Tax increment financing (TIF) is the most important fiscal instrument for local development initiatives in this country. However, in many cases its growth has been accompanied by “moral hazard,” or incentives for the misallocation of resources. By earmarking taxes on future increases in property values to pay for redevelopment costs, TIF can function as a type of unrecognized municipal debt, sharing the problems of accountability and repayment capacity raised by state and local debt of all kinds.
About the Author

Joan Youngman is Lincoln Institute Senior Fellow and Chairman of the Institute’s Department of Valuation and Taxation. She is an attorney, scholar, and author of numerous articles and books concerning land and building taxation and valuation. She has undertaken international research and educational work for the World Bank, the OECD, the International Monetary Fund, and the Harvard Law School International Tax Program. She is the author of Legal Issues in Property Valuation and Taxation, Cases and Materials (2006), a co-author of State and Local Taxation: Cases and Materials, American Casebook Series, (9th edition 2009), and is co-editor of the books Erosion of the Property Tax Base (2009), Making the Property Tax Work – Experiences in Developing and Transitional Countries (2008), The Development of Property Taxation in Economies in Transition: Case Studies from Central and Eastern Europe (2001) and An International Survey of Taxes on Land and Buildings (1994).
TIF at a Turning Point: Defining Debt Down

Joan M. Youngman

California Governor Jerry Brown’s proposal to end tax increment financing, or “TIF,” initiatives in that state signals a dramatic change in the fiscal landscape of a region with a long history of tax innovations, often with national repercussions. That was certainly true in the case of Proposition 13, and it was also true when California introduced tax increment financing in 1952. This new instrument spread across the country, adopted in some form in almost every state, and is now “the most widely used local government program for financing economic development in the United States.” Whatever the outcome of Governor Brown’s proposal, the suggestion that TIFs are no longer sustainable in California marks a turning point worth careful consideration. Moreover, municipal experience with TIFs may shed light on larger issues of debt finance now facing many state and local governments.

In theory, TIF creates a perfect closed system of self-sustaining finance, a textbook example of “value capture.” There are important differences among state approaches, but a set of common elements forms the basic pattern. Generally, a municipality identifies a specific geographic area for redevelopment. The redevelopment initiatives may be directed by the municipality or by an economic development agency, which is typically under municipal control. They may be funded on a cash basis or, more commonly, by issuance of bonds. The crucial feature is the earmarking of taxes on future increases in property values in the TIF district to pay for redevelopment costs.

1Jessica Garrison, “Jerry Brown’s Bid to Kill Redevelopment Agencies Sets Stage for a Fierce Battle,” The Los Angeles Times, January 15, 2011. In California, tax increment financing is undertaken by redevelopment agencies, or RDAs, and Gov. Brown’s proposal is discussed as a plan to eliminate these entities. E.g., “California Redevelopment Agencies Need a Complete Overhaul,” Editorial, Oakland Tribune, March 12, 2011 (“Gov. Jerry Brown . . . has been willing to offer some highly controversial changes in state finances. None is more contentious than his bold proposal to eliminate redevelopment agencies. . . .”)  
5For example, some states allow limited use of sales tax proceeds to fund TIF initiatives. See Lauren Ashley Smith, “Alternatives to Property Tax Increment Finance Programs: Sales, Income and Nonproperty Tax Increment Financing,” 41 The Urban Lawyer 705 (2009).
TIFs can be invisible to taxpayers, for the assessor continues to value property as before, and the taxpayer continues to pay taxes in the same way. But tax collections are now divided between the portion attributable to values in place at the time the TIF district was established and the portion that represents value increases since then. For the life of the TIF district, which may be twenty to thirty years, or even longer, \(^6\) taxes on value increases are earmarked for TIF spending or repayment of TIF debt.

