U.S. Department
of Transportation

**Federal Highway Administration**

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# Essential Nexus, Rough Proportionality, and But-For Tests

## State of the Practice

# Contents

# Executive Summary

States are exploring value capture techniques for several reasons. First, they raise needed revenue. Second, if properly designed and implemented, they can help integrate infrastructure investments with land use objectives by encouraging development near existing infrastructure, thereby reducing the sprawl that harms the environment and burdens taxpayers. Third, value capture techniques can enhance equity by operating more like fees than taxes. In other words, they raise revenues from those who benefit from infrastructure in proportion to the benefits received or from those who demand its expansion in proportion to the costs imposed. Fourth, if support for a tax increase is weak, value capture can be another revenue opportunity to fund infrastructure needs.

Simply put, "value capture" is value returned because value was received. By this definition, value capture encompasses user fees, access fees, and mitigation fees or requirements. User fees, such as the per gallon fee for water, highway tolls, transit fares, parking meter fees, etc., are rarely mentioned in the "value capture" discussion. Access fees, such as special assessments, seek to recoup publicly created land values from property owners who would otherwise receive a windfall profit at other taxpayers' expense. Access fees can also be referred to as "land value return."[1] Mitigation fees or requirements, such as exactions and impact fees, seek reimbursement from private development activity when it would otherwise impose costs on other taxpayers who neither caused nor benefited from those expenditures.

As States explore value capture implementation, they seek to understand the legal prerequisites and standards applied to these techniques. This report explores some of these legal issues.

States hold broad powers to impose taxes and fees, subject primarily to due process and uniformity requirements in federal and state constitutions and statutes. To the extent that a State delegates these powers, local jurisdictions may also impose taxes and fees pursuant to the delegation and according to the same due process and uniformity requirements. Thus, value capture techniques must meet uniformity and due process requirements.

Additionally, under some circumstances, some value capture techniques could be challenged pursuant to the "takings" clause of the Fifth Amendment. The reason for this is that, unlike a tax applied to all persons and property in a jurisdiction equally, many value capture techniques apply to some properties but not to others. If properly implemented and administered, these differences are justified and do not violate the Fifth Amendment.

In the case of infrastructure access fees (such as special assessments), some properties are receiving special benefits that are not available to other persons or property generally.

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[1] NCHRP Report 873, "*Guidebook to Funding Transportation Through Land Value Return & Recycling*," (2018)

Therefore, it is fair (and legal) for a community to charge beneficiaries for such special benefits. In the case of mitigation fees, private development is imposing a cost on the general public by requiring new infrastructure or capacity expansion for existing infrastructure. To the extent that a private development project will impose costs on the community, it is fair (and legal) for a community to seek reimbursement for these costs (or to avoid them) by requiring compensation (or in-kind infrastructure provision) from the development projects.

"If properly implemented and administered" is an important phrase. Private property owners are reluctant to part with funds or to incur publicly mandated costs. Their self-interest encourages them to see value capture techniques as arbitrary, non-uniform or as uncompensated "takings."

Receiving a windfall benefit from a public infrastructure project or imposing infrastructure creation or expansion requirements on a community are closely related to each other despite representing impacts to opposite parties.[2] In one instance, a private party is receiving a benefit without providing compensation. In the other, a private party is imposing costs upon others without providing reimbursement.

Nonetheless, when a community seeks reimbursement from a private party for imposing a cost on that community (through the imposition of exactions or impact fees), a community justifies this reimbursement by showing:

- There is an "essential nexus" (or "relationship") between the private party's activity and a burden that is placed on the community as a result; and
- The fee or requirement placed on the private party is "roughly proportional" to the burden imposed.

Similarly, when a community infrastructure project provides a special benefit to private property, the community might obtain compensation from that private property by imposing a special assessment. A community justifies this assessment by establishing:

- A nexus between the public project and the private gain; and
- The proportionality between the fee levied and the benefit received.

Although the Supreme Court developed the "essential nexus" and "rough proportionality" tests in the context of exactions and impact fees, because special assessments are related (albeit by

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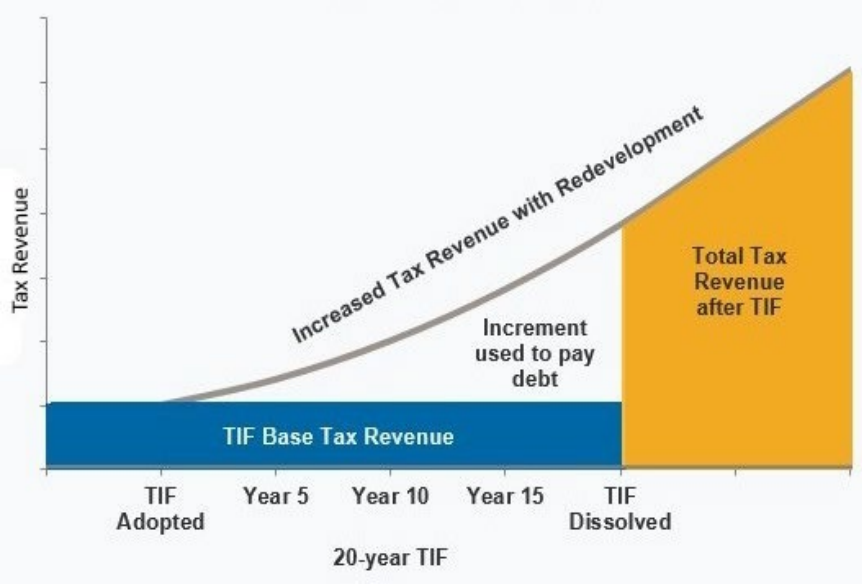
[2] Abraham Bell and Gideon Parchomovsky, *Givings*, 111 Yale Law Journal 547 (2001). https://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=4571&context=ylj . See also Rick Rybeck, ""Avoiding Mis-Givings: Recycling Community-Created Land Values for Affordability, Sustainability and Equity," Journal of Affordable Housing and Community Development Law, Vol 28 No 2, October, 2019, pp 299-323. *https://www.americanbar.org/content/dam/aba/publications/journal_of_affordable_housing/Volume28_Number2/ah_journal_10_18_19.pdf*

addressing benefits bestowed rather than mitigating costs imposed), jurisdictions and courts apply the same standards there as well.

- Tax increment financing (TIF) is a value-capture technique that does not fit neatly into the user-fee, access-fee, or mitigation-fee categories. See
- Figure 1. Although each TIF should be understood in terms of its particular mechanics, most follow the following pattern:
- There is a property (or cluster of properties or neighborhood) where development is desired but not occurring.
- Specified tax revenues from that property or neighborhood are benchmarked.
- A public project (site assembly, toxic waste cleanup, infrastructure improvement, etc.) is undertaken to catalyze development.
- Increases in tax revenues above the benchmarked amounts are defined as the "tax increment." The tax increment is segregated from the revenue stream and deposited into an account dedicated to paying for the public project for as long as is required to pay off the TIF portion of project costs.

**Figure 1. Tax Increment Financing Diagram**




*Source: Kentucky League of Cities,* https://www.klc.org/infocentral/detail/26

The key to this graphic is that revenues increase after TIF creation NOT because of higher tax rates, but because of increased development and economic activity that are subject to the existing tax rates. Although there have been academic critiques of the validity of the but-for assumptions, there has been little litigation of this requirement. In the illustration, benchmarked public revenues would remain constant if the public infrastructure project is not completed.

This might be true under certain circumstances, but under other circumstances, benchmarked revenues might decline in the absence of the project or they might increase—but by a smaller amount than if the project were undertaken. The definition of the tax increment can be and should be refined to reflect the actual situation in a particular place at a particular time. The critiques of TIF referenced later in this report provide analytical methodologies for determining the extent to which the but-for test could be satisfied. The judicial decisions on this topic summarized later in this report how that courts are reluctant to second-guess the findings of a legislative body.

TIF is based on the following assumptions:

- Without the public project, new development would not occur.
- Without new development, tax revenues would not increase.
- The public project is the only reason why benchmarked revenues increase.

This report concludes by exploring some analytical methods and tools for determining the extent of benefits received (or costs imposed) by properties in order to equitably apportion infrastructure costs among those who benefit from (or impose costs upon) infrastructure systems. Jurisdictions that follow the substantive and procedural requirements contained in value capture enabling statutes and that carefully analyze the special benefits created by public infrastructure (or the costs imposed by private development) will implement value capture techniques in a manner that is likely to survive legal challenges based on due process, uniformity, essential nexus and rough proportionality. Following these requirements should also meet the but-for test applied to TIFs.

# Introduction

Although there appears to be a broad consensus in the United States that there is a significant and unmet need for additional infrastructure maintenance and improvement, public sources of funding are often insufficient. Therefore, additional sources of infrastructure funding provide opportunities for States, counties, municipalities, and regional authorities to fill funding gaps.

Experience shows that new and improved infrastructure often increases the price of nearby land, promotes density, and can stimulate economic development. High land prices can displace some development away to cheaper, but more remote sites. Once these remotes sites are developed, occupants then demand the extension of infrastructure to these areas (even though there is excess capacity where the infrastructure was initially created or improved). And, once infrastructure is extended to these remote areas, land prices increase and the cycle repeats. The ensuing "urban sprawl" necessitates more driving, creates more impervious surfaces, and disrupts natural ecosystems. Thus, sprawl increases energy consumption and pollution. In addition to these adverse environmental consequences, sprawl is also costly for taxpayers who must pay for the wasteful duplication of expensive infrastructure.[3]

States are exploring value capture techniques for several reasons. First, they raise needed revenue. Second, if properly designed and implemented, they can help integrate infrastructure investments with land use objectives by encouraging development near existing infrastructure, thereby reducing the sprawl that negatively impacts the environment and taxpayers. Additionally, value capture techniques can enhance equity by operating more like fees than taxes. In other words, they raise revenues from those who benefit from infrastructure in proportion to the benefits received, or from those who demand its expansion, in proportion to the costs imposed.

As States explore value capture, they seek to understand the legal prerequisites and standards applied to these techniques. States hold broad powers to impose taxes and fees[4], subject primarily to due process[5] and uniformity requirements in Federal and State constitutions and

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[3] See the appendix for graphics that illustrate this point.

[4] U.S. Dept. of Treasury, State and Local Taxes, Resource Center. *https://www.treasury.gov/resource-center/faqs/Taxes/Pages/state-local.aspx* .

[5] U.S. Library of Congress, Due Process and Taxation: Doctrine and Practice. *https://constitution.congress.gov/browse/essay/amdt5_4_6_2_1/* .

statutes.[6] To the extent that a State delegates these powers,[7] local jurisdictions may also impose taxes and fees pursuant to the delegation and according to the same due process and uniformity requirements. Thus, value capture techniques must meet uniformity and due process requirements. Additionally, under some circumstances, some value capture techniques could be challenged pursuant to the "takings" clause of the Fifth Amendment. In the following sections, this report will explore the legal ramifications of the "essential nexus" test, the "rough proportionality" test, and the but-for test for certain value capture techniques. The final section of this report will explore analytical methods and tools for determining the extent of benefits received (or costs imposed) by properties in order to equitably apportion infrastructure costs among those who benefit from (or impose costs upon) these community-provided systems.

To meet the "uniformity" requirement, a tax applies equally to every subject (person, business or thing) in the same situation.[8] For example, every similarly situated person or business with identical income and expenses in a jurisdiction will pay the same income tax rate. Every purchaser of a taxable item in a jurisdiction will pay the same sales tax rate applied to that type of taxable good or service purchased. If infrastructure investment is likely to produce benefits of the same general magnitude for everybody, then a tax might be a fair way to raise funds to create, operate and maintain it.

However, if infrastructure investment produces unique benefits for only a few (in addition to or in lieu of general benefits for everybody), then it might be more efficient and more fair to charge these beneficiaries in lieu having all taxpayers subsidize them.[9] Studies show that transportation facilities and services often confer a special benefit on nearby properties to the extent that these properties end up with enhanced accessibility.[10] This enhanced accessibility is often reflected in increased land value.[11] In other words, urban land values typically reflect the access of parcels

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[6] Legal Information Institute, "Uniformity Requirement" *https://www.law.cornell.edu/constitution-conan/article-1/section-8/clause-1/uniformity-requirement* .

[7] "State & Local Government" at *https://www.whitehouse.gov/about-the-white-house/state-local-government/* . Some States delegate powers liberally to local governments; they are known as "home rule" States. Other States are stricter in their delegation of powers; they are known as "Dillon's Rule" States. It is not uncommon for a State to be liberal in the delegation of some powers (e.g., zoning) and strict in the delegation of others (e.g., taxation). In essence, all local government powers are derived from States and must be consistent with State constitution and laws.

[8] Legal Information Institute, "Uniformity Requirement". *https://www.law.cornell.edu/constitution-conan/article-1/section-8/clause-1/uniformity-requirement*.

[9] Rick Rybeck, *"Avoiding Mis-Givings: Recycling Community-Created Land Values for Affordability, Sustainability & Equity*," Journal of Affordable Housing and Community Development Law, Vol. 28, No. 2 (2019) pp 299–323. *https://www.americanbar.org/content/dam/aba/publications/journal_of_affordable_housing/Volume28_Number2/ah_journal_10_18_19.pdf*

[10] NCHRP Report 873*, "Guidebook to Funding Transportation Through Land Value Return & Recycling*," (2018). *http://www.trb.org/Main/Blurbs/177574.aspx*

[11] NCHRP Report 873.

to local and regional amenities. For example, urban land values typically spike in downtowns near the centers of roadway and transit networks; transportation improvements will typically make more amenities accessible and convenient to parcels that are well-served by those improvements.

