3
TAX INCREMENT FINANCING STRATEGY FOR YORK REGION

The Finance and Administration Committee recommends:

1. **the presentation from Ed Hankins, Director of Policy, Risk and Treasury, be received;**
2. **the recommendations contained in the following report, March 21, 2005, from the Commissioner of Finance, be adopted; and**
3. **the Regional Chair be authorized to write to the Minister of Finance after the Committee meeting outlining the Committee's recommendations and requesting the Province to take them into account in its current budget deliberations.**

1. RECOMMENDATIONS

It is recommended that:

1. Council endorse the concept of tax increment financing as a viable fiscal tool for supporting specific growth related development activities.

2. Council request that the Province introduce legislation to create tax increment financing as a fiscal tool for municipalities.

3. Staff be directed to prepare a further report outlining a more detailed strategy for using tax increment financing to support activities consistent with the Region's intensification strategy.

2. PURPOSE

The purpose of this report is to provide an overview of tax incremental financing (TIF) as a viable tool to help support the funding and/or financing by municipalities of certain types of large scale capital infrastructure projects such as Rapid Transit.

3. BACKGROUND

Tax increment financing (TIF) is a tax policy tool that has been used extensively in the United States. While TIF is not currently permitted by legislation in Ontario, in the provincial document *"Places to Grow—A Discussion Paper*, *Summer 2004—Better Choices. Brighter Future."* (Ministry of Public Infrastructure Renewal, 2004), tax increment financing is presented as a possible fiscal tool to support municipal growth plans. The use of TIF has already been identified as a potentially valuable financing tool to assist in the funding of York Region initiatives such as the Transit Oriented

Development associated with York Region Rapid Transit Plan. The Town of Markham has also stated its support for the use of TIF in its submission to the Province with respect to the Markham Centre project.

Tax increment financing refers to the use of incremental taxes to help fund the cost of specific development activities. In a municipal setting, when a property is rehabilitated or enhanced through a new activity, the value of the property will increase with a corresponding increase in realty taxes above a pre-development baseline. Normally this increment in realty tax would be shared proportionately by the lower-tier and upper-tier municipalities as well as with the school boards. In tax increment financing, some or all of this tax increment would be used to support the specific development activities.

TIF is used in some 45 US states for a variety of economic and social purposes (*"Municipal Financial Tools for Planning and Development"*, Ministry of Municipal Affairs and Housing, 2000). State legislation allows municipalities to create a TIF district and then to divert the tax increment to a TIF authority for a broad range of permissible development activities.

3.1 Current Legislation

Current legislation focuses on developer based activities as part of a Community Improvement Plan (CIP) under the *Planning Act* or the remediation and development of brownfields property under the *Municipal Act, 2001* (the Act).

Subsection 106(1) of the Act prohibits a municipality from directly or indirectly assisting any manufacturing or other commercial or industrial enterprise through the granting of bonuses for that purpose. These bonuses include, but are not limited to, grants, loans, guarantees, leasing or selling property below market value, and exemptions from any levy, charge or fee.

However, Subsection 106(1) does not apply to a CIP as defined by Section 28 of the *Planning Act* or the brownfields provision of Section 365.1 of the Act. A municipality may use Subsection 28(7) to provide grants or loans to registered or assessed owners or tenants of lands or buildings within the designated CIP area. An upper-tier municipality may also participate in supporting a CIP initiated by a lower-tier municipality but there is no provincial assistance.

The brownfields rehabilitation provision under Section 365.1 of the Act allows for tax assistance for the rehabilitation and development of eligible properties, what may be termed blighted lands. A municipality may provide brownfields "tax assistance", in essence tax relief, through the cancellation of taxes on a property during a rehabilitation period and a development period. Alternatively, a by-law may be passed to limit tax increases during the rehabilitation period and the development period. This tax relief may be matched by the Province (with the approval of the Minister) through the cancellation (or the foregoing of increases) of education taxes in a similar manner as provided for the municipal property taxes.