In theory, the TIF project requires no new taxes, and pays for itself by increasing the tax base. Because a finding of “blight” in the redevelopment area is often required for establishment of a TIF district, the government investment is considered targeted to a region that would not otherwise attract private capital. From this perspective, TIF is, as Professor George Lefcoe of the University of Southern California has written, a “win-win-win for the city, the private developer and the taxpayers.” \(^7\) It is no wonder that Sacramento Mayor Kevin Johnson, in opposing Governor Brown’s plan to end TIFs, called these projects “magical things.” \(^8\)

In appropriate situations a TIF can produce exactly these results. A formerly blighted area may blossom, tax valuations may increase as a result, and a strengthened tax base may permit expanded future public services. In other cases, government investment could fail to improve local conditions, while the freeze in future tax base growth could restrict services during the period for repayment, further diminishing the jurisdiction’s economic prospects.

The promise and popularity of TIF have placed it in a position of enormous fiscal importance. Governor Brown’s proposal signals the need to consider its risks and potential drawbacks as well.

**Risks and Incentives.** The risk of poor performance is inherent in any situation calling for financial judgment. An absence of private investment, which is the justification for government intervention, may also be a signal that the market has not identified development opportunities. In this situation, a certain number of unsuccessful investments might be the price for undertaking any ambitious redevelopment initiative. A more fundamental concern involves legislative provisions and larger institutional factors that could actually encourage unproductive investments. This constitutes what economists term “moral hazard,” an incentive for misallocation of resources. In 1952, TIF was seen as a means of raising matching funds for federal urban development grants. Several decades later, resourceful local governments facing an era of tax limitations were able to utilize this tool to support expanded spending in the face of such constraints.

Three structural elements of TIF are especially problematic: the interpretation of “blight,”

---

\(^6\) For example, Wisconsin last year extended the potential life of TIF districts to forty years. John Buhl, “Governor Signs TIF Expansion for Distressed Localities,” *State Tax Notes*, May 24, 2010, p. 576. See also text accompanying note 29, below.


the assumption that future increases in property value are caused by the TIF project, and above all the ability of a TIF district to appropriate the future tax base growth of other, overlapping jurisdictions, most notably school districts.

Blight. Many states require a finding of “blight” for establishment of a TIF district. Yet, as Professor Lefcoe has noted, truly blighted neighborhoods offer the fewest possibilities for easy increases in property value. Citing an Iowa study that found TIFs to be most successful in “booming suburbs and metropolitan areas,” he commented, “After all, that is where costly new developments have the best chance of being financed, built, and adding greatly to the property tax rolls. . . . TIF funded redevelopment built in distressed areas would seldom boost property values enough for the project to pay its own way.”

Nor would an instrument drawing on future value increases be able to support even a successful intervention in truly blighted areas if that project achieved only reduced rates of decline, or even stabilized values – however heroic such an accomplishment might be in fact. Over time, blight requirements have been all but ignored in many cases, with cities, courts, and consultants ready to accede to almost comical expansions of that term. Use of TIF as a general funding device and not as a means of assisting blighted neighborhoods is the first step away from its theoretical justification.

Causation. About twenty states require a finding that new development would not take place in the TIF district “but for” the government intervention. This has been treated as even more of a formality than a finding of blight. Blight, however subjective, at least refers to an observable physical attribute. The counterfactual prediction of what would happen but for establishment of a TIF district is so open to conjecture as to invite disregard. Because this finding is often left to the municipality establishing the TIF district, there is no incentive for an independent review. As Professor Richard Briffault has written, “The conceptual heart of TIF is that the TIF expenditure is the but-for cause of subsequent economic growth in the TIF district. . . . But for the most part, as TIF has spread the but-for requirement has fallen away. . . .”