Returning publicly created land values to the community ("land value return") is one approach for charging beneficiaries for the special benefits that they receive. To the extent that this approach relies on utilizing a standard rate applied universally to objectively determined land values for all parcels, such an approach satisfies standards of uniformity. This variant of the property tax (applied to land value only) acts more like a fee than a tax to the extent that land values are directly related to public infrastructure improvements. Charges based on land values are proportional to the benefits received.[12]

Communities might also choose different value-capture techniques, such as a special assessment or tax-increment financing (TIF). Special assessments impose a surcharge on the existing property tax, but only for properties deemed to receive a special benefit from new or improved infrastructure. Because a special assessment is applied to some properties and not to others outside of the district, it might raise the issue of uniformity. Jurisdictions using special assessments take care to comply with the principles of uniformity and due process when seeking compensation for publicly created benefits conferred on particular properties. They also make findings that infrastructure projects provide identifiable special benefits to the properties subject to the assessment and that the assessment itself is proportional to the benefits received or costs incurred.

Another approach to value capture when infrastructure creates a special benefit is tax increment financing. Unlike special assessments, TIF does not impose a special or additional tax burden on properties that benefit from transportation improvements. Thus, TIFs are not typically challenged in court by affected property owners. In fact, property owners often advocate for TIF creation.[13] But TIFs segregate some revenue from a community's general fund in a dedicated account for specific infrastructure improvements, and for this reason, some enabling legislation might constrain the application of TIFs to "blighted" areas where development would not otherwise occur but for the improvement of nearby infrastructure.[14] This report examines the state of the practice regarding the but-for test.

Whereas some types of infrastructure creation or improvement might benefit some properties more than others, sometimes private development might create unfair burdens for others. In a jurisdiction where the variable costs associated with water and sewer services are paid for by a per-gallon fee, and fixed costs associated with facilities (pipes, reservoirs, and purification

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[12] NCHRP Report 873.

[13] Sean McCarthy, Tax Increment Financing in Arizona, (ATRA) 2017, p 2. *http://www.arizonatax.org/sites/default/files/publications/special_reports/file/tif_in_arizona.pdf*

[14] Not all TIFs are restricted to blighted areas—for example, Transportation Reinvestment Zones in Texas.

plants) are paid for by a fixed percentage applied to ad valorem property taxes, if there is excess capacity in the system and new development occurs in the existing service area, the per-gallon fees for water consumption and sewage production in the new development will cover the variable costs. The new development's generation of revenue for fixed costs is likely to be negligible in terms of the entire system. This is not a problem if this development is primarily using existing pipes, reservoirs, and purification plants.

But in a jurisdiction where the water and sewer treatment systems are at full capacity, new development will require new treatment facilities to avoid system failure. This is similar to new development in a rural area where municipal water and sewer pipes must be extended across miles of farmland to reach the proposed development. In each case, the per-gallon fees generated by the new development cover its share of variable operating costs, but its negligible generation of revenue for fixed costs does not come close to paying for the new treatment facilities or mainline pipe extension (or even for its share of the new facilities, assuming that capacity is greater than required for this one new development).

In this case, the fixed percentage applied to ad valorem taxes dedicated for water and sewage capital expenditures could be increased, the rate of ad valorem taxes could be increased throughout the jurisdiction, or the per gallon fee could be increased to cover new capital costs. Under these three approaches, all taxpayers pay for increasing system capacity although this expenditure is necessary only to accommodate the new development. In other words, a system of general taxation requires the occupants of a new development to pay a small share for essential facilities while most other taxpayers end up paying more for new facilities that provide them with little or no benefit. Thus, payment for new capacity out of general revenues constitutes a subsidy to the new development, raising issues of equity and fairness.[15]

In the special assessment and TIF example, a jurisdiction's infrastructure investment created a special benefit for some property owners. The infrastructure needed for new private development is imposing a cost on the community that will exceed its share of general taxes paid. In such circumstances, to avoid an unfair and unintended subsidy to new development, jurisdictions might demand that developers provide specified public facilities, dedicate land for such facilities, or pay cash for their fair share of such facilities as a condition for development permit approval. These demands are referred to as "exactions." Some jurisdictions negotiate exactions on a case-by-case basis.[16] Some jurisdictions have adopted formal calculations to determine the appropriate cash payment for offsite infrastructure improvements necessitated by various types of new development. These are often referred to as development impact fees.[17]

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[15] See the appendix for illustrations of whether incremental tax revenue is sufficient to pay for additional public facilities and services required by new development.

[16] FHWA, Value Capture Implementation Manual: Capitalizing on the Value Created by Transportation, August 2019. See Section 4.2, "Negotiated Exactions."

[17] FHWA, Value Capture Implementation Manual, Section 4.1, "Impact Fees."

Exactions are cash or in-kind infrastructure required of developers in return for development permits. Although exactions could be described as cost reimbursement or cost avoidance, exactions have induced some property owners to claim that the implementing jurisdiction has taken their property without just compensation. Lawsuits brought by property owners are often referred to as “inverse condemnation.” Under condemnation, a government agency uses its eminent domain power to initiate a judicial proceeding to obtain private property for a public purpose and with just compensation (as determined by a court) pursuant to the Fifth Amendment. Under inverse condemnation, the property owner initiates the proceeding, claiming that the government has taken property through over-regulation and must be required by the courts to pay compensation. Supreme Court opinions on such cases have given rise to the essential nexus and rough proportionality tests that are the subject of the next section.

# Exactions and Special Assessments: Essential Nexus and Rough Proportionality

Exactions are used not only by jurisdictions to obtain compensation or avoid expenditures for additional infrastructure costs imposed by new development, they have also been used to protect the public interest from adverse impacts of development on view sheds or public land access. Yet landowners have frequently challenged exactions in court as takings that fail to meet Fifth Amendment requirements. Although courts generally uphold the right of jurisdictions to regulate property through zoning, historic preservation ordinances, and exactions, they have also invalidated some regulations as going too far.

## Evolution of the Case Law

The purpose of this subsection is to review the evolution of Supreme Court rulings on essential nexus and rough proportionality to indicate how jurisdictions can use exactions to protect the public interest while satisfying the court's demands that jurisdictions avoid uncompensated takings. (The Analysis of the Case Law subsection, p. 13, discusses Supreme Court rulings on exactions and their validity.)

The Fifth Amendment to the U.S. Constitution limits the ability of the government to take private property. Such takings are subject to "due process," must be undertaken for a "public use," and must provide "just compensation" to the owner.[18] Thus, if government were to take private property for a public facility (such as a road, park, or courthouse), it would exercise eminent domain by condemning the property.

During the last hundred years, all levels of government have relied increasingly on economic regulations to satisfy various governmental objectives. Not surprisingly, when government regulations limit the type, intensity, or siting of development, property owners may feel that their ownership rights have been diminished and they might object to this by making a claim that the government has taken their property without just compensation in violation of the Fifth Amendment. Such claims are sometimes referred to as "inverse condemnation" because instead of the government going to court to condemn a private property, the property owner must sue the government to show that the government, through regulatory over-reach, has effectively taken the property without providing just compensation.

The judicial record on takings, however, shows considerable deference to the exercise of police powers by local jurisdictions. Many rulings over more than 100 years have made clear that:

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[18] The Fifth Amendment to the U.S. Constitution reads, in part, "No person shall . . . be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use, without just compensation." *https://constitution.findlaw.com/amendment5.html*

> [C]laimants generally are not entitled to takings compensation for adhering to generally applicable obligations that advance the public interest,[19] safeguards that prevent owners from using their land in ways harmful to others,[20] or baseline standards for market and social interactions.[21],[22]

The fact that the regulations in each of these cited cases may have diminished the economic value of property or limited future development was not, in itself, a taking. Nonetheless, in 1922 in the case *Pennsylvania Coal Co.* v. *Mahon,* 260 U. S. 393 (1922),[23] it was recognized that if the protection against physical appropriations of private property was to be meaningfully enforced, takings must include excessive regulation as well.[24]

## AGINS V. CITY OF TIBURON (1980)

In the case of Agins v. City of Tiburon,[25] Dr. and Mrs. Agins (the landowners) acquired five acres of land in Tiburon. Thereafter, a California law was enacted requiring Tiburon to create a general land use plan governing both land use and the development of open land. Tiburon did so and then enacted a zoning ordinance to help implement the plan. The zoning for the five-acre parcel limited use to single-family homes and related accessory buildings. Between one and five homes were allowable for development on the five-acre parcel. Shortly after enactment of the

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[19] See *Gorieb* v. Fox, 274 U.S. 603, 609-10 (1927) (holding that a setback requirement did not constitute a taking); *Village of Euclid* v. *Ambler Realty Co.*, 272 U.S. 365, 379-80, 395-97 (1926) (holding that a zoning scheme did not constitute a taking); *Welch* v. *Swasey*, 214 U.S. 91, 103, 107-08 (1909) (holding that a statutory building height limit did not constitute a taking).

[20] See Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 474-77, 500-02 (1987) (upholding a Pennsylvania regulation that limited how much subsurface coal could be mined in order to protect surface structures); Goldblatt v. Town of Hempstead, 369 U.S. 590, 591-92, 595-96 (1962) (upholding a town regulation that prohibited excavation below the water table, which in turn rendered petitioner's quarry effectively useless); Walls v. Midland Carbon Co., 254 U.S. 300, 309-10, 324-25 (1920) (upholding a statute conditioning the burning of natural gas); Hadacheck v. Sebastian, 239 U.S. 394, 404-05, 409-11 (1915) (upholding a regulation that banned the operation of brick factories within Los Angeles' city limits); Reinman v. City of Little Rock, 237 U.S. 171, 176-77 (1915) (upholding a regulation banning livery stables from certain areas in the community); Mugler v. Kansas, 123 U.S. 623, 653, 675 (1887) (upholding a regulation that banned the production of alcohol for recreational purposes); Powell v. Commonwealth, 7 A. 913, 914-16 (Pa. 1887) (upholding a law that outlawed the production of oleomargarine).

[21] See Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 415-18, 445-48 (1934) (upholding the constitutionality of a state mortgage moratorium law, which allowed courts to extend the period of redemption for foreclosure sales); Block v. Hirsh, 256 U.S. 135, 153-58 (1921) (holding that a rent control law, which regulated rent prices and allowed tenants to stay in their apartments so long as they paid on time and satisfied any other conditions of the lease, was not a taking).

[22] Timothy M. Mulvaney, "The State of Exactions," William & Mary Law Review, Volume 61 Issue 1 (October 2019) pp 169-221 at pp 218-219. (The quote includes the three footnotes, numbered differently in the original.)

[23] *https://supreme.justia.com/cases/federal/us/260/393/case.html*

[24] *Lucas* v. *South Carolina Coastal Council*, 505 U.S. 1003 (1992) discussing Pennsylvania Coal at 1014.

[25] *Agins* v. *City of Tiburon*, *447 U.S. 255* (1980). *https://supreme.justia.com/cases/federal/us/447/255/*

zoning ordinance, Tiburon attempted to acquire the parcel through eminent domain. Tiburon abandoned this effort after one year and reimbursed the landowners for their costs related to that proceeding. The landowners did not file a development plan nor seek development permits. However, the landowners sued on the grounds that the zoning ordinance constituted a "taking without compensation." [26]

The court denied this claim. The court cited *Euclid v. Ambler Realty*[27] and other cases to show that the proper use of a jurisdiction's police power does not constitute a "taking" under the Fifth Amendment. The court found that the attempt to acquire the parcel by eminent domain was irrelevant to this proceeding.

When property owners file a claim that the exercise of police powers constitutes a "taking," courts often cite *Euclid v. Amber* which is the Supreme Court case that validated zoning law. They also mention *Penn Central Transportation Company v. New York City.*[28] In this case, the Penn Central railroad company hoped to develop the air rights above Grand Central Terminal. Grand Central Terminal had been previously designated as a landmark by New York City. Pursuant to the City's landmarks law, any alterations required approval from the New York City Landmarks Commission. Penn Central submitted two plans to the Landmarks Commission which rejected both plans. In exchange, the Commission offered Penn Central transferable development rights. In other words, Penn Central could sell its development rights to another property owner (in certain designated receiving areas) where these owners could then add that development density to the density already allowed by existing zoning. Penn Central declined this offer and sued New York City for a taking without just compensation.

Of particular importance, in the Penn Central case, the Supreme Court articulated a three-part balancing test for deciding a regulatory taking:

- "[t]he economic impact of the regulation on the claimant,"
- "the extent to which the regulation has interfered with [the claimant's] distinct investment-backed expectations," and
- the "character of the governmental action."

In cases like *Penn. Central Transportation Company v New York City* and *Agins* v *City of Tiburon*, the Supreme Court determined that the burden of proof that a taking occurred was on

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[26] *Agins* v. *City of Tiburon*, *447 U.S. 255* (1980). *https://supreme.justia.com/cases/federal/us/447/255/*

[27] *Village of Euclid, Ohio v. Ambler Realty Co.*, 272 U.S. 365 (1926)

[28] *Penn. Central Trans. Co. v. New York City*, 438 U.S. 104, at 122 (1978)

the property owner plaintiff. Furthermore, the property owner would need to show that almost all practical use of the property has been prohibited in order to meet that burden of proof.[29]

Both the burden of proof and the court's analysis began to shift in *Nollan* v. *California Coastal Commission*.

## *NOLLAN* AND ESSENTIAL NEXUS (1987)

In the 1980s, the Nollan family owned an ocean-front property in Ventura County, California. A bungalow on the property had fallen into disrepair. The Nollans filed an application with the California Coastal Commission to demolish the bungalow and replace it with a three-bedroom house. The Commission agreed to approve the request, but only if the Nollans created a legal easement granting public access across their private beach, connecting two public beaches on either side of the Nollans' property. When the Nollans objected, the Commission stated that it was acting to protect the public's legitimate interests in having views of the beach and access to the beach. The Nollans sued the Commission on the grounds that the easement constituted an uncompensated taking. [30]

The court ruled in favor of the Nollans against the California Coastal Commission. The court agreed that the Commission had a legitimate public interest in assuring that the public had views of the beach and access to the beach. However, the court found no connection between these legitimate interests, the Nollans' development activity, and the creation of an easement for people who were already on public beaches to the north and south of the Nollans' property. In other words, there must be an "essential nexus" between the legitimate public interest and the condition imposed upon the property owner to achieve that interest.