The simplest form of financial assistance that can be offered is to cancel the taxes or future tax increments on redeveloped property to the benefit of the developer. This could be a set percentage of the increment for a specified period such as 80% for 10 years or on a declining basis e.g. 100% in the first year declining by 10% for each subsequent year. This is a model proposed under the brownfields provision of the Act; however, as discussed previously, the Act limits the application of this tax relief to environmental rehabilitation projects.

As indicated previously, tax increment financing does not formally exist in Ontario. However, recently the Minister of Public Infrastructure Renewal, David Caplan, had requested that Minister Sorbara include tax increment financing in his upcoming spring budget.

3.1.1 Limitations of Current Legislation

York Region has only a limited number of brownfields properties; however, fiscal tools are required to better address the development of "greyfields" (former and underused retail property), the creation of transit infrastructure, and the enhancement of urban centres as contemplated in the Region's centres and corridors planning strategy. One initiative of great importance to York Region is the York Region Rapid Transit Plan, which will require a large capital commitment but may not necessarily generate a profit, making it difficult to attract significant private sector investment. Tools such as TIF could aid municipalities in financing these types of large scale infrastructure developments.

3.2 Request from the Town of Markham

On February 3, 2005, Finance and Administration Committee received correspondence from the Town of Markham regarding a submission that its council had endorsed pertaining to Financial Tools to Implement Markham Centre. The Town requested that the Province take the necessary action to introduce tax increment financing and to permanently remove tax capping within TIF zones. Markham has identified TIF as a valuable tool to support the Markham Centre project and foresees the use of TIF to finance parking structures in the early stages of the proposed project.

3.3 Actions to Date

On October 17, 2002, Council adopted Report No. 7, Clause 1 of the Finance and Administration Committee in respect to the report "Update on Fiscal Policy and Growth Management in York Region." This joint report of the Commissioner of Finance, Commissioner of Planning and Development Services, and the Commissioner of Transportation and Works references the use of tax increment financing as one of a number of fiscal tools to support the development objectives of the Region.

The York Region Rapid Transit Business Plan, October 2002, makes reference to the potential use of TIF as a financing tool to support infrastructure development for bus rapid transit.

The Town of Markham has made submissions to the Province, the Ministries of Public Infrastructure Renewal, Municipal Affairs and Housing, and Finance, requesting provincial consideration of five new financial tools required to help finance future public infrastructure investments in Markham Centre.

Similarly, since September 2004, staff from York Region, York Region Rapid Transit Corporation and its partner YC2002 has made presentations to the Ministry of Transportation, the Ministry of Public Infrastructure Renewal, and the Ministry of Finance on the possible use of TIF for transit infrastructure. The Province was requested to endorse TIF for major projects such as the transit system to serve as an alternative mechanism to provide incentives for the advancement of the Region's planned urban infrastructure initiatives directly related to and depended on the rapid transit system.

3.4 ROPA 43—Regional Centres and Regional Corridors

The Regional Official Plan, as Amended by ROPA No. 43 adopted by Council (in effect January 7, 2005), calls for innovative approaches to advance the implementation of the Region's planned urban structure of Regional centres linked Regional corridors, served by rapid transit. The plan calls for the creation of implementation strategies to encourage development and infrastructure investment in Regional centres. Implementation tools listed in this section include tax increment financing.

4. ANALYSIS AND OPTIONS

The value of tax increment financing comes from the partnership of the lower-tier and upper-tier municipalities and the Province. A rapidly growing region requires a substantial commitment to infrastructure development with a number of projects competing for limited capital. The financing burden for the Region alone is too great; a partnership is needed to finance the infrastructure required within an appropriate timeframe.

Growth in incremental taxation does not provide the total solution to financing municipal infrastructure; rather, it is one of a suite of tools that should be made available to municipalities to assist in funding infrastructure projects.