---


10 See Lefcoe, “After Kelo, Curbing Opportunistic TIF-Driven Economic Development,” note 9, above, at 15-22. One attorney is quoted as saying, “States’ definitions of ‘blight’ are so broad and vague that they could apply to practically every neighborhood in the country. (‘Blight’ can include such things as a home not having two full bathrooms or three full bedrooms.)” Id. at 15. A 2011 audit by the California state controller’s office found that, “Even though redevelopment agencies must spend their money on improving ‘blight,’ Palm Desert dedicated almost $17 million in redevelopment dollars to improve a luxury golf resort.” Tracy Seipel, “California Redevelopment Agencies Blasted in State Review,” Mercury News (San Jose), March 7, 2011. “Near San Diego, Coronado’s redevelopment area covers every privately owned parcel in the city, including multimillion dollar beachfront homes.” Judy Lin, “Audit Faults California Redevelopment Agencies,” The Boston Globe, March 7, 2011.

Tax Base Growth. The inability to predict what would happen in the absence of TIF undermines its theoretical basis as a self-financing device that does not raise taxes. The assumption that tax base growth is caused by the TIF justifies earmarking the tax base increment to pay for that development, and lies behind the claim that TIF allows new spending with no tax increase. But it is extremely difficult to prove a specific cause for any change in property value. A municipality may have an incentive to draw the boundaries of the TIF district as widely as possible, including development that may be unrelated to the TIF investment. And value increases due only to general growth or inflation cannot be attributed to the TIF. If tax base growth that reflects inflation is allocated to the TIF district, the jurisdictions that depend on the property tax for basic funding may have to raise their tax rates or face budget shortfalls. Many local government budget items, such as health insurance for public employees, can rise at rates well above that of inflation.

The assignment of future valuation increases to the TIF district can encourage municipalities to target undeveloped land or other property with low assessed values, particularly agricultural land eligible for preferential farmland programs. These areas may not be blighted or underserved by private developers, but they may offer dramatic increases in assessed value simply by being reclassified as commercial or industrial. “A 1999 study found that 45 percent of Wisconsin’s 661 TIFs have been used to develop open space—primarily farmland—including, most famously, a Wal-Mart Supercenter built on what had been an apple orchard....”12 Moreover, many jurisdictions reassess property on a multi-year basis. For example, Cook County employs a three-year cycle, reassessing the northern suburbs one year, the southern suburbs the next, and the city of Chicago in the third year. In this situation, designation of a TIF district just before reassessment can insure an increment that has nothing to do with the TIF investment.

A plethora of economic studies have reached no consensus as to the effect of TIF on economic growth. This is not surprising, given the enormous variety of circumstances, regions, and types of projects at issue. Some studies have even found negative effects for TIF designation. For example, Professors Richard Dye and David Merriman undertook a major analysis of 235 Chicago area municipalities and concluded that “property values in TIF-adopting municipalities grew at the same rate as or even less rapidly than in nonadopting municipalities.” They reported that a second study three years later did not find “the earlier provocative result of a significantly negative impact of TIF adoption on growth, but we still find no positive impact of TIF adoption on the growth in citywide property values. Any growth in the TIF district is offset by declines elsewhere.”13 Analysts who have reviewed the voluminous literature on this point generally agree that

---

research on the effects of TIF has raised more questions than it has answered.”14 “The effect of TIF on property value growth at the municipal level thus remains unresolved.”15 “There is little clear evidence that TIF has done much to help the municipalities that use it, while it is a source of intergovernmental tension and a site of conflict over the scope of public aid to the private sector.”16

Overlapping Jurisdictions. By far the greatest moral hazard posed by TIFs concerns the ability to freeze the assessment base of overlapping jurisdictions, such as school districts. The municipality establishing the TIF district may be able to appropriate value increases, including those due only to inflation, from independent districts with no power to block this transfer. Just as tax credits and deductions can make it rational to construct an otherwise uneconomic building, the ability to draw on the tax base of separate jurisdictions provides an incentive for expenditures that would not be approved if funded by the municipality itself. In fact, a municipality may have an incentive to set up a TIF even if it reduces growth. As Professors Richard Dye and Jeffrey Sundberg explain:

With a positive pre-TIF rate of growth, the district is able to “capture” that portion of the growth in property value for use in TIF financing.