## *LUCAS*: REGULATIONS THAT ARE INTRINSICALLY TAKINGS (1992)

In 1986, petitioner Lucas bought two residential lots on a South Carolina barrier island, intending to build single-family homes such as those on the immediately adjacent parcels.[31] At that time, Lucas's lots were not subject to the State's coastal zone building permit requirements. In 1988, however, the state legislature enacted the Beachfront Management Act, which barred Lucas from erecting any permanent habitable structures on his parcels. He filed suit against the South Caroline Coastal Council, contending that, even though the Act may have been a lawful exercise of the State's police power, the ban on construction deprived him of all "economically viable use" of his property and therefore effected a "taking" under the Fifth and Fourteenth Amendments that required the payment of just compensation.[32] The trial court ruled in favor of

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[29] Mulvaney, 2019 *op. cit*., citing 438 U.S. 104, 124, 128 (1978) (citing Goldblatt v. Hempstead, 369 U.S. 590, 594 (1962).

[30] *Nolan v. California Coastal Commission*, 483 U.S. 825 (1987), at 837

[31] *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003 (1992)

[32] Agins v. City of Tiburon, 447 U. S. 255, 261.

Lucas. South Carolina appealed and the South Carolina Supreme Court ruled in favor of the State. Lucas appealed to the U.S. Supreme Court which ruled in his favor.

For our purposes, the key finding of the court was that the ad hoc balancing tests (such as the one applied in *Penn Central*) are not necessary in two types of cases: where there is a physical invasion, no matter how small,[33] and "… where regulation denies all economically beneficial or productive use of land."[34] In these two types of cases, a taking has occurred categorically and all that remains is to calculate the value of the taking for the purpose of compensating the owner. [35]

## *DOLAN* AND ROUGH PROPORTIONALITY (1994)

Florence Dolan owned a 1.67-acre parcel in the city of Tigard, Oregon. On the eastern portion of the lot was a 9,700-square foot store and a gravel parking lot. The west side of the lot bordered Fanno Creek. Dolan petitioned to increase the size of the store to 17,600 square feet and to pave a parking lot for 39 cars. The proposed use was consistent with the zoning. Periodic flooding occurs along Fanno Creek. Tigard's comprehensive plan prohibits development within the 100-year floodplain and calls for properties within the floodplain to dedicate that area as a "greenway." It also calls for new development to create bicycle paths where possible (consistent with the bicycle plan) or to pay for their creation offsite if necessary.

Tigard accepted the proposed development plan provided that Dolan dedicate land in the floodplain to a greenway (to mitigate additional storm water runoff) and dedicate a 15-foot-wide strip adjacent to the floodplain for a bicycle path (to mitigate additional traffic generated by the store's expansion).[36] Tigard noted that the land dedication constituted 10 percent of the parcel

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[33] "Physical invasion" means that the government or its agent is physically possessing part of the property. An example could be a cell phone repeater or magnification device. Even if it is very small, because it is attached to the roof or outside wall of a building, this constitutes a physical occupation of part of the property. Likewise, if the government requires an easement for a bicycle or pedestrian path, this constitutes a physical invasion because this easement prevents the property owner from being able to exclude other people from his property. According to the court, the ability to exclude other people is a defining characteristic of private property.

[34] Lucas at 1015 citing *Agins*, 447 U.S., at 260

[35] Lucas at 1015. The court does make an exception if the regulation in question prohibits a use that would be considered a nuisance under common law. See Lucas at 1029. The rationale is that it's not a taking if, even in the absence of the law or regulation, a contemplated use would unreasonably obstruct, injure, inconvenience, or annoy others making reasonable use of their own property or public space**.** An example might be maintaining an impoundment pond for hog waste in an urban neighborhood. The stench would prevent others from making reasonable use of their adjoining properties. Thus, a regulation prohibiting hog waste impoundments in an urban neighborhood would not constitute a per se taking because, even in the absence of the regulation, the common law of nuisance would not permit such an activity.

[36] *Dolan* v. *City of Tigard*, 512 U.S. 374 (1994)

and that it would count toward the 15 percent open space requirement for all parcels already required by zoning.

Dolan appealed for a variance without citing extenuating circumstances. The city denied the variance request and noted that the required dedication was reasonable to mitigate the proposed increase in impervious surface that would contribute to flooding of Fanno Creek. Upon appeal, the city found that the required dedication was reasonable and related to the goals of mitigating flooding and for providing bicycle access to mitigate increased traffic generated by the store's expansion.

The court begins by noting its deference to land use regulation generally and quoting the finding in Agins that "A land use regulation does not effect a taking if it "substantially advance[s] legitimate state interests" and does not "den[y] an owner economically viable use of his land." *Agins* v. *City of Tiburon,* 447 U. S. 255, 260 (1980)."[37] But then the court distinguishes the "legislative" nature of the land use controls in Agins against the "adjudicative" nature of the conditions applied to Dolan's particular property.[38] Furthermore, the dedication of land (deeding the land to the city) is not a limitation on use but a required divestiture of land.

The court found that there was an essential nexus between the required dedication of land, the legitimate need to reduce or mitigate storm water runoff, and the property owner's action to increase impervious surfaces on the site (by expanding the building's footprint and paving the gravel parking lot). There was also a legitimate interest in using bicycle paths to reduce traffic congestion.

However, the court then went on to "determine whether the degree of the exactions demanded by the city's permit conditions bears the required relationship to the projected impact of petitioner's proposed development.[39] The court noted conflicting standards in the lower courts, with some courts relying on generalized statements by jurisdictions regarding this relationship and other courts requiring that jurisdictions provide "a very exacting correspondence, described as the "specifi[c] and uniquely attributable" test."[40] The court concluded that the first standard was too lax and insufficient and that the second standard was too strict. It therefore adopted a middle-level test adopted by some state courts seeking jurisdictional findings that the conditions

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[37] *https://supreme.justia.com/cases/federal/us/447/255/case.html*

[38] A legislative exercise of power is a policy that applies consistently to a broad category of properties whereas an adjudicative determination is the discretionary application of a policy to the situation of a particular property. Thus, enacting a zoning regulation or setback requirement, applicable to many properties would be "legislative." But a determination applying the zoning or setback requirements to a particular property would be adjudicative.

[39] Dolan at 388. Referencing *Nollan, supra,* at 834, quoting *Penn Central Transp. Co.* v. *New* York City, *438 U. S. 104*, 127 (1978). ("A use restriction may constitute a 'taking' if not reasonably necessary to the effectuation of a substantial government purpose.") *https://supreme.justia.com/cases/federal/us/438/104/case.html*.

[40] Dolan at 389.

imposed on development bore a "reasonable relationship" between the impact of development and the burden of the required dedication.[41] The court shied away from this language because it thought that "reasonable relationship" sounded too much like (and could be confused with) "rational basis," which is a very lax standard of review. [42]

Therefore, the court chose "rough proportionality" to indicate that a jurisdiction must make an individual determination about proportionality for each burdened property without requiring the jurisdiction to provide exact mathematical proof. And here, the burden of proof rests with the jurisdiction, not the plaintiff. The court justifies this shift by noting that generally applicable legislative regulations should be treated with more deference than property-specific adjudicative determinations.

## KOONTZ V. ST. JOHNS RIVER WATER MGMT. DIST., 570 U.S. 595 (2013)

Koontz owned about 15 acres of undeveloped land in Florida east of Orlando. He wanted to develop about 3.7 acres. Pursuant to Florida's Water Resources Act and the Warren S Henderson Wetlands Protection Act, Koontz needed a permit from the St. Johns River Water Management District, which could impose "such reasonable conditions" on the permit as are "necessary to assure" that construction will "not be harmful to the water resources of the district" and that any damage to wetlands be offset by creating, enhancing, or preserving wetlands elsewhere.[43] Koontz, in his permit application, offered to create a storm water retention pond (to handle runoff from the building and parking lot). Koontz also offered a conservation easement to preclude future development of the remaining 11 acres of the site. Because the 11 acres being offered for preservation were already an existing wetland, the district found it insufficient as mitigation for the wetlands being impaired. The district denied the permit request and proposed two alternatives. Koontz could either:

1. Reduce the development site to one acre and provide a conservation easement for the remainder
2. Proceed with the 3.7-acre development, create a conservation easement for the remainder, and pay contractors to either
    a. Replace culverts on a parcel of District-owned land or
    b. Fill in ditches on another parcel of District-owned land
    c. Accomplish something equivalent to "a" or "b."

Actions related to 2.a or 2.b would improve about 50 acres of district-owned wetlands. Koontz filed suit seeking relief under Fla. Stat. §373.617(2), which allows owners to recover monetary

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[41] Dolan at 390

[42] Dolan at 391

[43] Koontz at 597 citing the Florida Water Resources Act, 1972 Fla. Laws §4(1), at 1118 (codified as amended at Fla. Stat. §373.413(1)) and the Warren S. Henderson Wetlands Protection Act, 1984 Fla. Laws ch. 84–79, pt. VIII, §403.905(1), pp. 204–205.

damages if a state agency's action is "an unreasonable exercise of the state's police power constituting a taking without just compensation."[44] Koontz contended that the demands were unreasonable pursuant to the *Nollan-Dolan* standards. [45,46]

By deciding the case in favor of Koontz, the court expanded Nollan-Dolan in two respects:

- Nollan-Dolan standards could be applied to impact fees and not merely to physical invasions such as land dedications or easements.
- Nollan-Dolan standards would apply not only to a permit that was granted with onerous conditions, but also to a permit that was denied or being negotiated with onerous conditions, provided that those conditions were in the form of a specific and concrete demand.

### KNICK V. TOWNSHIP OF SCOTT, PENNSYLVANIA, NO. 17-647, 588 U.S. (2019)

Before this case, a property owner was required to exhaust State court remedies before filing a suit in federal court for a violation of the Fifth Amendment. In this recent decision, the Supreme Court removed this requirement, thereby making it easier for property owners to access the Federal court system.

## Analysis of the Case Law

In this subsection of the report, key holdings of the Supreme Court are provided, along with questions and tips to help communities ensure that their exactions and special assessments are valid with respect to these holdings.[47,48]

The court cases in *Nollan*, *Dolan* and *Koontz* involve exactions. Typically, Supreme Court decisions are narrowly tailored and applicable only to the facts of a particular case. Therefore, the analysis that follows is tailored to exactions. But similar rules apply to special assessments. Special assessments are levied on the basis that a governmental body is providing a special

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[44] Koontz at 599

[45] Timothy Mulvaney, "The State of Exactions," William & Mary Law Review, Volume 61 Issue 1 (October 2019) pp 169-221 at 179. *https://wmlawreview.org/sites/default/files/Mulvaney-State%20of%20Exactions-Final.pdf*

[46] Id at 179 (see footnote 36)

[47] Insights and ideas for this section are provided by John J. Delaney, Exactions, Dedications and Impact Fees: Applicability of Nollan-Dolan Rough Proportionality Requirements to Non-Possessory Exactions And Exactions Imposed by Legislative Enactment, an outline prepared for the ALI-ABA Land Use Institute, Boston, August 19, 2000. *http://www.impactfees.com/publications%20pdf/delaneyI.pdf* ; and also by Timothy Mulvaney, "The State of Exactions," William & Mary Law Review, Volume 61 Issue 1 (October 2019) pp 169-221. *https://wmlawreview.org/sites/default/files/Mulvaney-State%20of%20Exactions-Final.pdf*

[48] Regarding TIF, there must be a relationship between an infrastructure improvement project and future development. This relationship has not been adjudicated by the Supreme Court. It is defined in the context of the but-for test and is discussed in the next section of this report.

benefit to identifiable properties and is merely seeking compensation for costs incurred to confer that benefit. Therefore, the concepts of nexus and proportionality apply. Essentially, governmental bodies make findings to show that infrastructure projects will confer a benefit on a particular property or set of properties (nexus) and that the special assessments are proportional to the benefits received or the costs incurred to create the benefit (proportionality) and do not exceed either the value of the benefit or the costs incurred in their creation, whichever is less.[49]

## Foundation for Takings

A land use regulation does not effect a taking if it "substantially advance[s] legitimate state interests"[50] and does not "den[y] an owner economically viable use of his land."[51]

### SUBSTANTIALLY ADVANCE LEGITIMATE STATE INTERESTS

Are the goals related to a jurisdiction's powers as delegated by the state? In particular, are the goals related to the health, safety, and welfare of the community? Is there an "essential nexus" between these goals, the actions of private parties, and the regulations or exactions imposed upon them? This is the Nollan test.

