

# **Tax Increment Financing Study & Formulating Committee Report**

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**METROPOLITAN GOVERNMENT OF  
NASHVILLE & DAVIDSON COUNTY**

**May 2019**

***DRAFT***

## Summary

On September 19, 2018, Mayor David Briley signed ordinance BL2018-315 creating a Tax Increment Financing Study and Formulating Committee. The goals of the Committee were to study how the Metropolitan Government utilizes tax increment financing (TIF) and to formulate recommendations for its implementation in a more transparent, equitable, effective, and understandable manner. The committee was asked to look at how tax increment financing is awarded, the strengths and weaknesses of how tax increment financing is currently awarded, whether alternative lawful approaches exist for structuring tax increment financing awards, and whether methods for awarding tax increment financing should be revised following the emergence of transit-oriented redevelopment districts and other developments.

Members of the committee were:

- Mr. Charles Robert Bone
- Dr. Paulette Coleman
- Mr. Brian Kelsey
- Ms. Talia Lomax O'dneal
- Mr. Bert Mathews
- Councilmember Bob Mendes
- Mr. Richard F. Warren

Mr. Bone is an attorney and has served on the Board of the Metropolitan Development and Housing Agency ("MDHA") for the past two and one-half years and currently serves as its chair.

Dr. Coleman is the former chair of the Affordable Housing Task Force for Nashville Organized for Action and Hope ("NOAH") and is trained as an urban planner.

Mr. Kelsey is the Chief Strategy Officer in the Mayor's Office; prior to that he worked in Austin, Texas, focusing on economic development issues including the use of TIF, and teaching courses on those topics.

Ms. Lomax-O'dneal has worked in the city's Finance Department for the past 18 years, serving as Director of that office for the past three years.

Mr. Mathews is active in the real estate business as a broker, owner, and developer of projects, some of which have included TIF loans.

Mr. Mendes serves as an at-large Council member. He is a business lawyer and has been involved with some projects that included TIF.

Mr. Warren has practiced law in Nashville for the past 42 years with much of his practice focused on commercial real estate development, some of which has included projects that received TIF loans.

The committee met 11 times over 6 months to learn more about how Metro and MDHA have used TIF, heard presentations from developers, attorneys, and lenders who had previous experience with TIF in Nashville, transit-oriented development, as well as affordable housing providers and advocates. (For more information and minutes of the meetings, access [Nashville.gov](http://Nashville.gov) and search under Boards and Commissions for Tax Increment Financing Study and Formulating Committee.)

## What is TIF generally?

Tax increment financing (TIF) is a tool originally designed to address “blight” in urban areas but is now used for a variety of economic development or redevelopment purposes in nearly every state. TIF, in practice, can vary by state depending on its enabling legislation, but municipalities are usually the lead administrative entities. Although in some states, counties and redevelopment authorities approve TIF projects.

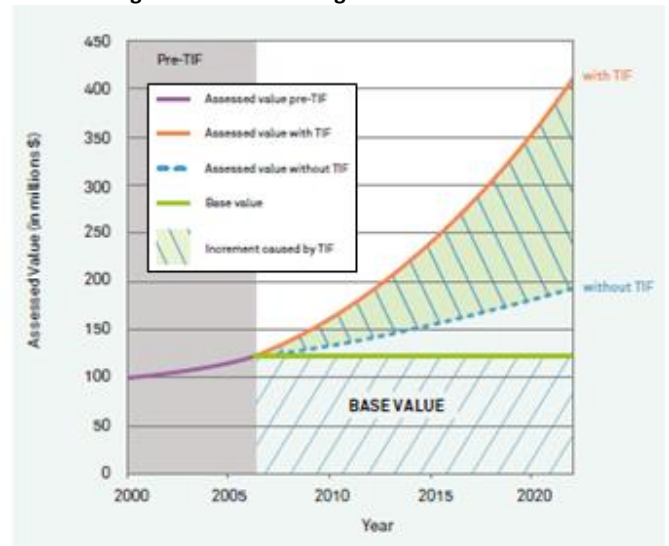
Conceptually, TIF is a pledge of future tax revenue to fund present-day investments. Municipalities use TIF to fund improvements, typically utilities, transportation, or other types of infrastructure, in a designated area, referred to as a zone or a district in most states. These improvements, in turn, are expected to attract private investment, which then raises property values and increases the tax base. The increasing tax revenue in the district, or the “increment,” is used to make debt payments on the financed capital improvements.