This points out what we consider to be one of the gravest flaws in TIF. If property values would grow at a high rate in the absence of TIF, even a project that results in a permanent reduction in the growth rate would be easy to finance. Policy makers unused to the concept of opportunity cost might be susceptible to making a poor decision if financial viability is confused with efficiency.17

The importance of tax base capture is such that, as Professor Lefcoe points out, “In states where local governments have no opportunity to pledge tax increments from other taxing

entities such as counties and school districts, there is very little TIF. Why have so few states granted schools, counties and other taxing entities the right to opt out of sharing their tax increments? The short answer probably lies in an analysis of the lobbying effectiveness of redevelopment agencies, schools and counties.18

The effect on school districts provided a major impetus for Governor Brown’s proposal to end TIFs in California. As Professor Tracy Gordon writes, “The catch is that the money has to come from somewhere. In California, the state is on the hook for property taxes that would have otherwise gone to schools.”19 Even ten years ago, California TIF districts were estimated to receive ten percent of all property tax revenues in the states, or $2.1 billion annually, and to have accumulated $51 billion in bonded indebtedness.20

Larger Questions. Many legislative enactments rest on faulty theoretical justifications, and it is unrealistic to look for a perfect match between the conceptual basis and the practical implementation of fiscal measures. In this situation, larger institutional structures are a principal defense against excesses and abuses, and the failure of these systemic protections is of perhaps even greater concern than a wishful legislative rationale for new enactments. At the most general level, clarity and transparency are essential to citizen oversight, but many TIF programs are largely hidden from taxpayer notice. At a very specific level, debt limits and a requirement of voter approval constitute a deliberate check on municipal borrowing, but legislatures, courts, and local officials have generally circumvented these measures by agreeing that bonds secured by tax increment financing do not constitute debt for these purposes.

Transparency. Professor Lefcoe states, “Development agencies often keep the public in the dark about their transactions.”21 The theory of self-financing can lend legitimacy to politically expedient nondisclosure. If in theory taxpayers are not required to make any new payments for these projects, lack of public participation or even awareness becomes less problematic. In the same way, the assumption that all future tax base growth is due to TIF investment helps justify the exclusion of overlapping jurisdictions from the decision to earmark that growth for TIF development. This theory presents the TIF process as a “closed circuit”: “[T]he incremental revenues pay for the public expenditures, which induce the private investment, which generates the incremental revenues, which pay for the public expenditures.”22 Yet a frozen tax base is likely to require higher tax rates, new fees, or other mechanisms to fund ongoing government operations.

Judicial Oversight. Although courts can also provide institutional protection against abuse, judicial oversight has played little role in TIF developments. This may reflect the

18 Lefcoe, “Competing for the Next Hundred Million Americans,” note 7, above, at pp. 25, 32.
21 Lefcoe, “Competing for the Next Hundred Million Americans,” note 7, above, at p. 36.
22 Briffault, “The Most Popular Tool,” note 3, above, at p. 68.
goodwill naturally extended to an apparently self-financing program to assist blighted areas. In addition, lack of public awareness reduces the likelihood of taxpayer challenges to TIF programs. When even public officials do not understand TIF provisions, it is extremely difficult for taxpayers to evaluate their impact. The professionals most familiar with these complex structures may have a vested interest in avoiding conflict over them. For example, with regard to “blight” determinations, “The attorneys most capable of filing such challenges are jeopardizing their future dealings with the city officials they sue and with officials in other cities who get wind of their whistle-blower-like behavior.”

And once TIFs became the primary instrument for municipal redevelopment and even development, the sheer magnitude of these investments, and the rise of entire businesses and professions assisting in their implementation, place an extremely heavy burden on efforts to change their method of operation. A 2007 Florida Supreme Court decision characterizing TIF financing as debt would have required voter approval of TIF bonds. The court ruled three weeks later that its decision was not retroactive, and it reversed itself entirely the following year.