Are the burdens imposed on a property owner (particularly in an adjudicative setting) "roughly proportional" to the harm or burden created by the property owner upon the larger community? This is the Dolan Test.[52]

If a case appears to be within the Nollan-Dolan framework, is the regulation or exaction "legislative" or "adjudicatory?" A legislative regulation or exaction would be a policy affecting many properties, a type of property or a type of situation. An adjudicative regulation or exaction would be the application of a policy to a particular property under particular circumstances. If

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[49] Eugene Mcquillin, *The Law of Municipal Corporations* [section] 38:39 (3d ed., 2008). See also "The Seattle Waterfront Local Improvement District," Miller Nash Graham & Dunn Attorneys at Law, October 30, 2013. *http://www.millernash.com/the-seattle-waterfront-local-improvement-district-lid-10-30-2013/*

[50] *Agins* v. *City of Tiburon*, *447 U. S. 255*, 260 (1980). *https://supreme.justia.com/cases/federal/us/447/255/case.html*

[51] *Keystone Bituminius Coal Assn*. v. *DeBenedictis*, 480 U.S. 470, 484-485 (1987)

[52] In this context, Albuquerque, New Mexico, has an impact fee ordinance that developers must pay to offset the costs of needed infrastructure such as roads, drainage, parks, and public safety facilities. To satisfy the exaction requirement, the property owner could pay money, build the improvements, or give the city property. If the value of these exactions was more than the impact fees due, the developer would receive credits that could be used to pay for future impact fees, sold to others, or in some cases, exchanged with the city for cash. The credits expire after seven years. See Robert H. Thomas, "NM App: No Property in Impact Fee Gift Card," October 6, 2020. *https://www.inversecondemnation.com/inversecondemnation/2020/10/nm-app-no-property-in-impact-fee-gift-card.html*

legislative, deference is shown to the jurisdiction and the burden of proof is on the property owner plaintiff.[53] If adjudicatory, the burden is on the jurisdiction to prove essential nexus and rough proportionality.

Is the condition imposed on potential development possessory or nonpossessory? In the decisions mentioned above, the Supreme Court appears to use heightened scrutiny and defer to the property owner where the condition imposed on the property owner is possessory—as was the case in both Nollan and Dolan.

Possessory conditions include easements and dedications of land or waterways. These conditions infringe on an owner's ability to exclude others, which the court holds to be a fundamental aspect of property ownership. Nonpossessory conditions include impact fees, mitigation fees, and fees in lieu of land dedication.

Koontz, however, broke new ground by applying the Nollan-Dolan tests to nonpossessory interests (impact fees). Therefore, when imposing any condition on development or property utilization, it is prudent to always demonstrate an essential nexus between a legitimate State interest and the impacts or consequences of property owner actions *and* to ensure that the burden placed on the property owner is roughly proportional to the impacts being avoided or mitigated.

## DENY AN OWNER ECONOMICALLY VIABLE USE OF HIS LAND

This invokes the three-part balancing test discussed in Penn Central:

- The character of the governmental action
- The economic impact of the regulation upon the claimant

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[53] In a Florida case, an agency demanded an exaction related to "reclaimed water" for all new subdivisions. In this respect, the exaction appeared to be more legislative than adjudicative because it was applied across the board and not in relation to the specific conditions of any particular development. Yet, the Florida District Court of Appeals applied heightened scrutiny in lieu of a rational basis review. Nonetheless, the court found that Polk County met both the nexus and proportionality tests. "Highlands applied for a permit to develop a subdivision consisting of sixty residential lots as well as common areas. The County required the installation and dedication of reuse improvements in the subdivision that will be used by the future residents for landscape irrigation. The conditions imposed by the County are directly related to the impact of the subdivision on the state's water resources and do not impermissibly reach beyond that impact. The fact that reclaimed water was not available for two years, requiring Highlands to use potable water to irrigate the landscaping in its common areas during that time, does not alter the conclusion that the reuse improvements have a rough proportionality to the impact of the development. The unavailability of reclaimed water for the common areas for a period of two years is insignificant in comparison to the availability of reclaimed water for the indefinite future of the entire sixty-lot subdivision." Highland-in-the-Woods, LLC v. Polk County, No. 2D15-2801 (Apr. 28, 2017) as reported by Robert H. Thomas in his blog: "Fla App: A Sorta-Legislative Exaction Is Subject to Nollan-Dolan, But This One Passed the Test," April 28, 2017.
*https://www.inversecondemnation.com/inversecondemnation/2017/04/fla-app-a-sorta-legislative-exaction-is-subject-to-nollan-dolan-but-this-one-passed-the-test.html*

- The extent to which the regulation has interfered with property owner's distinct investment-backed expectations.

The *Penn Central* decision does not appear to provide any criteria or standards against which this balancing can be assessed. If a regulation or exaction denies all economically viable uses, however, then per Lucas, no balancing of interests is required because the regulation is a per se taking.[54]

Does repeated denial of a permit application, without the imposition of easements, dedications, or impact fees constitute a taking under Koontz? A jurisdiction can exercise its discretion in denying a permit. As long as failure to comply with impermissible conditions is not the reason for the denial, as of yet there is no Supreme Court case indicating that the denial of a permit, by itself, constitutes a taking.

## PROCEDURAL NOTE

In *Williamson County Regional Planning Commission v. Hamilton Bank of Johnson City*,[55] the court ruled in 1985 that property owners could not file a taking case in federal court until they had exhausted their remedies in state courts. The court overruled this procedural holding in *Knick v. Township of Scott, Pennsylvania*, No. 17-647, 588 U.S. (2019).

[54] *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003 (1992) at 1014-1019. Regulations that deny the property owner all "economically viable use of his land" constitute one of the discrete categories of regulatory deprivations that require compensation without the usual case specific inquiry into the public interest advanced in support of the restraint.

[55] *Williamson County Regional Planning Commission v. Hamilton Bank of Johnson City*, 473 U.S. 172 (1985)

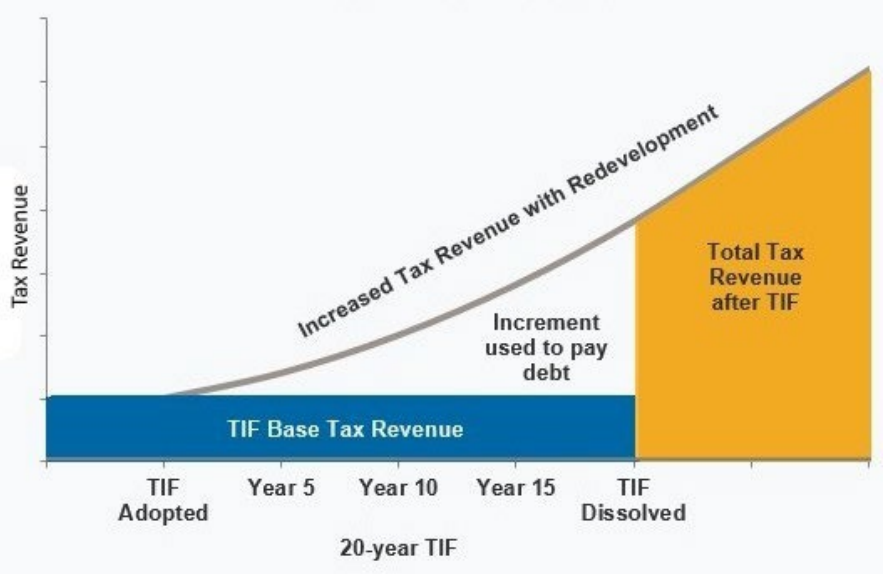
# Tax Increment Financing and the But-For Test

## What is Tax Increment Financing?

Another approach to value capture involves tax increment financing (TIF). In economically distressed areas, infrastructure improvements might be necessary to induce development. Yet, because of economic distress and a lack of economic activity, revenues may not be available for making such improvements. TIF was created for such situations. The concept is simple:

- Specified tax revenues in an eligible designated area are benchmarked prior to any infrastructure improvement.
- After infrastructure improvements have commenced, any revenue from this area up to the benchmarked amount continues to be deposited into that jurisdiction's general fund. However, any increase in revenue in this area above the benchmarked amount (or a designated portion of such an increase) is defined as the "tax increment." This increment is deposited into a special account in lieu of the general fund.
- The tax increment revenues, deposited into the special account are used exclusively for infrastructure improvements to benefit the properties and businesses in that designated area (TIF district).

**Figure 2. Tax Increment Financing Diagram**




*Source: Kentucky League of Cities website at* https://www.klc.org/InfoCentral/Detail/26

Revenues increase after TIF creation NOT because of higher tax rates, but because of increased development and economic activity that are subject to the existing tax rates. In this illustration, benchmarked public revenues would have remained constant if the public infrastructure project had not been undertaken. This might be true under certain circumstances,

but under other circumstances, benchmarked revenues might decline in the absence of the project or they might increase—but by a smaller amount than if the project were undertaken. The definition of the tax increment can and should be refined to reflect the actual circumstances in a particular place at a particular time.

TIF supporters claim that infrastructure improvements are being paid for by revenue from economic development that would not occur without these improvements. Therefore, these infrastructure improvements appear to be self-financing. In other words, TIF is an example of value capture whereby a portion of private economic gain, created by public infrastructure investment is returned to the public sector to pay for that public infrastructure.

This relatively simple funding/financing technique rests on three primary assumptions:

- Absent an infrastructure improvement project(s), economic development would not occur in the TIF district.
- Without new development, public revenues would remain unchanged or decline into the future.
- Infrastructure improvement project(s) are necessary for private development to occur. In other words, the new development that generates the tax increment would not occur but-for the infrastructure improvement project(s) being paid for by the tax increment.

Based on these assumptions, TIF-funded infrastructure projects can be funded without reducing spending on existing programs or projects and without increasing tax rates. Taxpayers are subject to the same tax rates regardless of whether a TIF is implemented or not. It is only the increase (increment) in revenue, derived from increased economic activity, that funds the TIF portion of an infrastructure project. The ability to fund infrastructure projects without competitive spending or tax rate increases is politically advantageous. As a result, this technique has become very popular.[56] The popularity of TIFs can be seen in Figure 3, which shows the growth in the number of TIF districts and TIF revenue in Chicago from 2001 until 2019.[57] The figure shows the changing number of TIF districts in Chicago while also showing total property tax revenue allocated to the general fund and total property tax revenue dedicated to TIF districts.

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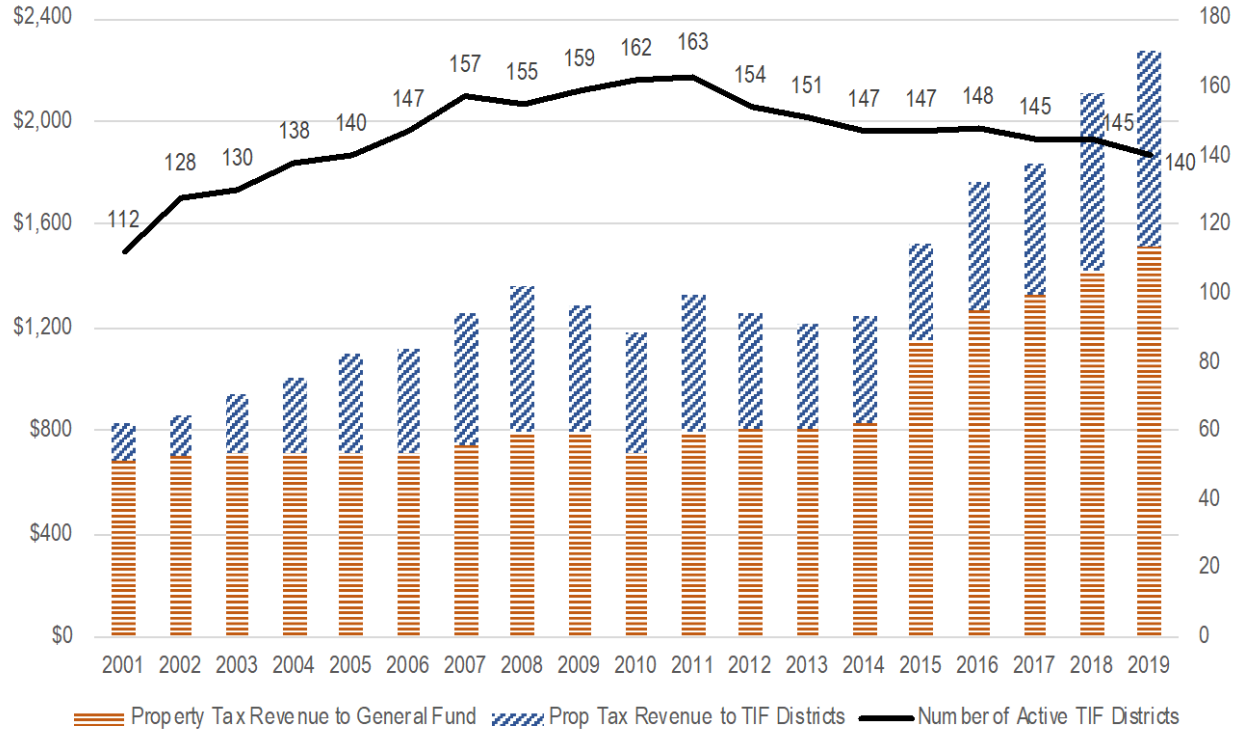
[56] See also Bridget Fisher, Flávia Leite and Lina Moe, "*TIF Case Studies: California and Chicago*," Schwartz Center for Economic Policy Analysis, The New School, August 20, 2020. *https://www.economicpolicyresearch.org/insights-blog/tif-case-studies-california-and-chicago*

[57] Citizens Budget Commission, "*Tax Increment Financing: A Primer*," December 5, 2017. *https://cbcny.org/research/tax-increment-financing-primer*

**Figure 3. Property Tax Revenue Directed to TIFs and to Chicago's General Fund, Fiscal 2001–2019**




*Source: Sean McCarthy,* Tax Increment Financing in Arizona*, ATRA, 2017, p. 2.*
http://www.arizonatax.org/sites/default/files/publications/special_reports/file/tif_in_arizona.pdf

The widespread use of TIFs has generated concerns that TIF revenues might be reducing general fund revenues and thereby depriving public services of funding. This concern has focused attention on TIFs' underlying assumptions.

Assumption number one is that tax revenues in the affected area will not increase but-for the improvement of specified infrastructure which will catalyze private sector development and other economic activity. If this assumption is not true, and tax revenues would have increased anyway, then a TIF deprives the general fund of revenues and diminishes resources for existing projects and programs.[58] For this reason, some state enabling statutes limit TIFs to blighted areas where development is not otherwise occurring.[59]

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[58] Schwartz Center for Economic Policy Analysis the New School, "*TIF Case Studies: California and Chicago*," August 20, 2020 *https://www.economicpolicyresearch.org/insights-blog/tif-case-studies-california-and-chicago* .

