consistent presentation and analysis of objective data should be a first step in any effective cost-benefit analysis. VEPC also makes abundantly clear on its website and in its TIF materials how this review is conducted and what are the standards.

Even in the case of voter education, a cost-benefit analysis would not be additive or helpful. It is the responsibility of the municipality to decide to borrow money for public infrastructure projects and the voters in the municipality decide, through the ballot process, if the investments are worthwhile. There are many attributes of a public investment including:

- Short term benefits to the local economy based on construction costs
- The potential for additional economic activity
- Providing services to businesses and/or residents
- Preventing environmental damage
- Complying with state and federal mandates

All of the above are valid interests and it is important for the municipality to communicate the value of each when presenting the bond vote to the citizens. We do not believe that a mandated cost-benefit analysis helps citizens with this exercise, in that it is relatively easy to show greater benefits than costs and the results of the analysis will typically just show orders of magnitude of greater benefits.

VEPC is always exploring ways to improve our analysis. But a "cost-benefit" analysis as recommended in the report would not improve the quality of VEPC's analysis.

**B. An independent, professional, impact evaluation would help resolve many of the missing data points in the report and inform future policy.**

No specifics are provided with report's consideration that monitoring and evaluation be improved, other than such evaluation should be independent and occur every 5-7 years. We recommend that impact evaluations be commissioned for new TIF districts, that updates be done every five years, and that a monitoring and evaluation plan be adopted by new TIF municipalities before infrastructure projects begin that establish measurement criteria and baseline data and incorporate impact evaluations into future planning.

"Impact evaluation" has an obvious plain language meaning, but it is also a term of art. A professional impact evaluation assesses the changes that can be attributed to a particular program or policy, both the intended ones and the unintended ones. In contrast to outcome monitoring (which examines whether targets have been achieved) or a performance audit (which assesses whether resources are being effectively and efficiently used toward goals), an impact evaluation is structured to answer how outcomes would be different if the intervention had not been

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<sup>81</sup> It should be noted that examples of cost-benefit analyses done in other states, as well as the state-level standards that apply to any such analyses, were extremely difficult to locate. The fact that Vermont rates highly on transparency with regard to TIF applications – and that information about what VEPC reviews and what standards are applied are very easy to find – should lend some benefit of the doubt as to the fact that VEPC conducts a more quantitatively rigorous analysis than these other states.

undertaken. This involves counterfactual analysis: a comparison between what happened and what would have happened in the absence of the intervention. Both qualitative and quantitative methods are used, and provision could be made to evaluate the downstream effects of a TIF elsewhere in the state. Impact evaluations have been successfully used by the UN, OECD, World Bank, USAID, and the Department of State in evaluating the success of policy interventions as diverse as poverty reduction programs, workforce development programs, and children's health and nutrition programs.

Should any changes be considered to the TIF statute, we recommend that it start with this sort of impact evaluation, the results of which would effectively inform future policy discussions about TIF more than existing research or artificial models.

**VI. The report's claim that TIF creates equity issues among municipalities and its repeated invocation of "statewide benefits" is designed to create controversy where none exists.**

The report suggests that the fact that TIF is used by only some municipalities but leverages incremental statewide Education Fund revenue creates "equity issues," in that some Vermonters are paying for infrastructure in other Vermonters' towns. This claim is problematic, apart from the fact that it relies on the inaccurate assumption that TIF is a net cost.

Vermonters pay property taxes that go into the Education Fund, regardless of whether the taxpayer has, will have, or has had children that will attend Vermont schools. Vermonters pay gas taxes and motor vehicle purchase and use taxes that pay for bridges and roads that they may never drive on. Public education and roads are goods that benefit all regardless of individual patterns of use. We believe that healthy, vibrant downtowns across the state are a statewide public good and benefit all Vermonters. The report has presented no evidence to suggest otherwise.

And even if this were not the case, such concerns are misplaced. As noted in 24 V.S.A. § 1893, one of the four goals of TIF is to "enhance the general economic vitality of the municipality, the region, or the State." Again, as noted in Section IV.A, that list is disjunctive, and so it is not currently a requirement of the statute that TIF have statewide benefits.

As a final note, as discussed in Section III above, Vermont is one of a few states with a TIF statute that does not create a perverse incentive for municipalities to compete with one another for revenue or for business. To date, the environment in Vermont is collaborative, with some towns learning from others' experience whether TIF is appropriate for their needs. The report's comments on this matter appear to assume Vermont's towns compete in a Hobbesian state of nature and are designed to create controversy. No such controversy currently exists.





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# Memorandum

**To:** Steve Klein, Legislative Joint Fiscal Office  
**From:** Tom Kavet, State Economist for the Vermont Legislature  
**CC:** Catherine Benham, Joint Fiscal Office  
**Date:** January 22, 2018  
**Re:** Review of JFO Report entitled, "An Examination of the State of Vermont Tax Increment Financing Program," per Act 69 of 2017, Section J2

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Per your request, and as a party listed in the statutory charge to produce the subject report, I am writing to provide a few supplemental comments on the JFO report entitled, "An Examination of the State of Vermont Tax Increment Financing Program." While the report is an admirable effort to cover a complex topic, I believe the result may create more confusion than clarity.