4.1 The TIF Process

The first action required for tax increment financing is to assess the current property taxes (the base before development) being paid in the development area or zone. This may be simple for a small development or complex for a large scale TIF zone. This baseline tax is usually protected in that it continues to move to the taxing authorities, in York's case, the lower-tier and upper-tier municipalities and the Province. The incremental future taxes are then estimated based on the nature and timing of the development process: this is the "tax increment" that is the basis for the financing process.

To use the YRTP as an example, the base property tax revenue is determined in the transit corridors. The value enhancement of the property and the attendant increment in tax revenue is estimated. The base tax revenue continues to the taxing authorities as it always has; it is possible to have a revenue escalator to recognize the normal development that would have occurred in the corridor. The tax increment above the base (and possible escalator) is used to fund the infrastructure development.

The construction of dedicated transit infrastructure is required early in the process and therefore much of the capital cost is front-ended. To fund the capital required, the Region would have to issue debt. It is easier to issue the debt if a municipal and provincial partnership is working together by channelling the tax increment or “uplift” to the repayment of the debt.

It is also necessary to establish a time period for the TIF mechanism. For infrastructure, this could well be 20 to 30 years whereas the current brownfields legislation contemplates a much shorter period of time. At the end of the TIF period, the tax revenue reverts to the normal proportionate distribution between the partners, that is, the upper-tier and lower-tier and education portions. It is assumed that this revenue will be substantially greater than would have been anticipated if the TIF related project had not been undertaken.

4.2 Strategies for the Application of TIF to the Needs of York Region

4.2.1 TIF for Transit Oriented Development

Transit Oriented Development is development that is in proximity and related to transit stations served by high quality, high performance transit. The Rapid Transit plan is a particular application of TOD. The Rapid Transit 10-year capital plan indicates a capital financing requirement of $2.2 billion. Of this, $631.5 million or approximately one-third would have to be provided by the Region through the issue of debt. In the past the Province has provided 70-80% of transit capital; the Rapid Transit plan proposes a one-third share for each of the Federal, Provincial and Region levels of government, the same share as for the current Quick Start program.

Studies in US metropolitan areas have shown substantial value enhancements of 10-25% occurring in corridors where transit lines were introduced, including a finding of 25% by the American Public Transit Association. The Sheppard Avenue corridor in North York is an example of redevelopment following the extension of the subway. It is realistic to expect that value enhancements could be achieved in the YRTP service corridors of an order appropriate to TIF type funding.

4.2.2 Implementing TIF to Accelerate Development

For a broader infrastructure application such as the YRTP, the bulk of the costs are incurred early in the project to create or accelerate the development. Thus, a method is needed to finance the front-end costs on a timely basis. However, using direct charges such as property tax, special area levies and development charges has been shown in studies to be detrimental to planning objectives such as the intensification of development. Tax increment financing is transparent to the taxpayer because it represents the taxes that would normally be paid on the property. TIF is not an additional property tax or special area levy.

4.2.3 Implementing Front-End Financing

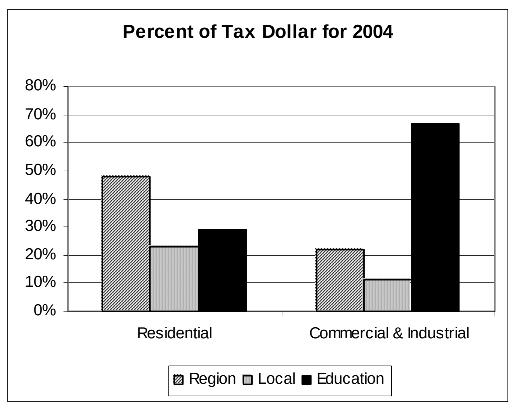
The capacity is required to build infrastructure in advance of the development that it serves. One approach would be to monetize the TIF revenues through a development bond or similar vehicle. A realistic term for major capital infrastructure development may well be 25-35 years. The capability to issue debt will also be affected by the uncertainty of the amount of future revenues and the timing of the receipt of those revenues.