[59] Benjamin Scheider, "*City Lab University: Tax Increment Financing*," October 24, 2019 at *https://www.bloomberg.com/news/articles/2019-10-24/the-lowdown-on-tif-the-developer-s-friend* .

Although some parcels reside in a single taxing jurisdiction, other parcels might exist in multiple taxing jurisdictions. For example, a property might receive a single property tax bill including taxes to be paid to a city, a county, a State, a school district, a water and sewer district, and a road improvement and maintenance district. Typically, only one of these tax authorities is authorized to implement a TIF, but implementing a TIF could potentially affect revenues for these other taxing authorities. Where multiple taxing authorities exist, the process for creating a TIF might be more complex and controversial. This complexity is not insurmountable. It does, however, require more outreach, negotiation, and possibly inter-jurisdictional agreements to protect each jurisdiction's interests.

Assumption number two is that increases in development and economic activity will yield sufficient additional tax revenues to fund the specified infrastructure improvements. If this assumption is false, then either additional funding sources will be required to repay the debt or infrastructure project lenders won't be repaid. If additional funding sources are required, then in all probability the infrastructure project will compete for funding with other projects and programs.

Assumption number three is that new growth induced by the TIF will not generate new demands for increased government-funded facilities or services other than the TIF-funded project. Some types of development catalyzed by a TIF may not place additional demands on government-funded infrastructure and services like schools, parks, traffic management, police, fire and EMS services, hospitals, water supply, waste treatment, etc. However, if a TIF generates an increased demand for these public facilities or services, TIF-designated revenue sources will not cover their costs.[60] Consequently, supplemental funding for the general fund or general fund access to a portion of the tax increment may be justified and equitable. Some jurisdictions have modified their TIF enabling legislation to accommodate such arrangements.[61]

Assumption number four is that increases in development and economic activity in a TIF district are not displacing or inhibiting growth in another location. If this assumption is false, then revenue might increase in a TIF district but might not grow as fast or might actually decline in another location as a result of the TIF-induced growth.[62] Consequently, overall net revenues might not grow as much as they might appear to be based only on a review of revenue in the TIF district. This is particularly relevant if different governmental jurisdictions are involved and competing for growth and development using TIF as a growth inducement.

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[60] See graphics and explanatory notes in the Appendix to this report.

[61] Cook County, Ill., "*Chicago City Transit TIF Fact Sheet"*. *https://www.cookcountyclerk.com/sites/default/files/pdfs/2017 Transit TIF RPM1 Fact Sheet_0.pdf*. See also Bridget Fisher et al., "*TIF Case Studies: California and Chicago*"

[62] Sean McCarthy, *Tax Increment Financing in Arizona*, (ATRA) 2017, p 3. *http://www.arizonatax.org/sites/default/files/publications/special_reports/file/tif_in_arizona.pdf*

Shifting development from one location to another location might be valuable and satisfy a legitimate public purpose. But it won't satisfy the assumption that the tax increment would not exist but for the TIF project.

## The But-For Test

Most States authorize TIF.[63] The only exceptions appear to be Arizona and Puerto Rico. However, each State's TIF legislation is unique. Some TIF-authorizing statutes might limit the creation of TIFs to projects that are necessary to catalyze increases in economic activities and resulting tax revenue. This is known as the but-for test:

- Is the proposed TIF infrastructure project necessary to generate increased economic activity and tax revenues in the TIF district?
- But for the TIF project, economic development would not occur in this location.

Imagine that a jurisdiction's legislature is considering spending taxpayer dollars on an infrastructure project that will confer a significant benefit on a few property owners or businesses. In all probability, such a proposed project, funded out of the jurisdiction's general fund revenues, would be opposed because public tax dollars should not be spent to benefit private entities. TIF solves the problem of using public funds for private gain by claiming that, but for the infrastructure project, these public tax revenues would not exist. In other words, economic activity generated by the project, that would not otherwise exist, will produce the revenue used to fund or finance the project. This but-for claim suggests that the project is paying for itself, and not transferring wealth from the public sector to the private sector.[64]

## Does the But-For Test Ensure Equity?

Does the but-for test create equity by ensuring that new development pays for itself? Typically, taxpayers in a TIF district pay taxes at the same rate as they would if the TIF district did not exist. When new development occurs, it often requires additional public goods and services. The taxes paid by new developments (the tax increment) typically cover a portion of the new operating expenses associated with these additional public goods and services. But, when a TIF district is created, the tax increment is dedicated to fund a particular infrastructure project and is therefore unavailable to cover increased costs for providing other public goods and services to

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[63] Council of Development Finance Agencies. (2015). *Tax Increment Finance State-by-State Report: An Analysis of Trends in State TIF Statutes*. *https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=201601-TIF-State-By-State.html*. Accessed September 8, 2020.

[64] Not all state statues require the but-for test.

new developments in the district for the duration of the TIF, which can be a substantial number of years.[65] This can create hardships for other agencies affected by TIF induced growth.

In 1972, concerns that California TIFs were depriving schools of property tax revenue were addressed when the State promised to reimburse school districts for lost TIF revenues.[66] More recently, in 2016, Chicago created a TIF for transit. This TIF was structured so that Chicago Public Schools would receive their proportionate share of TIF revenues (based on their share of regular property tax revenue). Of the remainder, 80 percent would go to the Transit TIF and 20 percent to other taxing districts.[67] And, in some States, the State TIF-enabling statute mandates approval from other tax districts when an overlapping taxing authority creates a TIF potentially impacting their revenue.[68] These types of modifications to the TIF structure could provide for greater equity and political support.

The preceding paragraphs raise a concern that new developments in a TIF district might not pay their fair share of government operating expenses. And, if new developments create a need for new infrastructure capacity, then the new developments would not be paying for this capital expense either.[69] Thus, the mere fact that a development generates tax revenue that would not otherwise exist (thereby satisfying the but-for test) does not mean that a TIF will not have an adverse impact on a jurisdiction's existing public goods and services.

A Public Policy Institute of California study compared 38 California TIF districts to similar areas without TIFs. Because baseline tax assessments increased in the non-TIF areas during the same time period, only four TIF districts were found to generate enough new revenue to be self-financing.[70] This implies a need for equity adjustments. Therefore, to avoid or minimize diverting funds from existing public goods and services, some TIF laws require a finding that increased tax revenues within a TIF district (the tax increment) would not exist but for (in the absence of) the infrastructure project being funded by the tax increment revenues.

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[65] Benjamin Scheider, "City Lab University: Tax Increment Financing." Bloomberg CityLab. October 24, 2019. *https://www.bloomberg.com/news/articles/2019-10-24/the-lowdown-on-tif-the-developer-s-friend*.

[66] Bridget Fisher et al., "*TIF Case Studies: California and Chicago*" Schwartz Center for Economic Policy Analysis The New School, August 20, 2020. *https://www.economicpolicyresearch.org/insights-blog/tif-case-studies-california-and-chicago*

[67] Cook County, Ill., *Chicago City Transit TIF Fact Sheet*. *https://www.cookcountyclerk.com/sites/default/files/pdfs/2017 Transit TIF RPM1 Fact Sheet_0.pdf*

[68] Bridget Fisher et al., "*TIF Case Studies: California and Chicago*." *https://www.economicpolicyresearch.org/insights-blog/tif-case-studies-california-and-chicago*

[69] For an elaboration, see discussions about development impact fees, especially FHWA, *Value Capture Implementation Manual, Section 4, "*Developer Contributions." *https://www.fhwa.dot.gov/ipd/value_capture/resources/value_capture_resources/value_capture_implementation_manual/ch_4.aspx*

[70] Michael Dardia, *Subsidizing Redevelopment in California*, (Public Policy Institute of California) January 1998, p xiii. *https://www.ppic.org/content/pubs/report/R_298MDR.pdf*

Even if infrastructure investment increases land values, property owners are paying taxes at the same rate they would otherwise pay in the absence of a TIF. Thus, "value capture" is limited to what these taxes would accomplish even in the absence of a TIF. Although property tax rates vary from place to place, the national average is about one to two percent of value paid annually.[71] A present value calculation shows that such a tax on a long-lived asset (like land) in an economic environment where interest rates are five percent returns between 20 percent and 40 percent of the publicly created land value.[72]

Thus, to the extent that infrastructure investments lead to higher land values, the lion's share (60 percent to 80 percent) end up as windfall gains to affected landowners. Given concerns over growing inequality, spending public funds to benefit private landowners might be difficult to justify. This explains why many property owners and developers lobby for TIF creation. In the final analysis, TIF might be accurately described as "revenue segregation" rather than as "value capture."[73]

Of course, a TIF project might lead to new development activity. Thus, in addition to taxes on increased land value, new development in a TIF district will be contributing additional revenues related to the value of new buildings and the taxable economic activities that occur in them. As mentioned previously, new buildings and economic activity will place demands on public goods and services. Tax revenues derived from new buildings and economic activity subject to a TIF will not be available to pay for these public goods and services until TIF termination—generally between 15 and 30 years from TIF inception. Some states have modified their enabling legislation to address this.

In Minnesota, the State statute governing TIFs mandates a test to determine whether a proposed TIF district satisfies Minnesota's but-for requirement:[74]

- The development would not happen solely through private investment in the "reasonably foreseeable future."

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[71] Alan Mallach, *The Divided City: Poverty and Prosperity in Urban America,* Island Press 2018, p 164.

[72] Present value for a perpetual stream of income or expense = Annual income (or expense) / interest rate. Thus, a perpetual payment of $2 has a present value of $2/.05 = $40. So if a landowner receives $100 in publicly created land value and must pay an annual $2 fee (the present value of which is $40), then the landowner is receiving $100 minus $40 (the present value of tax payments), leaving a $60 (60 percent) windfall gain.

[73] NCHRP Report 873, "*Guidebook to Funding Transportation Through Land Value Return and Recycling*," p 17. *http://www.trb.org/Main/Blurbs/177574.aspx*. See also David Merriman, "*Improving Tax Increment Financing (TIF) for Economic Development*," (Lincoln Institute of Land Policy) 2018, p 12. *https://www.lincolninst.edu/sites/default/files/pubfiles/improving-tax-increment-financing-full.pdf*

[74] Minnesota House Research Department, "*The But-For Test*," *https://www.house.leg.state.mn.us/hrd/issinfo/tif/butfor.aspx*, accessed Oct. 25, 2020.

- The induced development will yield a net increase in market value for the site compared to the likely development that would occur without TIF. To determine this:
    a. Determine the increase in market value of the site that would reasonably be expected to occur without using TIF. [Estimated future market value (at the end of the TIF period) minus current market value.]
    b. Determine the increase in market value of the proposed TIF development, minus the present value of the TIF assistance. [Estimated future market value (at the end of the TIF period) minus current market value minus the value of the TIF assistance.]
    c. There is no net increase in market value if the value of b. is less than or equal to the value of a.

## Litigation of the But-For Test

The previous section highlights concerns raised in articles that challenge the validity and equity of the but-for assumption in certain instances. Perhaps more importantly, due to the proliferation of TIFs in California and the perception that TIFs were depriving school systems of revenue, the California legislature took the following steps:

California eliminated TIFs in 2012. In 2014, California replaced TIFs with Enhanced Infrastructure Finance Districts (EIFDs). EIFDs are allowed to issue TIF-type debt. But EIFD debt is subject to more stringent limitations including:

- EIFD revenues are not drawn from taxes that fund schools
- Approval is obtained from any affected tax district
- Voter approval to issue EIFD bonds is obtained.[75]

So concerns exist about the but-for test that have generated academic studies and articles. And, in some places, like California, they have generated legislative reform. But what about litigation?

Unlike special assessments, exactions, or impact fees, TIFs do not impose a special or additional tax burden on properties that benefit from the government assistance projects. Thus, affected property owners are not motivated to challenge TIFs in court. To the contrary, property owners often support TIFs because, while paying taxes that they would pay in any event, a TIF dedicates funding for infrastructure projects that will provide them with a special benefit.[76] For

[75] Bridget Fisher, Flávia Leite and Lina Moe, "*TIF Case Studies: California and Chicago*," Schwartz Center for Economic Policy Analysis The New School, August 20, 2020. *https://www.economicpolicyresearch.org/insights-blog/tif-case-studies-california-and-chicago*

[76] Sean McCarthy, *Tax Increment Financing in Arizona*, (ATRA) 2017, p 2. *http://www.arizonatax.org/sites/default/files/publications/special_reports/file/tif_in_arizona.pdf*

this reason, there has not been as much litigation regarding TIFs as there has been regarding exactions and special assessments.

Nonetheless, some parties can be aggrieved by the creation of a TIF. Taxing districts (such as school districts) might believe that a TIF designation will deprive them of revenue for the life of a TIF. As mentioned earlier, this can be as long as 25 or 30 years. Therefore, a taxing district that could lose revenue might have both an interest in challenging the legality of a TIF as well as the resources for undertaking such a lawsuit.

Businesses might be motivated to challenge a TIF if they are located in a building that a TIF-subsidized redevelopment plan will demolish, particularly if they believe that they will not be able to survive the hiatus between demolition and redevelopment or if they believe that they won't be able to afford rents (or even be offered space) in the new development.

And, in some cases, a taxpayer might sue because they challenge a municipality's exercise of its taxing and spending powers pursuant to a TIF enabling statute. Generally, a person cannot sue the United States or an individual State simply because they are a taxpayer. However, taxpayer standing has been permitted to challenge county and municipal actions in certain instances. See the *Malec* case below.