What is Debt? The Florida decision dealt with the underlying challenge of characterizing debt for legal purposes. Nearly every state imposes statutory or constitutional limitations on the amount of debt municipalities may incur, and most require a voter referendum for such “general obligation” borrowing. Revenue bonds secured by a new and segregated

---

23 Lefcoe, “Competing for the Next Hundred Million Americans,” note 7, above, at p.16.
25 For a discussion of the nineteenth-century background to debt ceilings and referenda requirements, including state and local borrowing for railroad, canals, and other commercial projects, see Philip J. F. Geheb, “Tax Increment Financing Bonds as ‘Debt’ Under State Constitutional Debt Limitations,” 41 The Urban Lawyer 725, 732-33 (2009). Note 47 of that article cites work by Professor M. David Gelfand “describing the New York City fiscal crisis of the Boss Tweed era in the 1870s and the resulting twenty years it took for the City to extricate itself from the debts it incurred as a result of corruption and special interest capture.” M. David Gelfand, “Seeking Local Government Financial Integrity Through Debt Ceilings, Tax Limitations and Expenditure Limits: The New York City Fiscal Crisis, the Taxpayer’s Revolt, and Beyond,” 63 Minnesota Law Review 545 (1979). This year Professor John Wallis told the The Wall Street Journal that current state debt provisions can be traced “back to those defaults in 1841, after which legislators amended constitutions to clamp down on new borrowing. Over time, these rules have been perverted by politicians, meaning that ‘constitutional rules have made it harder to raise taxes than to raise expenditures’…. When the defaults began in January 1841, investors dumped state bonds, pushing yields above 12% in early 1841, and to nearly 30% by 1842. The consequences of those defaults would last for decades: Among historians, the rule of thumb is that U.S. states would pay interest rates one percentage point higher than Canadian issuers the rest of the 19th century. To this day, Mississippi hasn’t paid back some of those bonds, even after a 100-year English bid to collect…. For Mr. Wallis, the lessons of the 1840s are bracingly clear. Taxpayers and politicians have lost the connection between borrowing and costs. So taxpayers must be willing to approve tax rises as a direct part of new borrowing plans. ‘There is nothing
source of funds, such as tolls for a highway or bridge to be built with bond proceeds, have long been exempt from these provisions, which are designed to protect general tax revenues. TIF debt has similarly been free of these requirements, most crucially the need for a public vote on bond issues. This can be justified on the theory that it too is secured by a segregated account. But in this case the account consists of future growth in the basic property tax revenue that supports such general government functions as education, public safety, and transportation.

Criticism of the referendum requirement generally focuses on its costs and the barriers it places in the path of worthy projects. “In response to these criticisms, state courts have developed judicial doctrines that evade constitutional debt limitations. . . . In the last twenty years, judicial complicity with state and local officials has freed local governments to increase the number of TIF applications and push it from a ‘fringe’ development finance tool to a mainstream public finance method.”26 Yet the public has not been averse to supporting the issuance of debt for specific purposes. For example, Professors H. Spencer Banzhaf, Wallace Oates, and James Sanchirico studied over 1500 local referenda held between 1998 and 2006 dealing with open space conservation, and found that more than three-quarters of them were approved by voters.27

The legal classification of borrowing secured by taxes on value increments as something other than general obligation debt reflects the larger problem of characterizing and accounting for future liabilities. Legislative and judicial interpretation may have excluded TIF claims on future tax receipts from this category of debt, but the effect on local governments that must deal with reduced future revenues may not be the less constraining for that reason.

The Chicago Example. Chicago presents an important case study of the potential benefits and pitfalls of TIF programs. The city has made use of TIF on an extremely large scale, with Mayor Daley repeatedly calling it “the only game in town.”28 At the same time, its academic community has undertaken major studies of the impact of TIF development, and its investigative journalists have examined the political process of TIF approval and operation in great detail.