In most states, TIF projects are funded through the increase in property tax revenue in the designated area. There are also some states that allow the use of sales tax revenue and other sources of funding, in addition to property taxes. TIF is predicated on the idea that private investment in the designated area would not have occurred “but for” availability of TIF to help fund improvements that make the private investment possible.

Figure 1 illustrates how the increment is calculated, which can vary based on state legislation and local practice. The “base” value is the assessed value of property when a district is created. Cities may assume that the base level remains constant. Alternatively, cities may assume that the base value appreciates over time. In either case, the amount of increment is the difference between the base value (or, alternatively, the appreciated base without TIF) and the future expected value of property after TIF-funded development occurs.

In Tennessee, cities are authorized to calculate the increment as the difference between a constant base value and future expected value with TIF.

Figure 1 Understanding the Increment in TIF<sup>1</sup>



## What are advantages/disadvantages of TIF?

The most significant advantage of TIF in terms of promoting economic development is that, when used appropriately, it does not require a city to assume much risk on behalf of a private entity. Cities or redevelopment agencies may finance a project using the tax increment, but the private entity is responsible for making the debt payments if tax revenues are not high enough to pay the required TIF loan payments.

In Nashville, TIF is non-recourse debt, meaning that the redevelopment agency does not serve as a guarantor for the private entity. If tax revenue on the increment is too low to pay TIF loan payments, then the private entity must make up the difference. If the private entity is not able to pay the difference or goes bankrupt, then the lender cannot make the city pay.

One disadvantage of TIF is that it is difficult to know for certain what might happen “but for” availability of TIF, especially in areas that are already experiencing tax base growth. There is also research showing that TIF may use revenue that might otherwise be used for other government purposes, and that TIF can sometimes make transactions less transparent.

<sup>1</sup> Source: Merriman, David. *Improving Tax Increment Financing (TIF) for Economic Development*, Lincoln Institute of Land Policy (2018), p. 7.

## How is TIF used in Nashville now?

TIF loans in Nashville are approved by the Metropolitan Housing and Housing Agency (MDHA) or the Industrial Development Board (IDB). Because the IDB has only ever approved one TIF loan, this report focuses mainly on TIF loans awarded by MDHA.

MDHA has written policies for how to apply for a TIF loan in an economic redevelopment district. There are also unwritten practices. As the city considers using TIF in Transit-Oriented Redevelopment Districts (TORD), unless other decisions are made, the present approach would be to have the same policies and practices apply in TORDs.

### *Economic redevelopment districts*

Since TIF was first used in Nashville in the 1980s, all but one TIF loan in Nashville has been in an MDHA economic redevelopment district. Typically, to create a district, the mayor asks MDHA to prepare a written economic redevelopment plan for a certain geographic area. MDHA's board and the Metro Council must approve the district before TIF loans can be approved.

In all of the current redevelopment districts, only MDHA may initiate an amendment to the plan terms. Any amendment proposed by MDHA is subject to Council approval. No Council approval is required for any TIF loan. Each current district started with a 30 year term. No district has ever expired. MDHA and the Council have instead extended the length of plans.

The one TIF loan outside of a redevelopment district involved the IDB and a shopping mall redevelopment project in Bellevue.

### *Policies and practices in making new TIF loans*

MDHA has a TIF loan application form available online. At the time of this report, MDHA also had two partially outdated documents online – "TIF Policy" and "TIF Priorities." However, there are other unwritten practices that are relevant in applying for a TIF loan.

For example, MDHA acknowledges that very few TIF recipients have ever been "walk-ins" who simply applied according to the directions available online. More frequently, a developer will first contact the mayor's office. Sometimes, a developer will contact one of several people at MDHA as a first step. While the mayor is not a part of MDHA's governance structure or formal decision-making process, the committee believes that no major TIF loan has ever been awarded in Nashville without the active support of the mayor's office. While these practices appear to be commonly known by parts of Nashville's development community, they are not formal policies and there are legitimate questions about whether every developer has equal practical access to obtain a TIF loan.

Once a TIF loan application is submitted and been reviewed administratively by MDHA's staff, MDHA's board has the legal power to approve the TIF loan. However, while the mayor has no formal authority to reject a TIF loan application, the committee does not believe MDHA has ever approved a TIF loan over the objection of the mayor's office. No Council approval is required for TIF loans. The committee is not aware of any informal process that would allow the Council as a body to reject or block a TIF loan application.