The lack of litigation related to the but-for requirement for TIFs might indicate that:

- Property owners who are financially affected by infrastructure and other types of projects undertaken pursuant to TIFs and who have the resources necessary to litigate on behalf of their financial interests are typically supportive of TIFs and therefore unlikely to sue, even if a legislative prerequisite has not been satisfied.
- People or groups who have an interest in maintaining revenue for a jurisdiction's general fund:
  - Accept putative claims that the but-for requirement has been met
  - Lack an ability to prove that the but-for requirement has not been met
  - Lack the resources to engage in litigation
  - Lack standing to litigate this issue.

There are not as many cases litigating TIFs as there are litigating special assessments and exactions. The research team was unable to find any TIF but-for litigation that had been decided by the U.S. Supreme Court. The cases summarized below are from State appellate courts.

## *BOARD OF EDUCATION* V. *THE VILLAGE OF BURR RIDGE* (2003) AND THE NEED TO DOCUMENT THE BUT-FOR REQUIREMENT

In 1997, Illinois enacted the Tax Increment Allocation Redevelopment Act (TIF Act).[77] This act enables a municipality to eliminate blighted conditions within its boundaries by allowing the municipality to collect real property tax increment revenues from local taxing districts such as schools, park, sanitary and fire districts located in the TIF district and use these revenues to fund TIF development projects or other ancillary expenses in the TIF district.

The Village of Burr Ridge in Cook County, Illinois, created a TIF ordinance to facilitate the development of a vacant 85-acre parcel in 1998. After several experts had determined that the parcel did not qualify for TIF designation, the village hired a consultant to prepare a TIF eligibility study and redevelopment plan. The study found that pursuant to the TIF Act, growth and development of the parcel had been impeded by four blighting factors: diversity of ownership, flooding, obsolete platting, and tax delinquencies. Village counsel reviewed the study and informed the village that compliance with statutory requirements was marginal. A review board concluded that the parcel did not qualify for a TIF designation because it did not satisfy the statutory requirement for blight. Subsequently, the Village Board of Trustees enacted ordinances designating the parcel as a TIF district and approving the redevelopment plan.

The school district sued and claimed that the village's ordinances did not comply with the provisions of TIF Act because the village's legislative findings of blight made in the ordinances were erroneous and not supported in fact. [78] The school district claimed that if the TIF ordinances were implemented and the attendant redevelopment plan and project allowed to proceed, the school district and other overlying taxing districts would be irreparably harmed by the illegal and improper diversion of tax revenues from their taxing districts. The school district sought an order declaring that the ordinances were void as a matter of law and an injunction preventing the village from implementing the ordinances and selling bonds or undertaking any obligations or making expenditures pursuant to the ordinances.

With regard to motions for summary judgement, the village presented the eligibility study and its author. The school district presented an urban planning expert who relied upon the guidelines promulgated by the Illinois Department of Revenue as set forth in the 1988 TIF compliance manual (TIF Guide) that is commonly relied on by experts and courts in interpreting the TIF Act.

The trial court entered an order granting the school district's motion for summary judgment on the ground that the subject property did not contain any of the blighting factors necessary to qualify it for TIF designation under the TIF Act. The village appealed. The Appellate Court of Illinois affirmed the trial court's decision.

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[77] Tax Increment Allocation Redevelopment Act (TIF Act) (65 ILCS 5/11-74.4-1 *et seq.* (West 1994))

[78] Board of Education, Pleasantdale School District No. 107, Cook County Illinois v The Village of Burr Ridge, 793 N.E.2d 856, 341 Ill. App.3d 1004, 276 Ill. Dec. 97 (Ill. App. 2003)

In order for the parcel to be deemed blighted, the village was required to establish that the growth and development of the property as a taxing district was impaired by a combination of two or more statutory blight factors. The blight factors are:

- "Obsolete platting" of the vacant land
- Diversity of ownership of such land
- Tax and special assessment delinquencies on such land
- Flooding on all or part of such vacant land
- Deterioration of structures or site improvements in areas adjacent to the vacant land.[79]

The trial court noted that deference is given to legislative findings. When reviewing the eligibility report, however, the court found no fact that established blight according to guidelines in the TIF compliance manual. The expert's assertion that the facts were sufficient did not make them so.

The trial court also found that development of the parcel would occur without the aid of TIF designation. The TIF Act requires a showing that the parcel "would not reasonably be anticipated to be developed without the adoption of the redevelopment plan."[80] This is the but-for test. The trial court was aware that development of the parcel had languished, but there was no evidence that this stagnation was attributable to any alleged blighting factors on the parcel but, rather, was due to the tax disparities between Cook and DuPage counties. The trial court also noted that, in spite of the large tax impediment, a 30-screen movie complex and a residential townhome development had been proposed for the parcel but had been denied by the Village Planning Commission after a large number of residents campaigned against the two projects.

This case highlights the importance of understanding and complying with the TIF-enabling statute and with official guidance documents. It also shows that, where a but-for requirement exists, there must be documentation to show compliance.

## *MALEC* V. *THE CITY OF BELLEVILLE* (2011) AND THE RURAL VS. URBAN CONTEXT

The City of Belleville procured a TIF eligibility study and redevelopment plan for several contiguous parcels comprising about 150 acres. Based on findings in the eligibility study, Belleville enacted ordinances creating a TIF district for the parcel for the purpose of creating new residences and a shopping center. In this case, Mr. Malec, a taxpayer, challenged the validity of the TIF ordinances and an accompanying economic incentive agreement for the shopping center portion of the parcel, contending that land that is being actively farmed should not qualify as "vacant" or "blighted" pursuant to the Illinois TIF Act.[81] In addition to the farming activity, there were five or so vacant structures on about 2.5 acres of the parcel and there was a

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[79] 65 ILCS 5/11-74.4-3(a) (West 1994).

[80] 65 ILCS 5/11-74.4-3(n)(J)(1) (West 2002).

[81] Malec v. the City of Belleville, 943 N.E.2d 243, 407 Ill.App.3d 610, 347 Ill.Dec. 953 (Ill. App. 2011)

risk of subsidence due to an abandoned, underground mine beneath the site. The roads adjacent to the site were also deemed to be insufficient for the daily traffic volume.

The TIF Act specifically exempts farmland from being classified as "vacant" for the purpose of satisfying the criteria for "blight." [82] However, the TIF Act was amended to make an exception for farmland that had been subdivided. The parcel had been subdivided over the years, although it remained under the control of one or two families who, by oral agreement, leased the land to a farmer. The economic incentive agreement statute, however, does not define "vacant" nor make an exception for farmland.

The trial court and appellate court agreed that the land was vacant for the purposes of the TIF act. They recognized that TIFs and economic incentive agreements were created for urban development and, in that context, land without structures is "vacant." They buttressed their decision based on the subdivision of the property. They noted that the TIF statute did not address whether blighted structures on a parcel constituted a significant or preponderant characteristic of the parcel. Therefore, they declined to insert any such qualification. They also agreed that the weight of the evidence showed that the land would not be developed for commercial purposes but for the TIF arrangement to remediate the abandoned mine to reduce the risk of subsidence.

The dissenting appellate judge investigated the amendments allowing farmland to be classified as vacant if the farmland had been subdivided. The judge noted that these amendments were "special legislation designed to validate specific pork barrel TIF projects in Illinois."[83] This judge argued that the presence of blighted buildings on 2.5 acres of the site did not permit the remainder of the site to be classified as "blighted." The dissenting judge noted that there was both residential and commercial development nearby that occurred despite the presence of abandoned mines and a risk for subsidence in those areas also. Therefore, the dissenting judge disagreed that the but-for test had been satisfied.

This case highlights the importance of statutory definitions and that the definition of "improved" and "vacant" property can be very different depending on whether the context is urban or rural. This distinction becomes meaningful and important particularly where rural and urban areas abut one another.

### *JG ST. LOUIS W. LIMITED LIABILITY CO.* V. *CITY OF DES PERES* (2001) AND THE RELUCTANCE OF COURTS TO CHALLENGE A LEGISLATURE'S BUT-FOR FINDING

A shopping center in St. Louis (the City) sought to attract a Nordstrom store. To do so, the shopping center requested designation as a TIF to subsidize its redevelopment. St. Louis created a TIF Commission to investigate this request. The City also hired planning consultants

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[82] Tax Increment Allocation Redevelopment Act (TIF Act) (65 ILCS 5/11-74.4-1 *et seq.* (West 1994))

[83] Malec at 347 Ill.Dec. 984, 943 N.E.2d 274.

who concluded that the area was blighted and met the "but-for" test contained in the TIF statute. The City solicited redevelopment proposals for the shopping center and the shopping center submitted the only bid. They proposed a redevelopment budget of about $212 million, of which $50 million would be provided in TIF subsidy. The City negotiated for a TIF subsidy of slightly less than $30 million. At this point, the TIF Commission and the Board of Aldermen held separate public hearings. The plaintiffs in this suit objected to the TIF designation at both hearings. [84]

The Board enacted several ordinances to adopt the redevelopment plan and authorize the TIF obligations. JG St. Louis West Limited Liability Company and others filed suit against City seeking a declaratory judgment that the four TIF ordinances were invalid, as well as seeking an injunction to prohibit the use of TIF in the redevelopment of shopping mall. Plaintiffs asserted the TIF ordinances were invalid because Board acted arbitrarily and unreasonably in declaring shopping mall to be a blighted area, in finding that shopping mall would not reasonably be developed without the use of TIF, and in approving the use of public funds for clearly private purposes.

The trial court held that City's four TIF ordinances were duly enacted and the actions of Board were not arbitrary nor induced by fraud, collusion, or bad faith. The appellate court agreed and confirmed the trial court's decision.

The Missouri statute defines "blighted area," as

> An area which by reason of the predominance of defective or inadequate street layout, insanitary [sic] or unsafe conditions, deterioration of site improvements, improper subdivision or obsolete platting, or the existence of conditions which endanger life or property by fire and other causes, or any combination of such factors, retards the provision of housing accommodations or constitutes an economic or social liability or a menace to the public health, safety, morals, or welfare in its present condition and use.[85]

The Plaintiffs argued that the shopping center was the economic engine of St. Louis. It was an asset to St. Louis and, as such, could not be blighted or characterized as a liability. However, the board also found evidence that there were statutory blighting factors present that threatened the center's future success. Neither the trial court nor the appellate court sought to evaluate the board's reasoning. It was merely sufficient to see that the board raised debatable issues and consulted a wide variety of independent information sources including field investigations, records from local sources, interviews with local officials, and other independent studies.

The but-for test, contained in section 99.810, provides in pertinent part:

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[84] JG St. Louis West Limited Liability Company, et al. v. City of Des Peres and West County Center, LLC, ED77037, Missouri Court of Appeals Eastern District, 41 S.W.3d 513 (Mo.App. E.D. 2001)

[85] Section 99.805(1) RSMo 1994

> No redevelopment plan shall be adopted by a municipality without findings that: (1) The redevelopment area on the whole is a blighted area, a conservation area, or an economic development area, and has not been subject to growth and development through investment by private enterprise and would not reasonably be anticipated to be developed without the adoption of the redevelopment plan.

Here again, the court refused to evaluate the Board's reasoning. The court noted that the Board consulted different experts with different views and made a reasoned decision. No proof was presented that the Board's action was arbitrary or induced by fraud, collusion or bad faith. Therefore, the court refused to second-guess the Board's decision that the but-for test had been satisfied.

Finally, the plaintiffs argued that applying a TIF subsidy to a privately-owned and operated parking garage was not valid because a parking garage did not constitute a redevelopment cost pursuant to the TIF statute. The statute provides a substantial set of examples of redevelopment costs, and a parking garage is not included in those examples. However, the TIF statute states that the examples are illustrative and not intended to be an exhaustive or exclusive list. The court therefore refused to find that the parking garage was not a redevelopment cost that could be eligible for TIF assistance.

### *CASTEL PROPERTIES, LTD*. V. *CITY OF MARION* (1994) AND THE INABILITY TO CREATE BLIGHT BY ASSOCIATION

The City of Marion Illinois created two TIFs (TIF 1 and Illinois Center TIF). The TIF 1 area was about 1,400 acres and consisted of about 400 properties, many of which were blighted. The Illinois Center area was a 260-acre farm less than one-half mile from the interchange between Route 13 and Interstate Highway 57. Castel Properties sued Marion claiming, in part, that the TIFs were illegal because the finding of blight was not reasonable and because the TIFs did not satisfy the but-for requirement.[86]

The adopted redevelopment plan did not address or remediate the blighted conditions on TIF 1, and the farm was acquired and subdivided immediately prior to the TIF designation. These facts created an impression that the farm/Illinois Center TIF was attached to TIF 1 merely to imply blight by association. The fact that no action was taken to rectify the blight on TIF 1 implied that this action was more about developing the farm than about rectifying blight. As noted in the Malec case, farmland cannot be classified as vacant for TIF purposes unless it has been subdivided. The subdivision of the farm immediately before the TIF designation appeared to be an illegitimate attempt to qualify the farm as vacant for TIF purposes.

[86] Castel Properties, Ltd. v. City of Marion, 631 N.E.2d 459, 259 Ill.App.3d 432, 197 Ill.Dec. 456 (Ill. App. 1994)

While deference to an elected body's determinations and findings makes overturning them difficult, it does not mean that a court must validate them if they are based on a lack of evidence or evidence deemed to be spurious.