The Central Loop TIF, perhaps the nation’s largest, was established in 1984 under Mayor Harold Washington to finance investment in the notoriously hard-to-develop “Block 37,” a parcel bounded by Washington, State, Randolph, and Dearborn Streets. Mayor Washington predicted that the TIF could be closed by 1995. In fact, it was expanded in 1997 to include the area bounded by Wacker Drive, Michigan Avenue, Congress

———

Parkway, and Franklin Street. Before it was terminated in 2008, the TIF brought in over $1 billion in revenue, including $365.5 million in the final year alone. Meanwhile, the development of Block 37 remained unfinished. This experience is not unique. Professor Gordon has written, “Once redevelopment areas are born, they rarely die. For example, Los Angeles officials created the Hoover Redevelopment Project in 1966 to improve the area surrounding the city’s Memorial Coliseum. In 2004, 35 years before the project was due to end in 2039, state lawmakers extended it to 2051 . . . . As a Senate staff analysis noted at the time, ‘[T]he committee may wish to consider why it should [take] Los Angeles officials a century to redevelop the Hoover neighborhood.’”

In 2006 Chicago established a new TIF, LaSalle Central, in the financial district just west of the Central Loop, projected to accumulate more than $2 billion in revenue before it expires in 2029. In 1997, Chicago had 41 TIF districts; in the following four years, it created 86 more. At the beginning of 2009, the city had over $1 billion in TIF funds on hand, compared to an official city budget of $6 billion.

The large number of taxing entities within Cook County gives the city of Chicago a special incentive to appropriate these jurisdictions’ future tax base growth through TIF designation. There can be as many as fifteen overlapping jurisdictions in the city, including the Board of Education, the Chicago Transit Authority, the Chicago Park District, the Community College District, the Health and Hospital Commission, and Cook County itself. Moreover, Illinois legislation allows a municipality special freedom in TIF operation. For example, although “gerrymandering” of TIF districts is not uncommon, Illinois is remarkably lenient in allowing revenue from one TIF district to be spent in another.

Mayor Daley’s support for TIFs as the “only game in town” confronted no significant opposition during his tenure. The institutional factors that diminish oversight, such as lack of transparency and the absence of legal challenges, combined with public approval for new development and successful downtown revitalization, were especially strong in Chicago. Cook County Commissioner Mike Quigley undertook a review of TIF procedures, culminating in a major public report in 2007. None of his recommended reforms was adopted. His proposal to include TIF information on property tax bills failed at a County Board meeting presided over by Finance Chair John Daley, the Mayor’s brother. When Commissioner Quigley addressed Illinois legislators on TIF reform, the

---

29 Tracy Gordon, “A Funny Thing Happened on the Way to the Coliseum...,” note 19, above.
30 Jeremy Thompson, Jason Liechty, and Mike Quigley, A Tale of Two Cities: Reinventing Tax Increment Financing, April 2007, p. iii.
31 Id. at p. 1.
34 Thompson, Liechty, and Quigley, A Tale of Two Cities, note 30, above, at pp. 38-40.
Mayor sent Chicago alderman to rebut his arguments. After Quigley was elected to Congress, no other local official took on the challenge of reforming TIFs in Chicago.

Illinois law requires creation of a Joint Review Board (JRB) composed of representatives of affected jurisdictions and special districts to vote on TIF proposals. But as Commissioner Quigley wrote, “In practice, however, the JRB barely scrutinizes the TIF proposals that come before it, and has never voted one down. With the exception of Cook County, all JRB members are in effect representatives of the mayor of Chicago.”