4.2.4 Eliminating Capping Within TIF Areas

The *Municipal Act* capping provisions also constrain the effectiveness of the TIF by limiting the realty taxes on some business properties to well below the current value assessment tax level. The potential tax increment may be substantially less than at full CVA level taxes. While it is possible to claw back the revenue lost to capping protection, this shifts the burden to business properties outside the development area, effectively clouding the presumed transparency of the TIF vehicle, and it presumes that there are sufficient decreases available to fund the clawback.

4.2.5 Provincial Participation is Required

The Province is an important partner in the TIF strategy, not only as an enabler but also as a participant. The greatest benefit is achieved when the provincial government contributes a portion or the entire increment education tax portion of the property tax increment in the TIF zone.



As the accompanying graph shows, the educational component for the Commercial and Industrial property classes represents approximately 70% of the total taxes collected. Even for the Residential class, the education component still comprises approximately 30% of the total taxes.

4.3 Challenges

4.3.1 Value Enhancement a Projection Only

The value enhancement may come from a combination of changes in the classification of the property and from pure market value enhancement. The tax increment financing model for infrastructure development is largely predicated on the basis that property value will increase as a result of infrastructure development; this is, of course, subject to economic factors. Experience in the US has demonstrated that property values in proximity to the development increase with the infrastructure development but it will likely require a number of assessment cycles to be realized.

4.3.2 Uncertain Revenue Stream

A lack of certainty in the revenue stream will have some effect on the ability of an entity to monetize the costs through a vehicle such as a bond. This may result in substantial discounting of the costs that can be financed, a substantial increase in the yield of the instrument, and possibly in the guarantees or other support required for the financing. If indeed the anticipated revenues fail to materialize, a municipality may have to make good on a guarantee to support the debt repayment.

4.3.3 TIF Restricts Revenues for Other Purposes

Revenues committed to a TIF project are restricted from use for other regional growth related projects, in effect reducing the planning flexibility of future administrations. It is therefore incumbent upon the administration to enter carefully upon a course of action that may encumber future revenues for a significant period of time.

4.4 The Legislative Requirements for making TIF a Viable Option to Municipalities in Ontario

Based on the US experience, for TIF to be a viable option to municipalities in Ontario, the following legislative changes should be considered:

- Granting municipalities the authority to implement tax increment financing
- Granting municipalities the ability to assist the TIF entity in the financing process
- The Province joining as a partner in the sharing the contribution of incremental taxes to the development process
- Removing the capping restrictions within TIF areas to enhance the effectiveness and transparency of TIF
- Granting municipalities the ability to create a TIF authority or development corporation with the powers to undertake and finance development projects

4.5 Relationship to Vision 2026

Tax increment financing is consistent with Goal 6 of Visions 2026: Managed and Balanced Growth and specifically with the Action Areas of “Taking a Strategic Approach to Growth Management” and “Financing Growth.”

4.6 The Need for a More Detailed Strategy

The introduction of tax increment financing legislation by the Province will require a more detailed strategy with respect to the possible application of TIF in York Region. It is recommended that this strategy report be prepared in conjunction with the Planning and Development Services Department and the York Region Rapid Transit Corporation.

5. FINANCIAL IMPLICATIONS

There are no current financial implications associated with this report. The future success of regional projects such as the YRTP could be positively affected by the ability to use tax increment financing.

6. LOCAL MUNICIPAL IMPACT

Local municipalities would benefit from achieving planning objectives arising from infrastructure development. The enhancement of property values would improve property tax revenues from the business property classes to the benefit of taxpayers within the municipality and the region.

7. CONCLUSION

Tax Increment Financing is an attractive strategy if the Province makes the necessary legislative changes to create a viable process. It is recommended that Council endorse the concept of tax incremental financing as a viable fiscal tool for supporting specific growth related development activities.

It is also recommended that Council request that the Province introduce legislation to create tax increment financing as fiscal tool for municipalities. Further, it is recommended that staff be directed to prepare a further report outlining a more detailed strategy for using tax increment financing to support activities consistent with the Region’s centres and corridors planning strategy

The Senior Management Group has reviewed this report.