The trial court agreed with the City of Marion regarding the designation of TIF 1 but agreed with Castel Properties about the illegitimacy of the Illinois Center TIF. The appellate court affirmed the trial court's decision. For both TIF 1 and the Illinois Center TIF, the courts showed deference to Marion's legislative findings. But, despite showing deference, the courts were not able to sustain Marion's findings regarding blight and but-for related to the Illinois Center TIF because Marion did not provide convincing evidence.[87]

## Meeting the But-For Test and Other TIF Legal Requirements

Each State's statutory TIF requirements are unique.[88] Creating and administering TIFs will adhere to the substantive and procedural requirements established by the State TIF-authorizing statute and by local laws and procedures as well. If a State has created a how-to manual for TIFs and/or has an office responsible for overseeing TIF creation and administration, these provide authoritative sources for understanding legal and regulatory issues.[89]

State TIF-enabling statutes might include the following parameters for local implementing ordinances:

- A finding that a TIF district is "blighted" and unlikely to develop without public sector intervention. If this requirement exists, localities will typically hire a consultant to conduct an eligibility study to ensure that the proposed TIF district satisfies mandated State criteria.[90]

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[87] In a Minnesota case, Walser Auto Sales v. City of Richfield, 635 N.W.2d 391 (Minn. App. 2001), a consultant used dubious methods and erroneous procedures to find "blight" within a proposed TIF district. The appellate court concluded that the municipality's desired result determined the conclusion of the blight evaluation and analysis. On this and other counts, the case was remanded to the trial court for further review and adjudication.

[88] For citations to individual State laws authorizing TIF, see *https://www.fhwa.dot.gov/ipd/value_capture/legislation/tax_increment_financing.aspx* .

[89] Minnesota has extensive online materials related to TIF formation and implementation at *https://www.house.leg.state.mn.us/hrd/issinfo/tifmain.aspx?src=21* . Montana has a TIF manual available at *https://leg.mt.gov/content/Committees/Interim/2017-2018/Revenue-and-Transportation/Meetings/Sept-2017/tif-manual-2014-cornish.pdf* .

[90] Studies indicate that TIFs have often been used in areas that wouldn't be considered as "blighted." In some cases, TIF laws have been amended to eliminate the blight requirement. See David Merriman, *Improving Tax Increment Financing (TIF) for Economic Development*, (Lincoln Institute of Land Policy) 2018, p 7.

- A finding that subsequent development within a TIF district would not occur but for the specific intervention being proposed in the TIF implementation ordinance.[91]
- A delineation of activities (interventions) that could be permissibly undertaken by localities using TIF in support of private sector development.
- Compatibility of intended TIF development with local comprehensive plans and zoning.
- A maximum duration along with procedures for extending the term (if any) and for termination.

To the extent that these requirements exist in State law, localities typically hire consultants to conduct an eligibility study to ensure that the proposed TIF district boundaries satisfy mandated State criteria and to develop a TIF implementation plan. Working in concert with the local planning officials, civil engineers and budgeting officials, this plan should ensure that the proposed interventions are consistent with State law, that they satisfy any but-for requirement, and are consistent with local plans and zoning.

After the eligibility study and implementation plan have been completed, a public hearing is held in accordance with State law and/or local legislative procedures. Notice of the hearing is provided to the public generally and to property owners within the proposed TIF boundaries in particular. After the hearing and making any warranted change to the TIF plan, the TIF creation and implementation ordinance is drafted and subjected to the legislative process for enactment.

[91] Id., pp 15-16. Studies indicate that the but-for test has often been construed very loosely.

## Determining Costs and Benefits to Apportion Infrastructure Costs Equitably

Most taxpayers pay for infrastructure creation, operations, maintenance, rehabilitation, and replacement through taxes. However, funding infrastructure with general taxes leaves consumers oblivious to the consequences of some of their actions and creates no incentive for adjusting behavior in relation to the costs and benefits of public goods or services being consumed.[92] Value-capture techniques (user fees, impact fees, and access fees), however, inform consumers about the impacts of their consumptive behavior and motivate behavior changes that takes those impacts into account.[93]

Value capture techniques, because they are more like fees (prices) and to the extent that they are properly designed and executed, can mimic market transactions, thereby generating revenue while simultaneously internalizing externalities, creating market incentives to encourage more responsible and efficient use of public resources.[94] In this way, they also create economic incentives for more efficient and responsible land use decisions.[95] In particular, this section suggests that life cycle asset management budgets, fiscal impact analysis, real estate professionals and computer-assisted mass appraisal (CAMA) software programs can provide a basis upon which to satisfy the "nexus" and "proportionality" legal tests for various exactions and special assessments. These activities can also provide a foundation for developing an array of value capture techniques, including those related to land value return, that can simultaneously raise new revenue while also motivating infrastructure consumption and land development behaviors that minimize resource consumption, pollution and per capita tax

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[92] Rick Rybeck, "*Funding Long-Term Infrastructure Needs For Growth, Sustainability & Equity*" (DC Tax Revision Commission) 2013.

[93] Id.

[94] In the context of user fees, when somebody has a leaky faucet and pays for water with a per-gallon user fee, they don't see water going down their drain, they see money going down the drain, which motivates them to fix the leaky faucet. We could pay for water with a sales tax or income tax, but this wouldn't motivate people to fix leaky faucets. In the context of impact fees, they discourage development where infrastructure is lacking (or at least obtain payment for the additional infrastructure capacity required). Likewise, in the context of infrastructure access fees, returning publicly created land values to the community encourages the development of high-value sites where infrastructure amenities are abundant.

[95] Rick Rybeck, "*Funding Long-Term Infrastructure Needs For Growth, Sustainability & Equity*" (DC Tax Revision Commission) 2013 at *http://media.wix.com/ugd/ddda66_d46304b5437c178e2f092319a6f30364.pdf* . See also Rick Rybeck, "*Financing Infrastructure with Value Capture: The Good, The Bad & The Ugly*," at *https://www.strongtowns.org/journal/2018/2/20/financing-infrastructure-with-value-capture-the-good-the-bad-the-ugly/* .

burdens while enhancing affordability (for both residents and businesses) and economic vitality (employment).[96]

After the end of World War II, appropriations from Federal and State governments began laying the groundwork for the Interstate Highway System, expanded municipal water and sewer systems, and funded other infrastructure networks that facilitated suburban development.[97] Because the infrastructure was new, operations and maintenance expenses for the local governments were relatively small. This allowed suburban jurisdictions to impose relatively modest taxes and maintain balanced budgets. But, as the infrastructure aged, operations and maintenance expenditures began to rise. And, according to the nature of particular infrastructure assets, periodic rehabilitations are undertaken until system replacement becomes necessary. When rehabilitation and replacement spending spikes occur, Federal funding is typically not available, state budgets are often tight and local revenues might be insufficient.

As suburbs grew, excess infrastructure capacity began to shrink until it was nonexistent. New development, at that point, was very expensive because its tax revenues, while sufficient to meet its share of variable operating expenses, were not sufficient to pay for infrastructure capacity expansion. During this time, development impact fees were created to help ensure that new development would pay for its share of new infrastructure capacity.[98] While this was a step in the right direction, it's difficult to see how a one-time payment for capacity expansion will adequately compensate the jurisdiction for infrastructure facilities that are a perpetual fiscal liability.

Going forward, communities can develop comprehensive life-cycle budget schedules for key infrastructure assets. They can also perform fiscal impact analyses to determine the revenue per acre generated by potential future development scenarios and compare them to the life-cycle infrastructure costs per acre in various locations. Such analysis might reveal that low-density development, is not able to sustain the substantial life-cycle infrastructure costs that it incurs.[99]

Lifecycle budgets for infrastructure combined with fiscal impact analysis can provide the basis for exactions, including development impact fees, that satisfy legal requirements for essential

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[96] Id.

[97] "Our Nation's Infrastructure," Hearings of the Joint Economic Committee, Senate Hearing 98-647 Aug/Sept 1983 (GAO) 1984, Statement of Hon. Norman Rice, pp 367-368. See also, James P. Pinkerton, A Vision of American Strength: How Transportation Infrastructure Built the United States, (American Road and Transportation Builders' Association) 2015, pp 98—105.

[98] Peter N. Brown, City Attorney, Graham Lyons, Deputy City Attorney, City of Carpinteria, "*A Short Overview of Development Impact Fees*," League of California Cities Continuing Education Seminar, February 27, 2003 at *https://www.ca-ilg.org/sites/main/files/file-attachments/resources__overviewimpactfees.pdf* .

[99] Joe Minicozzi, *The Economics of Land Use in Florida*, March 11, 2020. *https://1000fof.org/wp-content/uploads/2020/03/U3-1000-Friends-3-11-20F-web.pdf*.

nexus and rough proportionality. A number of jurisdictions have also developed detailed ordinances, procedures and manuals for computing development impact fees. For example, here are the section headings for a development impact fee ordinance in Blaine, Washington:[100]

3.80.010 Authority and purpose.
3.80.020 Findings.
3.80.030 Definitions.
3.80.040 Administration.
3.80.050 Impact fee imposition.
3.80.060 Development service areas established.
3.80.070 Traffic impact fee formula.
3.80.080 Park impact fee formula.
3.80.090 Fire district impact fee formula.
3.80.100 School impact fee formula.
3.80.110 Resolution.
3.80.120 Computation of fees.
3.80.130 Deferral of impact fees for single-family residential construction.
3.80.140 Credits.
3.80.150 Accounting procedures—Reports.
3.80.160 Expenditure of fees.
3.80.170 Refunds.
3.80.180 Impact fee as additional and supplemental requirement.
3.80.190 Reconsideration of impact fees.
3.80.200 Appeals.

To the extent that impact fees increase the cost of development where necessary infrastructure is lacking, they can help discourage sprawl and the premature development of rural areas that are more appropriate for agriculture, conservation, and recreation. They encourage transportation and infrastructure efficient development patterns using market incentives.

Local value capture revenues (user fees, impact fees and land value return) could be calculated to cover both annual variable operating costs as well as periodic capital expenditures for rehabilitation and replacement.[101] Cash flow peaks and valleys could be smoothed out by appropriate financing techniques. But it is important to remember that bonds and other debt instruments are not sources of funding. They are sources of financing. The future taxes and fees that pay off any debts incurred are the sources of funding.

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[100] Blaine Municipal Code at *https://www.codepublishing.com/WA/Blaine/html/Blaine03/Blaine0380.html* (accessed January 13, 2021).

[101] Joe Minicozzi, *The Economics of Land Use in Florida*. Slides 244 to 255 show cascading spending requirements for a jurisdiction's capital budget based on construction costs and out-year rehab and replacement costs for roadway segments constructed at different times. *https://1000fof.org/wp-content/uploads/2020/03/U3-1000-Friends-3-11-20F-web.pdf* .

Today, many residents pay no fees to drive and park on public streets, even if they are congested. If distance- and congestion-based roadway user fees and performance-based parking fees were more used more extensively, economic incentives (to minimize payment of these fees) would encourage residents to locate homes closer to daily activities, encourage business owners to locate stores and offices closer to typical customers and employers, and to generate support for transportation facilities and services that could substitute for single-occupancy vehicles.

Today, infrastructure-created land values are primarily a windfall to owners of well-served sites.[102] A desire for these windfalls is the fuel for land speculation. Land speculation is the acquisition of land, not for the sake of using it, but for the sake of holding it until it appreciates in value. Land speculation (the buying and selling of land) creates nothing of value. But withholding land from development creates an artificial scarcity of land available for development. This artificial scarcity results in real increases in land prices, particularly at prime sites (sites near infrastructure amenities). These high land prices then drive development to cheaper, but more remote locations. Thus, infrastructure investments intended to facilitate development result in higher land prices that drive development away from infrastructure, exacerbating urban sprawl. Sprawl damages the environment, wastes energy, and necessitates the wasteful and expensive duplication of infrastructure facilities.[103]

Therefore, in addition to user fees and impact fees, land value return techniques could be key components of a value capture strategy. Land value return techniques include:[104]

- Special assessments (on land values)
- Long-term leases of public land and/or air rights
- Joint development agreements
- A two-rate or split-rate property tax whereby the tax rate applied to privately created building values is reduced while the rate applied to publicly created land values is increased.

Unlike exactions and impact fees that entail accounting for infrastructure costs, land value return techniques entail accounting for infrastructure benefits. With regard to special assessment districts, long-term leases of land or air rights, and joint development agreements, State and local governments could utilize real estate assessors, appraisers, development analysts and other professionals with similar skills to determine the geographic extent and intensity of

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[102] Rick Rybeck, "Avoiding Mis-Givings: Recycling Community-Created Land Values for Affordability, Sustainability and Equity," *Journal of Affordable Housing and Community Development Law*, Vol 28 No 2, p. 299, October, 2019. *https://www.americanbar.org/content/dam/aba/publications/journal_of_affordable_housing/Volume28_Number2/ah_journal_10_18_19.pdf*

[103] Rick Rybeck, "Financing Infrastructure with Value Capture: The Good, The Bad & The Ugly." *https://www.strongtowns.org/journal/2018/2/20/financing-infrastructure-with-value-capture-the-good-the-bad-the-ugly/*

[104] NCHRP Report 873, *Guidebook to Funding Transportation Through Land Value Return and Recycling*, p 17. *http://www.trb.org/Main/Blurbs/177574.aspx*

infrastructure-related land value uplift. Additionally, enabling state legislation could be created to transform the traditional property tax into a land value return fee for an entire jurisdiction. Use of computer-assisted mass appraisal software systems would facilitate this approach. Such systems have regression modules that can apportion total property value to its building value and land value components. This multiple regression analysis could also be used to determine how much individual infrastructure systems contribute to total land value, and this could be a factor in allocating land value return revenue among the infrastructure systems and agencies.

Although computer-assisted mass appraisal systems can be powerful analytical tools, households and individuals evaluate the difference between building values and land values whenever they purchase or rent a home. When a family is looking for a home, it typically narrows the search to characteristics such as number of bedrooms, total area, yard size, architectural style, and building condition. Families typically find many examples of houses or apartments that meet their criteria, but that sell or rent for vastly different prices depending on their location. Given that the physical buildings and yard sizes are similar, the primary factor in these price differences is related to the value of the land in different neighborhoods. Thus, while property assessment and appraisal is a technical endeavor, regular people understand it and make significant financial decisions based on their own understanding of these factors.

