

## WHAT IS TAX INCREMENT FINANCING?

### Questions and Answers About TIF

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1. Q: What is tax increment financing?  
A: Tax increment financing is a method of reallocating property tax revenues which are produced as a result of an increase in taxable valuation above a "base valuation" figure within a tax increment area. Until the tax increment debt within an area has been repaid, tax revenues produced by property tax levies imposed on the increased taxable valuation by a city, county, school district, area school or any other taxing jurisdiction are all allocated back to the city or county which has established the tax increment area, and must be spent by that jurisdiction for projects within that area.
2. Q: What is the statutory authority for tax increment financing?  
A: Chapter 403 of the Code of Iowa, the Urban Renewal Law. Major amendments to Chapter 403 were enacted in 1994 which changed many tax increment requirements as of January 1, 1995. Most of these are discussed below, along with later amendments which made it more possible for cities and counties to use tax increment revenues to finance public improvements related to private housing development.
3. Q: Which jurisdictions may create tax increment financing areas?  
A: Both cities and counties may exercise general tax increment powers.
4. Q: Why do cities or counties create tax increment financing areas?  
A: Tax increment financing areas are created as a means to maximize property tax dollars within particular areas, in order to pay the cost of public improvement projects (streets, water, sewer, etc.) or to make direct economic development grants or loans to private enterprise as an incentive to locate within the tax increment financing area. The funds must be spent within the area and may not be used by cities or counties to supplement their general operations.
5. Q: What is the difference between tax abatement and tax increment financing?  
A: Property tax abatement (authorized by both Chapter 404 and Chapter 427B of the Code of Iowa) provides an incentive for property owners to make improvements to property by exempting the resulting increase in valuation from property taxation for a period of time. The new valuation is "abated" and is, therefore, not subject to tax. Under tax increment financing, all increases in value are subject to the total consolidated property tax levies of all local taxing jurisdictions, but those revenues which are produced from the increased (or incremental) valuation are allocated back to the city or county which has established the tax increment area, and those revenues must be spent for projects within the tax increment area.

6. Q: May cities or counties have both tax abatement and tax increment areas?
- A.: Yes, but, as explained above, the concepts are basically contrary to each other and should be combined only after careful planning and consideration. For example, it will be difficult to repay tax increment debt if all the potential incremental value has been abated.
7. Q: What is the process for establishing an urban renewal/tax increment financing area and obtaining TIF revenues?
- A:
- a. identify the boundaries or legal description of the proposed area
  - b. determine if the conditions in the area qualify the area to be designated a "slum," "blighted" or "economic development" area, as defined in Chapter 403
  - c. prepare an urban renewal plan outlining objectives to be accomplished within the area
  - d. set a date for a public hearing by the City Council or Board or Supervisors
  - e. refer plan to the local plan and zoning commission for review
  - f. send a copy of the plan and the notice of hearing to each of the other affected taxing entities (counties, local schools and area colleges) and schedule a date and time for a "consultation session" with those other affected taxing entities
  - g. hold public hearing
  - h. adopt resolution approving urban renewal plan
  - i. adopt ordinance designating tax increment area
  - j. incur debt (see question 15)
  - k. file annual TIF debt certification with county auditor
8. Q: Must a city or a county receive permission from any other governmental entity before establishing a tax increment area?
- A: No, under most circumstances. However, a city must receive permission from a county in order to include property in a city tax increment area which is located up to two miles outside its city limits, and a county must receive permission from a city in order to include property in a county tax increment area which is located within two miles of a city's boundaries. In addition, a city or county is required to notify other taxing jurisdictions of its intent to create or amend a tax increment area and to give those jurisdictions an opportunity to comment on a proposed tax increment plan (see 7f above). There is no sign-off required by any State agency for the establishment of a tax increment area.
9. Q: Are there any restrictions on types of property that may be included in an urban renewal area?
- A: No, any category of real property may be included in an urban renewal area, but owners of agricultural land, as defined in Section 403.17 of the Code of Iowa, must give specific permission before that land may be made part of a city or county urban renewal area.
10. Q: What is the "base valuation" date for a tax increment area?
- A: The "base valuation" date is the starting point from which incremental value is calculated. For tax increment areas created prior to January 1, 1995, the base valuation date is January 1 of the calendar year prior to the year in which the tax increment designation ordinance was adopted. For plans approved after January 1, 1995, the base valuation date is January 1 of the calendar year prior to the year in which tax increment debt is first certified to the county auditor.
11. Q: What is the formula for determining the amount of incremental value which exists within a tax increment area?