Similarly, all fifteen members of the Community Development Commission (CDC) charged with oversight of TIF projects are appointed by the Mayor. The CDC has provided almost unanimous approval of city proposals. Of the 812 votes cast by its members between November, 2005 and April, 2007, 808 were affirmative, and no item failed to carry a majority. Commissioner Quigley’s report states, “We have to conclude that the CDC functions as a rubber stamp, exercising little actual oversight. . . . Four commissioners have been present for fewer than half of the votes taken since November 2005. One commissioner whose name has been read during 95 roll calls has been present for just three of them.” Again, this situation is not unique to Chicago. The Maryland Daily Record undertook a detailed examination of “The New East Baltimore” development project, headed by East Baltimore Development Inc. (EBDI). “The Daily Record’s investigation found that The New East Baltimore’s public funding is so complex and poorly scrutinized that local elected officials, some of whom serve on EBDI’s board, said they had little grasp of the $108.5 million in city funds committed to the project. . . .”

Chicago exhibits an extreme degree of the lack of transparency common to TIF programs. Journalists investigating TIFs reported, “Of the 11 aldermen who spoke with us about their TIF meetings, none was allowed to see the entire TIF budget—they were shown the revenues and expenditures planned for their wards alone and asked to sign off.” Commissioner Quigley’s report states, “The near total lack of public information readily available on Chicago’s TIFs is, in a word, inexcusable. . . . Why this should be so is perplexing, but the process one must go through just to get a minimally clear picture of TIF in Chicago requires time and fortitude average citizens simply don’t have.”

Without oversight or opposition, it can be hard to resist the use of TIF revenue for short-term needs. Chicago TIF funds were used for job training and street cleaning because, as

---

37 Thompson, Liechty, and Quigley, A Tale of Two Cities, note 30, above, at p. 15.
38 Id. at p. ii.
39 Id. at pp. 46-47.
42 Thompson, Liechty, and Quigley, A Tale of Two Cities, note 30, above, at pp. 41, 44.
on alderman said, “Streets and San is being shortened every day.” This is particularly ironic, because by 2005 the TIF budget for Chicago was greater than that of the entire Streets and Sanitation and Transportation Department. By 2005, ten percent of all property taxes in Chicago were earmarked for TIF purposes, and TIF districts covered more than one-quarter of the city’s area, causing overlapping entities to lose hundreds of millions of dollars in revenue. Commissioner Quigley’s report estimated that TIF caused a four percent rise in Chicago property taxes, but a flyer distributed by the city’s Department of Planning and Development, “Tax Increment Financing: Myth/Reality,” stated, “Myth: TIF will increase my taxes. Reality: TIF produces more tax revenue by encouraging growth in the neighborhood and expanding the tax base, but it does not change the way your taxes are assessed or change the way you pay taxes.”

**Borrowing from the Future.** Debt finance has an important place in funding long-term capital projects. However, the TIF experience gives dramatic evidence that the ability to spend against future revenues for unspecified purposes with little oversight presents opportunities for excessive borrowing. Chicago’s recent experience has also offered examples of this danger outside the realm of TIF.

In 2004, Mayor Daley decided to lease the Chicago Skyway, a 7.8 mile toll road connecting the western Indiana suburbs with the Dan Ryan Expressway to downtown Chicago. In 2005 a private consortium paid $1.83 billion for a ninety-nine year concession to operate the Skyway and collect its tolls. Political opposition was diminished in part because although the Skyway had been operated as a Chicago municipal department, most of its users were commuters from eastern Illinois suburbs and western Indiana, and not Chicago voters. The proceeds were allocated primarily to repayment of municipal debt and establishment of an $875 reserve fund, with $100 million spent on current outlays.

In 2008 the city sold the rights to collect its parking meter revenue for the next seventy-five years for $1.15 billion, with the avowed intent of putting the proceeds into a long-term reserve fund whose interest would help replace the $20 million in lost annual parking-meter revenue. In fact, nearly all that amount was spent within one year. Mayor Daley had “no qualms about raiding reserves he once called untouchable, in part, to dole out $200 grants to hard-pressed homeowners.” This led one alderman to cast his first “no” vote on a Daley budget in 16 years. “[T]he parking meter money was billed as a ‘perpetual replacement fund’ when the 75-year lease was rammed through the council a year ago. ‘We have breached our fiduciary duty to taxpayers. You can’t break a contract in 12 months that’s supposed to last for 75 years. It’s unconscionable. It’s irresponsible.