Having been a participant in the creation of the VEGI program and an architect of the Cost-Benefit model used to set subsidy award levels based on measurement of potential fiscal impacts, we have evaluated the net fiscal impact of Tax Increment Financing as a general VEPC economic development tool, as well as a number of individual proposed tax increment financing proposals advanced for legislative approval over the past 20 years. As the attached memo from a consensus Technical Working Group, which included economists from the Tax Department, JFO and Administration under contract with ACCD, concludes:

*It is our unanimous position that such expenditures cannot be considered fiscally neutral, unlike VEPC awards that are subject to the Cost-Benefit model analysis, and should not be treated as such. If the legislature chooses to make TIF expenditures, it should not do so under the false impression that they are fiscally neutral or positive to the State.<sup>82</sup>*

There is no unbiased regional economic and fiscal impact model, such as the REMI-based<sup>83</sup> VEGI Cost-Benefit model, that would show any significant net fiscal benefit at the state level from the TIF program as now structured.

This is the reason every consensus Education Fund forecast since 2005 has treated excluded TIF property value as a reduction in the tax base used to establish statewide property tax rates. As of 2017, this expenditure served to add about half a cent to the average statewide property tax rate, at a cost of about \$5.2 million.<sup>84</sup> The value of the

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<sup>82</sup> Memo to Speaker of the House, Rep. Gaye Symington, dated April 11, 2006, from Tom Kavet, State Economist for the Legislature on behalf of the Joint Fiscal Office, Jeff Carr, State Economist for the Administration, and Matthew Barewicz, Consulting Economists to VEPC, and Susan Mesner, Economist, and Mike Wasser, Tax Policy Analyst, for the Tax Department. Complete memo is attached.

<sup>83</sup> The current VEGI Cost-Benefit model is built on a Vermont state model maintained by Regional Economic Models, Inc. (REMI) of Amherst, MA

<sup>84</sup> Based on detailed town and property type calculations developed as a part of the October 2017 Education Fund forecast by Deb Brighton.

excluded property in 2017 totaled about \$338 million.<sup>85</sup> With the approval of six new TIF districts during the last legislative session, this expenditure is likely to grow, contributing to further increases in statewide property tax rates in 2018 and beyond.

While there may be public benefits to State subsidies to municipalities associated with infrastructure development, we do not generally subtract ambiguous potential benefits from State expenditures when characterizing or measuring program costs. To do so creates uncertain and unrestrained expenditures, no matter how good or important a particular program may be. For example, we do not adjust reported expenditure levels for K-12 education or roads and bridges by deducting the net fiscal benefits they may provide to the State. It would be easy to develop an economic model that shows vast net fiscal impacts from the existence of public roads and schools, but this does not mean the expenditure is somehow lower or does not exist – it simply means there is some public value, fiscal and otherwise, for every State expenditure.

Tax Increment Financing should be measured in the same way – without smoke and mirrors that erroneously characterize it as “free.” It should be controlled in the same way as all other public expenditures – via the political process that evaluates any State expenditure based on its relative merit and the revenue capacity of the State. Tax Increment Financing is currently paid for through the statewide Education Fund property tax, with no specific expenditure limitations and no conscious appropriation by the legislature or Administration. Its cost is a deduction from revenues estimated by State Economists when forecasting the Education Fund tax base used to set property tax rates.

While there are many technical and evaluative deficiencies in the JFO report, it does bring a greater consciousness to this program and opens discussion to ways it may be improved. There are program variations, some of which are mentioned in the report, that could dispense the same amount of State money to municipalities with basic prudential expenditure controls, enhanced transparency, simpler and cheaper program administration, more equitable regional distribution, and greater overall beneficial impacts.

Please let me know if you or others would like any further information or explanatory detail in connection with these comments and/or the broader issues raised in the subject report.

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<sup>85</sup> See Table 1 of the Consensus Education Fund October 2017 forecast, at: <http://www.leg.state.vt.us/jfo/education/2017-Equalized%20Education%20Grand%20List.pdf>

# Memorandum

**To:** Speaker of the House, Rep. Gaye Symington

**From:** Technical Working Group: Tom Kavet, Consulting Economist to the Joint Fiscal Office, Jeff Carr and Mathew Barewicz, Consulting Economists to VEPC, Susan Mesner, Tax Department Economist and Mike Wasser, Tax Department Policy Analyst

**CC:** Steve Klein, Tom Pelham, Fred Kenney

**Date:** April 11, 2006

**Re:** Technical Working Group Review of S.165, and Related Issues

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Dear Speaker Symington,

Per your request, the Technical Working Group has reviewed S.165 and has attached consensus recommended changes affecting the technical operation of the proposed program. If there are further changes to S.165 that affect the program operation and administration, we strongly recommend additional statutory review by the Working Group so as to insure that the program functions as intended.

Given the extraordinary complexity of the proposed program, the magnitude of the public outlays at stake, and past problems with program change implementation, our most significant recommendation is that the Technical Working Group be maintained for the purpose of implementing the new program and providing operational program oversight during the first two years of the new program. Any significant technical implementation and operational issues that arise would be reviewed by the Working Group, with consensus Group recommendations to be approved by the Joint Fiscal Committee.

As you will see in the attached, we also favor the development of a plan to transition as many if the existing VEPC awardees to the new program as possible. Although any such transition would be entirely voluntary, we believe it is in the State's interest for the Working Group to develop a fiscally neutral offering that would encourage such transition. Given the time constraints and complexity of this issue, this plan could be mandated in S.165 with implementation details created by the Working Group with the approval of the Joint Fiscal Committee.

There are also issues affecting some components of S.165 that are contained in S.291 – especially with respect to Tax Increment Financing Districts (TIFs). It is our unanimous position that such expenditures cannot be considered fiscally neutral, unlike VEPC awards that are subject to the Cost-Benefit model analysis, and should not be treated as such. If the legislature chooses to make TIF expenditures, it should

not do so under the false impression that they are fiscally neutral or positive to the State.

Please let us know if you or other members of the legislature have any questions associated with the attached recommendations or would like any further input on this issue from the Group or any of us individually.