- A. Incremental values are determined each year by subtracting the taxable valuation which existed on the base valuation date from the taxable valuation on the most recent tax roll. That difference is the incremental value.
12. Q: How are annual tax increment revenues determined?
- A: The amount of incremental valuation is multiplied by the consolidated property tax levy (city, county, school district, area college). The revenues produced from local debt service levies must be subtracted, because these are returned to each taxing jurisdiction in order to pay outstanding general obligation debt, and these revenues do not become part of the tax increment revenues. In addition, regular and voter-approved school physical plant and equipment (PPEL) levies are also subtracted and do not become part of the TIF revenues. The remaining revenues are allocated to the city or county which has established the tax increment area.
13. Q: What are the time limits on the collection and use of tax increment revenues?
- A: For all tax increment areas established prior to January 1, 1995, and for areas established after January 1, 1995, based on a finding of slum or blight, there is no statutory limit on the period of time for which the revenues may be collected and used. For areas established after January 1, 1995, based on a designation of economic development, tax increment revenues may be collected for no more than twenty years. For housing projects in economic development areas, there is a basic ten year limit, which may be increased to fifteen years (see next question).
14. Q: What are the restrictions on the use of tax increment financing to assist in the development of new housing?
- A: For tax increment areas established on a finding of slum or blight (see Question 7 above), there are no restrictions. With some minor exceptions, for tax increment areas established on an economic development finding, tax increment revenues may be used to finance the cost of public improvements related to housing, without regard to the cost of the homes or the income levels of the ultimate owners. However, an amount of funds equal to a certain percentage of the tax increment revenues that benefit a project must be used by the city or county to provide assistance related to housing for families whose incomes do not exceed 80% of the median income in the county. These funds for low and moderate assistance are not restricted to being spent inside the tax increment area but may be spent anywhere in the city or county. For cities or counties above 15,000 population, tax increment revenues from these projects may not be collected for more than ten years. For cities or counties under 15,000 population, collection may be possible for fifteen years, if all other affected taxing entities agree to the extension of time.
15. Q: How can tax increment projects be financed?
- A: Various types of debt are possible, including general obligation debt, pure tax increment revenue debt, internal loans between governmental funds and “rebate agreements”, in which all or a portion of annual tax increment revenues are paid back to developers. Rebate agreements are particularly useful for residential developments.
16. Q: Does debt payable from incremental taxes count against a city’s or county’s constitutional debt limit?
- A: Yes, it does. While Section 403.9 of the Code of Iowa contains language which states that such debt does not count against a constitutional debt limit, the Iowa Supreme Court ruled in 1975 that tax increment debt must be counted against a city’s or county’s constitutional debt limitation. However, if an “annual appropriation” clause is included in a bond issuance resolution or a rebate agreement, only annual payment amounts must be counted against a constitutional debt limit.

17. Q: How does tax increment financing affect local school districts?
- A: First, all debt service tax levies, as well as regular and voter-approved physical plant and equipment (PPEL) tax levies, are “protected,” which means that funds produced from those levies go to the school district and do not become tax increment revenues. Second, because of the state foundation aid program that funds a portion of each local school district’s general operating budget, only school districts that have significant general fund tax levies above \$5.40 per \$1,000 of valuation are likely to be seriously affected by a city or county tax increment financing district.
18. Q: May urban renewal/tax increment areas be expanded or combined with other areas, and, if so, what are the implications for the original area?
- A: New property may be added to existing urban renewal/tax increment areas, and separate areas may be combined or consolidated. It is not necessary that the new property be contiguous to the existing urban renewal area. The same process must be followed as that for creating the original area, including hearing and consultation session with other taxing entities. The areas which are added will be subject to the statutory rules in effect on the date that they are added, but the original district will not be affected. The property which is added will probably have a different base valuation date than the base valuation date for the original district.
19. Q: If a city or county has several separate urban renewal areas, may funds from any area be spent in any other area?
- A: Assuming that tax increment areas have not been combined or consolidated, as discussed above, and that the city or county wants its urban renewal areas to remain legally separate, funds must be spent within the boundaries of the urban renewal area from which they are derived, and, if there is more than one urban renewal area, the funds from one area may not be spent within another area.
20. Q: Is interest on tax increment debt exempt from federal or state income taxes?
- A: Depending upon the purposes for which the funds are expended, interest income on tax increment debt may be exempt from federal income taxation, as well as from state income taxation. If funds are used to make an economic development loan and/or if security is provided by a private enterprise, in the form of, for example, a minimum assessment agreement, or if TIF funds are not used for public improvements, the interest income may not be exempt from federal taxation, but it may still qualify for state tax exemption.
21. Q: May cities establish tax increment areas outside their city limits?
- A: Cities may include property located up to two miles outside their city limits in tax increment areas, but only after obtaining the consent of the County Board of Supervisors and any owners of agricultural land.
22. Q: What are the limitations on the establishment of county tax increment areas?
- A: County boards of supervisors may establish tax increment areas for projects in any area which is at least two miles outside the city limits of any city. In addition, with the agreement of a city council, a county board of supervisors may also establish a tax increment area within two miles of the city limits of a city, or inside the city.