### *Same rules to apply to TORDs*

In 2017, the State enacted legislation that would allow TIF to be used to help develop high-capacity transit corridors. The State legislation permits TIF loans in a TORD to finance transit stations and related infrastructure and affordable housing.

There was an attempt in 2018 to create a Donelson TORD. The legislation did not pass in the Council. The proposed Donelson TORD would have been different than Nashville's existing economic redevelopment districts in one important way. While TIF loans in economic redevelopment districts are supported by the tax increment from a single property or a small number of properties, the Donelson TORD would have collected the tax increment from every property in an entire 145-acre district.

Aside from this important distinction, the proposed Donelson TORD would have used the same written policies and unwritten practices as in economic redevelopment districts.

### **What challenges exist with TIF in Nashville?**

The committee believes that TIF is not inherently good or bad. Over the last generation, downtown, SoBro, and the Gulch have been transformed. There is widespread agreement that TIF has been an important tool in making this happen. However, once an area has been transformed, it is often difficult to remember how much the investment was needed at the start. There are many questions about how to measure the impact of TIF, whether to continue using TIF in and around downtown, and how TIF should be used and administered in the future.

The committee has discussed many factors that should be considered and balanced.

#### *Public benefit*

The most important first question is, "What is the public benefit being achieved with a TIF loan?" The committee learned that the goals of a district change over time. For Nashville's economic redevelopment districts, the initial primary goal was to upgrade blighted areas. As each district matures, at different times, the primary goal in any district may shift to affordable housing or improving infrastructure.

The committee acknowledges that MDHA typically works with the mayor's office to adjust goals over time. But, because districts have a 30 or more year life span, it is a challenge to incorporate input from the public or the Council into the goals for the districts as they change over time.

#### *Public education and accountability*

TIF is complex. Many people confuse economic development policy generally with TIF. To be clear, TIF is just one tool for economic development. Under state law, TIF may only be used in certain circumstances to pay for certain types of project costs. The committee found that TIF is not well understood in Nashville. Much greater education

efforts are necessary to help the public understand how to put the tool of TIF in context with broader economic development policy in Nashville.

It also is a struggle to provide meaningful, concise reporting to the public about TIF projects in Nashville. Providing up-to-date, complete, useful information may continue to be a challenge for the city.

If Nashville were to succeed in providing a more complete picture, the city would be able to have a common frame-of-reference for celebrating TIF successes and determining areas where improvement is needed.

#### *Percent of tax increment used for a TIF loan*

In Tennessee, the tax increment available to service TIF loans includes all of the tax revenue greater than the original base value. However, in 2016, Nashville passed an ordinance requiring that the city must retain the "debt services" portion of the tax increment from new TIF projects. Currently, that is about 15% of the new property taxes on a TIF property. Other than this ordinance, there is no written policy describing what percent of the tax increment may be pledged to support a TIF loan.

MDHA generally prefers to use all available tax increment so that the TIF loan can be paid back as quickly as possible. Other cities establish a cap on the percent to be used to pay loans in order to retain some new revenue to pay for basic government services. For example, the city of Chattanooga generally allocates a maximum of 75% of the tax increment for TIF loans having a term of 10 years or less and 60% of the tax increment loans for longer than 10 years. This is a policy question that should be addressed in Nashville.

#### *Budget predictability*

Metro Finance has identified that as the amount of tax increment being used to pay TIF loans has increased in recent years, it has been more difficult for Metro Finance to accurately plan the city's operating budget. Even while the committee has been doing its work in early 2019, MDHA and Metro Finance have begun to collaborate on how to more accurately project the tax increment

dedicated to TIF loans several years in advance. This should continue.

This issue impacts more than Metro Finance's planning. Especially for large departments like Metro Nashville Public Schools (MNPS), the current lack of predictability can have an impact of more than \$1 million per year on a department's budget.

#### *Consider all perspectives*

In addition to the public's interest and budget predictability issues, there are several other perspectives that must be balanced for TIF to work well.

Developers: The committee found that the development community sees a variety of challenges in trying to use TIF.

Some developers report that TIF is difficult to obtain. For example, a project must be located in a redevelopment district. Working through the mayor's office and MDHA, and a TIF lender, can be time-consuming and costly. Often, the city will force a developer to improve public infrastructure in the area immediately around a project. All of these in turn can add costs that cut into the value of any TIF that may be awarded.

Other developers complain about being left out of Nashville's TIF program, or that they do not know how to obtain a TIF loan, or that they have never been successful in getting a TIF loan.

