TAX INCREMENT FINANCING

Chris Webber, October 2010

Nick Clegg's announcement that Tax Increment Financing (TIF) is to be introduced in England is great news for cities. This note draws on a report the Centre for Cities authored on behalf of the All Party Urban Development Group (APUDG)[1] in 2009 to explain what TIF is and highlight some of the outstanding questions still to be answered.

1. **Tax Increment Financing works by allowing local government to raise money by borrowing against the expected increases in tax revenue associated with a new development.** The possibility of introducing TIF in England has been under discussion for some time (among think-tanks at least) and the idea is often referred to as Accelerated Development Zones (ADZs). Previously it was thought that the idea of introducing TIF in England was a no-go policy because the Treasury wasn't keen. Obviously things have changed.

2. **Lots of analytical work has already been conducted by the Core Cities Group** (with the support of PwC), the British Property Federation and others into the case for trialling TIF schemes. The UK model could involve one or more local authorities having the freedom to retain business rates over and above the existing receipts of the area resulting from new development (as Clegg explained). These rates would be securitised to pay for upfront infrastructure, with the debts repaid over a period of 20 plus years.

3. **There are a number of reasons to be cautious about TIF.** For example:

   - Similar to the US model, local authorities could finance TIF projects using prudential borrowing powers to raise money either in the capital markets or from central government sources. **This could add to public sector debt and pose a risk if the development is delayed, costs overrun or if forecast revenue is unable to cover the debt.**

   - **Our APUDG inquiry also stressed the importance of additionality.** TIF should only be permitted to fund investment that would not otherwise go ahead and must take into account the impact on tax revenues. The evidence presented showed the merit of TIF as a powerful regeneration tool in the US but stressed that the model had been overused because of competition between different local governments.

4. **Rationing TIF to only the most critical property development and regeneration projects would ensure that the tools genuinely stimulate additional investment** that would not otherwise have occurred. The use of TIF would be much less widespread than in the US, and the pitfalls of unmanaged regional competition could be avoided.

5. Key messages on TIF from our APUDG report included:

- TIF has **proved to be a powerful tool in the US in jump-starting regeneration**. TIF could be key to bridging the funding gap in the UK, learning from the experience of US cities and states.
- In implementing TIF, **establishing clear principles with regard to additionality and appropriate strategic oversight will be critical**.
- A **key challenge will be determining the extent to which a new development, facilitated by the use of TIF, generates additional tax revenues** on a national level rather than merely displacing revenues within the UK.
- The most effective way to work out details of implementation would be for national government to **sanction a number of TIF pilots.**

Some outstanding questions:

1. Will local authorities be able to group together (e.g. through local enterprise partnerships) to arrange TIF schemes or will it be limited to single local authorities?

2. How much involvement will national government have in deciding on the spread and scale of TIF schemes? Clegg's speech suggested that such decisions would be up to local authorities, but lessons from the US suggest that strong oversight would be helpful.

3. Will national government guarantee TIF schemes or will they leave it to local authorities? Borrowing will be much more expensive if national government doesn't guarantee the schemes.

4. How (if at all) will decision-makers try to judge whether a TIF scheme is additional?

5. Are the schemes that local authorities want to fund economically valuable in the first place? How many jobs will they actually create? Will local authorities be delivering on a genuine economic need or are they just borrowing in the pursuit of what might be considered unrealistic aspirations?

*1. APUDG (2009) **Regeneration and the recession: unlocking the money**. London: BPF*
Available from www.centreforcities.org/apudg

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