Public Service
http://www.publicservice.co.uk/feature_story.asp?id=15935

TIF: an idea whose time has come

Friday, February 18, 2011
By Kevin Hoctor

The Deputy Prime Minister has committed the government to bring forward new powers for local authorities to borrow based on growing business rate income, along the lines of tax increment financing (TIF) in the US. But, asks Kevin Hoctor, what could TIF look like in the UK, what might it deliver and what are the risks?

***

The principle behind TIF is a simple one – local authorities and local businesses can fund upfront public investment in an area by borrowing against expected increases in property tax revenues resulting from the development. Over the allotted period the extra funds generated by the development are then ring- fenced until the debt is paid off.

There are a number of reasons why this option is attractive for the business community. It offers a new option for local regeneration project funds at a time of public spending cuts and a struggling economy. It also provides an avenue to fund the local infrastructure needed to support new business growth, without the need to raise new taxes. It has also been operating for many years in the US and Canada.

A 2008 report for the Core Cities Group by PricewaterhouseCoopers made the case for accelerated development zones – a variation of TIF – in England. They argued that by enabling local authorities to capture future business rate growth from development, investment could be made to fund the regeneration of a number of derelict city areas. By their assessment, schemes in Sheffield's Lower Don Valley, Birmingham's Eastside and the Aire Valley area of Leeds would generate 26,000 extra new jobs, 6,150 homes and GVA growth of £1 bn a year. Since that time, other areas have also been making the case for TIF, notably the Black Country and Edinburgh, whose TIF proposal has recently been approved by the Scottish government.

There are pitfalls from the US TIF experience that would need to be avoided for this to work here. First introduced in the 1950s, TIF use has massively expanded since the 1970s, with notable examples in Illinois, New Mexico and California. Chicago in particular has seen a rapid expansion and now has hundreds of TIF projects. The sheer proliferation of schemes in the US has, however, been a problem, with a lack of oversight limiting their effectiveness and creating unnecessary competition. Given the fact that TIF will be unprecedented territory for the UK, the initial number of projects should be limited, but have sufficient variety to see what works well, before any further expansion.

Any schemes will need to address the problem of additionality – that is focusing TIF on projects that will support business growth in areas that would not otherwise be developed, creating new private sector jobs and investment. Some US schemes have been criticised for targeting areas that offer obvious high property value growth or generate income diverted from existing funds and investment in the region. It is therefore important that TIF schemes in the UK demonstrate clear additional benefits – for example, by creating the conditions for growth in areas that are crying out for more private sector activity and employment.

The other key concern is ensuring that the risks involved in TIF projects are appropriately managed. While many TIF schemes have proved to be successful in generating the necessary returns to pay off their borrowing debts, there is a clearly an element of risk that others will not deliver the predicted returns. In California, TIF schemes jeopardised by changes to the constitution to restrict property tax increases resulted in the State of California and city authorities having to bail out the schemes to prevent a default on the loan. An outcome like this, with the result that further tax increases would be needed, cannot be allowed to happen in the UK. This should not mean restricting how projects are financed in terms of the share of risk taken on by developers or how repayment will be structured, but it should mean an assessment of the overall level of risk, viability and value for money of TIF projects. Whether it is by the Treasury or another national body, locally developed schemes should undergo a robust approval process.

It is also critical that the local business community leads and shapes TIF schemes to ensure that they have the necessary economic development focus. Areas that get approval to set up local enterprise partnerships should use this forum to enable businesses and local government to discuss and develop effective TIF proposals. The government should also link the introduction of TIF with other measures to drive local business growth, such as the planned business increase bonus proposals and exploring the creation of a new generation of enterprise zones (with reduced business costs and regulatory barriers).

TIF increasingly looks like an idea whose time has come. For businesses, TIF offers the potential for investment in economically critical infrastructure projects without the need for upfront tax increases, providing it can be structured to deliver the best economic outcomes.

Kevin Hoctor is senior policy adviser at the British Chambers of Commerce