The committee concludes that the complexity and costs of TIF loans makes TIF more difficult to use in smaller projects and in the more economically challenged redevelopment districts. These challenges may also explain why the group of developers whose projects have received TIF loans do not fully reflect Nashville's diversity.

Lenders: A bank typically requires one or more people to sign a personal guaranty to ensure payment of a TIF loan. Nearly all TIF loans in Nashville have been successfully repaid using tax increment funds. This is not the experience everywhere and, if a project were to falter, a lender wants to have personal guaranties from the developer to ensure that the loan is paid.

Since TIF projects usually are high dollar investments, a lender's requirement for personal guaranties limits the pool of possible developers that could qualify for a TIF loan. The committee sees this as a challenge to broadening the group of developers who can use TIF.

MDHA: MDHA wants to serve Nashville and do the best job possible in accomplishing its twin goals of housing and development. In doing this, MDHA must comply with federal, state, and local laws and regulations. While MDHA is sometimes criticized for a perceived lack of transparency, its executive and board leadership have expressed an interest in improving this perception.

Since the committee was formed, MDHA already has taken important steps toward increased transparency, including making additional board materials available online, and agreeing to have board members complete an annual Metro conflict of interest disclosure form. Among other things, the annual disclosure will identify any direct or indirect ownership interest in Davidson County real estate.

MDHA's staff is professional and hard-working. However, there are not any staff members that are dedicated exclusively to administering the TIF program. Additional resources may be necessary, especially if Nashville begins to use TIF for transit-oriented development.

#### *Affordable housing*

There is a great deal of confusion in the community about whether TIF may be used to pay for affordable housing.

Under state law, in economic redevelopment districts, TIF loan proceeds may not pay for the bricks and mortar of any housing units. However, TIF loan proceeds may be used to pay for land costs, infrastructure improvements, and parking garages related to housing units. To comply with state law, when a TIF project includes housing, MDHA is required to confirm that no TIF loan proceeds are used to build the housing units.

With TORDs, state law is different and allows TIF loan proceeds to be used to pay directly for the construction of affordable housing units.

At the time of this report, there is no written strategy or policy in Nashville about when or how to use TIF on affordable housing projects. There is no written strategy or policy about how to help affordable housing developers pair TIF with other available affordable housing financing tools. Market conditions and funding programs shift over time. These issues will continue to be a challenge for Nashville.

#### *Transit-oriented development*

TORDs pose different challenges than traditional economic redevelopment districts.

The Donelson TORD that was proposed in 2018 would have collected the tax increment from an

entire 145-acre district. Nashville has never done that before, and there are unresolved questions about how to project the future tax increment from an entire district. There are also unresolved questions about who should prepare the projections, and about what percent of the tax increment is appropriate to use in a TORD.

#### *TIF through the Industrial Development Board*

The committee is aware of only one TIF loan approved by the IDB. The committee encourages the IDB to review the committee's work and evaluate what opportunities it might have to align any future TIF loans with the principles and recommendations in this report.

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## Observations and Recommendations

Throughout the process, the committee collected its observations which became the foundation for identifying the committee's recommendations. Those observations were:

### **Observation #1**

Many in the community lack full information about the laws, processes, and results of TIF as used in Nashville. We are lacking a "common set of facts" about how TIF has been used in Nashville and what the impacts have been, which detracts from the quality of public debate about it.

### **Observation #2**

State law limits how TIF may be used. State law creates different sets of rules for how TIF may be used in an economic redevelopment district, a transit-oriented redevelopment district, or by an industrial development board. These varying restrictions contribute to the complexity and lack of understanding of TIF.

### **Observation #3**

The goals of each redevelopment district are unclear. State law requires that the purpose must be to address blight. However "infrastructure" and "affordable housing" are frequently cited as the actual goals of certain districts.

### **Observation #4**

The city's goals for a redevelopment district may shift before the 30-year term of a redevelopment district is complete.

### **Observation #5**

Certain aspects of the TIF and redevelopment districts work seem inefficient and Nashville does not take advantage of all of Metro's capacities.

### **Observation #6**

There is inadequate collaboration between MDHA and Metro Finance to analyze and predict the impact of TIF on future Metro operating budgets.

### **Observation #7**

There is a perception that TIF is available for "insiders" only and not everyone has equal access

to the tool. The complexity and costs of obtaining a TIF loan create barriers for some developers.

### **Observation #8**

MDHA requires that each TIF recipient set a goal to award at least 20% of the total dollars contracted for the project to diversified business enterprises. Most recently, MDHA measured the average participation rate at 14%.