---

44 Thompson, Liechty, and Quigley, *A Tale of Two Cities*, note 30, above, at p. ii.
45 *Id.* at pp. 6, 9.
46 *Id.* at pp. i, 48.
It’s disingenuous. – The decision to raid this fundamental asset is mind-boggling.”

The budget approved at the end of 2009 left only $773 million of the combined $3 billion realized from the lease of the Skyway and the sale of parking meter rights.

In 2011, David Brunori wrote in State Tax Notes, “In 2007, I mentioned that the city of Chicago was considering leasing its parking meters. In 2008 it leased the 36,000 parking meters for 75 years for $1 billion. Morgan Stanley later then sold the lease to Abu Dhabi. The emirate has complete control over the city’s parking meters and has ended free parking on holidays.”

The State of Illinois. Chicago’s problematic use of debt is reflected and magnified at the state level. In February, the state of Illinois sold $3.7 billion in bonds to “hedge funds, mutual funds, and non-U.S. buyers” in order to make a legally required payment to its public employee pension plan. The Illinois bond rating is one of the lowest of the fifty states, and these bonds carried an interest rate approximately two percentage points greater than would be required from a private company with a similar bond rating. That same month, Governor Quinn announced plans to issue more than $8 billion in bonds to pay past-due bills, such as amounts owed to state vendors. The Governor said, “This is not, not new borrowing. Billions of dollars of existing bills will not go away by magic.” The past-due bills are already in existence, but the declaration that an $8 billion bond offering is “not, not new borrowing” has a through-the-looking-glass quality.

From the mayor of Sacramento to the governor of Illinois, magic seems to figure heavily in considerations of debt. More than seventy years ago, the philosophy of legal realism sought to demystify judicial decision-making by removing it from the realm of scholasticism, first principles, and natural law. In his enormously influential article, “Transcendental Nonsense and the Functional Approach,” Felix Cohen mocked the idea of “magic ‘solving words’” such as “property rights,” “fair value,” and “due process.” “Legal arguments couched in these terms are necessarily circular, since these terms are themselves creations of law, and such arguments add precisely as much to our knowledge as Molière’s physician’s discovery that opium puts men to sleep because it contains a dormitive principle.” The magic solving words of “debt” and borrowing have been much in evidence in creative finance, including TIF, in recent years.

---

49 Id.
50 Id.
53 Id.
55 “‘When I use a word,’ Humpty Dumpty said, in rather a scornful tone, ‘it means just what I choose it to mean — neither more nor less.’” Lewis Carroll, Through the Looking-Glass, Chapter 6 (1871).
From another perspective, perhaps Governor Quinn can be interpreted as acknowledging that functional, rather than technical, borrowing does not occur when the state undertakes a bond offering, but at an earlier time when it enters an obligation for which it lacks funding. Professors Dye and Merriman term this “implicit borrowing.” They write, “Past choices to implicitly borrow by not putting aside sufficient funds to cover future pension liabilities have made Illinois pension underfunding the worst in the nation.” In this view, debt might include all varieties of payment obligations, whether or not technically subject to legislative and constitutional restrictions and referendum requirements.

After the first generation of tax limitation measures, much spending was supported by borrowing that avoided the magic solving word of “debt.” Leasing parking meters, sale of an expressway, and borrowing secured by taxes on future value increments can avoid classification as debt for specific legal purposes. Unfortunately, the name given to these fiscal instruments does not change the experience of repayment. Motorists paying increased tolls, drivers whose parking fees have quadrupled, taxpayers called upon to honor unfunded pension obligations, or property owners facing higher tax rates because of a frozen tax base do not bear less of a financial burden because what they are repaying is not termed “debt.” If the cycle of tax limitations was followed by a cycle of borrowing that was not classified as debt, the next cycle, that of repayment, will require political, legal, and economic expertise to help local governments through this transition without the aid of magic.

---