### **Observation #9**

The economics of parcel-by-parcel TIF and entire-district TIF are different and should be treated differently.

### **Observation #10**

In Nashville, TIF projects typically use all of the increment generated for loan payments until the debt is retired and the full value of the development returns to the tax roll. But other cities take different approaches to determining that allocation depending on factors such as size or term of a loan, location, and public benefits.

### **Observation #11**

There is currently no agreed upon methodology to assess the impact of TIF or redevelopment districts.

### **Observation #12**

Other cities apparently use TIF through industrial development boards more than Nashville. This is not well understood in Nashville. TIF through an IDB does not require a redevelopment district or a finding of "blight".

### **Observation #13**

Enhanced opportunities for public review of and comment on proposed TIF projects will strengthen confidence in how the tool is used in Nashville.



## Recommendations

The following recommendations were generated and agreed upon by the entire committee. They are organized into three areas of work: Transparency, Communication, and Education; Policy and Process; and Accountability and Roles. Overarching all these recommendations is the committee's desire for transparency in how the city approaches TIF to ensure a good understanding by all interested parties.

### Transparency, Communication, and Education

1. Create a single portal for information regarding this study group's work, including an interactive map with information on redevelopment districts and TIF projects.
2. Work with key stakeholders and community groups to hold periodic "TIF 101" education to increase understanding of how TIF is used and to diversify the pool of applicants to achieve greater representativeness of the community.
3. MDHA to post on-line all board agendas, full board materials and minutes related to TIF activities.
4. Improve the format of TIF reporting and add diversified business enterprise goals and participation rates for TIF projects.
5. Utilizing the model of the Metro Human Relations Commission's Affordable Housing Booklets, create similar resources to explain how TIF works and make them available.

### Policy and Process

6. In the absence of a well-resourced and fully staffed Department of Economic and Community Development, designate the Mayor's Office of Economic and Community Development to receive all applications for all economic incentives rather than having multiple points of entry.
7. Explore ways to lower barriers of entry for smaller TIF loans with form documents and lower cost of borrowing. Subject to further analysis, examples may include the possibility of a governmental entity acting as a guarantor and/or establishing a program to reduce the transaction costs for smaller TIF loans.
8. Evaluate a tool or program that would reduce or eliminate barriers in redevelopment districts where TIF is rarely considered and/or with smaller projects.
9. After sufficient experience with the Do Better Bill, as amended (Ordinance BL2017-983), determine application to TIF projects.
10. The Metro Council and MDHA to amend redevelopment plans to establish 75% as the standard percent of tax increment to be used for TIF loans subject to written criteria for increasing or decreasing the percentage for a particular loan.<sup>2</sup>
11. MDHA and Metro Finance to create a methodology to complete a fiscal impact analysis for individual TIF loans exceeding an agreed upon threshold. The Committee suggests three million dollars.
12. The Metro Council and MDHA to amend redevelopment district plans to require a periodic assessment of the impact and goals of each district, and to require that the Council and MDHA must agree in order for new TIF loans to continue being made in the district after the assessment. The periodic assessment

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<sup>2</sup> Our entire committee agrees with this recommendation generally. However, we had a split vote (4-2) to choose "75%" instead of "70%." The committee has adopted everything else in this report unanimously.

may be requested by the Council or MDHA any time after 7 years, but must take place at least every 10 years.

13. The Metro Council and MDHA to amend redevelopment district plans to allow either the Council or MDHA to propose plan amendments, subject to the approval of the other.
14. Create a consensus methodology by Metro and MDHA for the creation of a district.
15. Metro and MDHA to work together to improve and streamline the design review process.
16. Encourage the IDB to review the work of this study group and evaluate TIF collaboration opportunities

### **Accountability and Roles**

17. Establish the following commitments to ensure easy access to information and materials:
  - a. MDHA is the primary party responsible for creating the TIF “portal” with the interactive map, with assistance from the Mayor’s Office and Metro ITS, if necessary. The committee’s document library on Sharepoint will be migrated to the portal.
  - b. No later than October 31, 2019, MDHA, the Mayor's Office, and Metro Finance shall provide the Council with a written description of which agencies or departments have been assigned the task of accomplishing each of the recommendations in this report, including estimates of the resources required to complete implementation.
  - c. No later than December 15, 2020, MDHA, the Mayor's Office, and Metro Finance shall provide the Council with a written report describing the status of accomplishing each of the recommendations in this report.