By returning infrastructure-created land values to communities, the following objectives can be achieved:[105]

- Infrastructure becomes financially self-sustaining to a greater degree.
- Profits from land speculation are reduced, thereby reducing the speculative demand for land and moderating land prices at prime sites.
- Higher costs for holding prime, high-value sites, will result in increased development at prime sites near existing infrastructure facilities.

Thus, instead of infrastructure investments chasing development away to cheaper, but more remote sites, infrastructure investments will attract development, resulting in more compact development patterns that are less impactful on the environment and that can be served by more efficient (less extensive and less expensive) infrastructure networks.

As shown above, appropriate user fees, impact fees and access fees (land value return) in a balanced combination, would not only raise revenues, but would also reduce costs by encouraging more compact development that requires less infrastructure per capita.

[105] NCHRP *Guidebook to Funding Transportation Through Land Value Return and Recycling*, Appendix E

# Conclusion

This report has reviewed the state of the practice regarding the "essential nexus" and "rough proportionality" tests associated with exactions such as easements, land dedications, and impact fees. These issues have been heavily litigated. However, the case law, overall, relies on the balancing test enunciated in the Penn Central case. In some instances, this balancing is informed by the "essential nexus" and "rough proportionality" tests. But given the propensity of property owners to oppose government limitations on development activities, these tests do not lend themselves to a simple check list that will ensure the avoidance of litigation. However, while the essential nexus and rough proportionality tests have favored property owners in certain circumstances, courts are generally deferential to a government's exercise of its police powers if the government establishes the following:

- A relationship between the technique and the powers delegated to it by its State.
- The exercise of this power advances a legitimate jurisdictional interest (health, safety, welfare).
- Due process was provided in the enactment of the law or regulation and in its implementation.
- Compatibility with uniformity. (In these cases, this means demonstrating that fairness is achieved by subjecting some people and property to fees or conditions while not subjecting others.)
- An "essential nexus" between a legitimate interest of the government, the impact of a landowner's actions on the attainment of that interest, and the fee or condition imposed on the landowner to protect or achieve that legitimate interest.
- The burden imposed by the fee or condition on property owners is proportionate to the benefits received by them or to the costs that they impose on the community. Under no circumstances can the burden of the fee or condition exceed the cost to the public sector of providing a special benefit or mitigating an adverse impact.

Regarding the but-for test for TIF districts, there has been considerable academic interest in investigating the validity of the but-for finding that accompanies most TIF ordinances. Despite this controversy, there has been relatively little litigation. When litigation occurs, courts deem TIFs to be legislative actions requiring judicial deference. This means that courts will not second-guess a legislative body regarding the wisdom or correctness of its decision. However, where TIF-enabling legislation requires findings of blight or a finding that economic development would not occur but for the TIF project, jurisdictions that fail to make these findings or that rely on spurious evidence to reach a pre-determined conclusion risk the invalidation of their TIF ordinances. For this reason, it is difficult to establish metrics or analytical tools that will ensure that a particular TIF district will survive a but-for legal challenge. But judicial decisions in the relevant State (or in States with a similar TIF-enabling statute) will illuminate the legal standards and thresholds for validity.

Many States and local governments have already developed the analytical tools (asset management lifecycle costing and fiscal impact methodology) to implement exactions and impact fees within an acceptable legal framework. Also, many jurisdictions use computer assisted mass appraisal (CAMA) systems to assess property value accurately. CAMA and real estate professionals have the capability to implement land value return techniques that can reduce land speculation, make infrastructure financially self-sustaining, and reduce sprawl.

# Glossary

**Assessed value**—The dollar value assigned to a property for purposes of measuring applicable taxes. There are three primary methods for determining assessed value:

- Comparable sales
- Cost to replace minus depreciation
- Income

Assessed value multiplied by a tax rate determines the tax liability for a property. Determination of the assessed value of a property is an administrative function. Setting tax rates is a political function.

**Authorizing or enabling legislation—**State-level legislation that authorizes / enables a subordinate jurisdiction (county, parish, township, city, etc.) to levy a special assessment, create a TIF or require exactions. This legislation will provide substantive and procedural requirements for establishing these value capture techniques.

**Benefit (general)—**The typical level of benefit that accrues to properties throughout a jurisdiction from a particular public facility or service. For example, a new highway might reduce traffic congestion, speed up freight deliveries and reduce the price of goods throughout a jurisdiction.

**Benefit (special)—**A specific and direct benefit that accrues to some properties as a result of their proximity (in distance or time) to a particular public facility or service. For example, while a new highway might benefit all properties generally, those properties closest to highway interchanges obtain even more value from the highway (due to easier access) and this would be reflected in higher property values as a result.

**Blight—**A condition of individual properties or neighborhoods. For an individual property, a significant lack of maintenance that results in deterioration of a building or an unkempt vacant lot that is overgrown or strewn with rubble. For a neighborhood, the prevalence of deteriorated or boarded-up buildings, vacant lots and/or deteriorated infrastructure are characteristics. Statutes that limit TIFs to blighted areas will define blight more specifically.

**Bond—**A certificate that acknowledges the indebtedness of the bond issuer to the holder. The holder of the bond is the lender (creditor), the issuer of the bond is the borrower (debtor).

**But for**—In the context of a TIF, this characterizes the necessary relationship between infrastructure improvement and future private sector development. In other words, the diversion of the tax increment away from a jurisdiction's general fund and into a dedicated fund for an infrastructure improvement project is permissible only if the private sector development would not occur without (but-for) the infrastructure improvement project.

**CAMA—**Computer-assisted mass appraisal. This is software that automates the real property assessment process.

**Condemnation—**The process whereby a governmental entity exercises its power of eminent domain to take private property for a public purpose. This typically entails a judicial proceeding where "just compensation" is ascertained.

**Eminent domain—**The power exercised by a governmental entity or agent to take private property for a public purpose pursuant to the Fifth Amendment to the U.S. Constitution. If property is taken for a public purpose, just compensation must be provided to the private owner.

**Essential nexus**—This refers to the relationship between a legitimate state interest, the impact of development activity upon that interest, and the ability of an exaction to compensate, remediate or mitigate that impact. (See also, "Rough Proportionality.") Although "essential nexus" is language applied by courts regarding the validity of exactions, a similar concept is employed for special assessments whereby the assessing jurisdiction establishes a nexus between an infrastructure project and a special benefit conferred upon a particular property or properties. In the context of TIFs, the relationship between infrastructure improvements and future private sector development is referred to as the but-for test.

**Exaction**—An in-kind provision of infrastructure, dedication of land for infrastructure, or cash payment for off-site infrastructure required of developers to mitigate the impact of new development on infrastructure capacity. This mitigation is required as a condition for obtaining development permits.

**Excise tax—**This is a tax levied against the quantity of a good purchased or sold. A per gallon tax on motor fuel, for example, depends solely on the amount of fuel sold. Fluctuations in the price of motor fuel do not lead to changes in revenue as long as the amount sold remains constant. (This is in contrast to a sales tax which is levied against the price of the good sold.)

**Fee—**This is a charge for a good or service. It is similar to a "price," in that the consumer is either paying for a direct benefit received from the government or compensating the government for an expense incurred because of or on behalf of the person or entity paying the fee. Fees are distinguished from "taxes." Regarding taxes, there is no direct relationship between the payment of a tax and the receipt of benefits (or compensation for costs incurred). Regarding fees, most people pay for water with a per-gallon fee for the operation of a municipal water purification plant and distribution system. The more water you use, the more you pay. Many people also pay property taxes, some of which might be used to fund capital expenses for the water authority. This is a tax and not a fee because payment is unrelated to the utilization of municipal water. However, the land value portion of the property tax is more like a fee because access to municipal water (and other infrastructure amenities) enhances the value of land. So, the part of the property tax applied to land values is more like a fee and the part applied to building values is more like a tax.

**Fee rate** —— The means for determining the amount of a special assessment. A "fee rate" could be expressed as a "cost per front foot" or as a "rate (percentage) applied to property value."

**Fee schedule**—An adopted and published fixed-fee for defined public services such as water main and sewer main hookups, curb cut installation, or zoning changes requested by the property owner.

**Front foot**—A measure of distance along the side of a property that faces a street. Distance is one of the primary cost variables in many types of infrastructure projects (sidewalks, streets, utility lines, etc.) The length of an infrastructure facility segment constructed along one or more sides of a property is expressed in "front feet."

**Implementing ordinance**—Legislation that establishes a special assessment, development impact fee or TIF to fund particular infrastructure projects. This legislation satisfies the substantive and procedural requirements provided in the applicable State's authorizing legislation.

**Inverse condemnation—**As mentioned above, under "condemnation," a governmental entity initiates a judicial proceeding to acquire private property through eminent domain. However, in the event that a government law or regulation imposes an excessive burden on private property, a property owner may initiate a judicial proceeding claiming that the government has effectively taken property without providing just compensation. Because the property owner is initiating this proceeding, it is referred to as "inverse condemnation."

**Land value return—**Providing public goods and services (infrastructure) typically enhances the value of well-served sites. Returning some of this publicly created land value to the community that created it is referred to as "land value return." Land value return encompasses several value capture techniques including (but not limited to):

- The land value portion of the traditional property tax
- Special assessments (applied to land value only)
- Sales or leases of public lands or air rights
- Joint development agreements.

**Land value uplift—**The increase in land value caused by the creation or improvement in nearby infrastructure. As mentioned in the report, even the expectation of infrastructure improvement can lead to land value uplift prior to the commencement of improvement activities.

**Police powers—**The Tenth Amendment to the US Constitution confers powers to the States (and potentially delegated by them to local governments) enabling them to adopt laws and regulations to prevent crime and to secure the safety, health and prosperity of their citizens by preserving the public order and preventing the conflict of rights. Zoning, building codes, and other development regulations are examples of police powers exercised by State and local governments.

**Rough proportionality**—This refers to the relationship between the impact of private development upon a legitimate state interest and the burden placed upon that development by an exaction to remediate or mitigate that impact. In other words, the burden must be roughly proportional to the impact being mitigated. Although "rough proportionality" is language applied

by courts regarding the validity of exactions, a similar concept is employed for special assessments whereby the assessing jurisdiction establishes that a special assessment is proportional to the benefit conferred to or the costs imposed by a private property. In this context, a special assessment may not exceed either the benefit conferred, or the cost imposed, whichever is less. In the context of TIFs, there is no parallel concept except that TIF revenues cannot exceed the cost of the infrastructure project and any financing costs that might also be entailed. Once TIF project costs or debt service are retired, a TIF is dissolved and all revenues from the benchmarked revenue sources are allocated to the general fund.

**Single occupancy vehicles**—Cars carrying only one person, the driver. Compared to walking, biking, carpooling (high occupant vehicles or HOV) and well-utilized transit, single-occupancy vehicles consume more energy and space per person per trip.

**Site value—**Land value. This term emphasizes that land value is related to the location of the site and not merely to the value of dirt.

**Special assessment**—A fee imposed on properties that receive a special (specific and direct) benefit from a particular public facility or service.

**Tax**—This is a charge owed to a government. However, payment of a tax bears no direct relationship to any particular benefit received or costs incurred. Instead, taxes represent a payment for general and possibly indirect benefits. Most people pay for water with a per-gallon fee for the operation of a municipal water purification plant. The more water you use, the more you pay. Many people also pay property taxes, some of which might be used to fund capital expenses for the water authority. This is a tax and not a fee because payment is unrelated to the utilization of municipal water. However, the land value portion of the property tax is more like a fee, because access to municipal water (and other infrastructure amenities) enhances the value of land. So, the part of the property tax applied to land values is more like a fee and the part applied to building values is more like a tax.

**Tax increment—**The difference in revenue generated by a benchmarked revenue source after an infrastructure project has been undertaken compared to the revenue generated prior to the project. Based upon the language in a TIF ordinance, the tax increment is that portion of the difference which is diverted away from a jurisdiction's general fund and into a dedicated fund used solely for the infrastructure improvement project.

**Tax increment finance (TIF**)—A technique for funding an infrastructure project without allocating existing revenues or raising new taxes. Thus, TIF is as much a budgeting tool as it is a funding technique. TIF relies on an assumption that but-for an infrastructure project, tax revenues in a defined location would remain constant. Tax revenues are measured and benchmarked at this "pre-project" level. If a TIF ordinance is enacted, any future increase in tax revenues (as identified by the ordinance) above the benchmarked level in the defined location is deposited into a special account dedicated to the funding of the infrastructure project. An important feature of most TIFs is that the public pays the same taxes regardless of whether a TIF exists or not. For this reason, TIF might be characterized as "revenue segregation" rather than as "value capture."

**Tax levy—**The amount of revenue collected by a particular tax or jurisdiction.

**Tax liability—**The amount of taxes owed by a taxpayer, either for a particular tax or a combination of taxes.

**Tax rate—**Percentage or fixed dollar amount which is used to determine how much tax is owed. For ad valorem property taxes, a tax rate is expressed in terms of dollars per $100 or $1,000 of assessed value. Thus, a tax rate of 1 percent ($1/$100) is the same as a tax rate of 10 mills ($10/$1000). For a property with an assessed value of $100,000 at a tax rate of 2.5% or 25 mills, the following equation would be used: $100,000/$1,000 x 25 = $2,500 tax liability. For sales taxes, the tax rate is expressed as a percentage of the price of the good or service being purchased. For excise taxes, the tax rate is expressed as an amount of money per quantity of the good purchased. Thus, the price per gallon of gas might fluctuate, but the excise tax, per gallon, remains constant.

**Uniformity—**The legal requirement that all taxpayers or taxable property in the same circumstances and conditions should be treated the same.

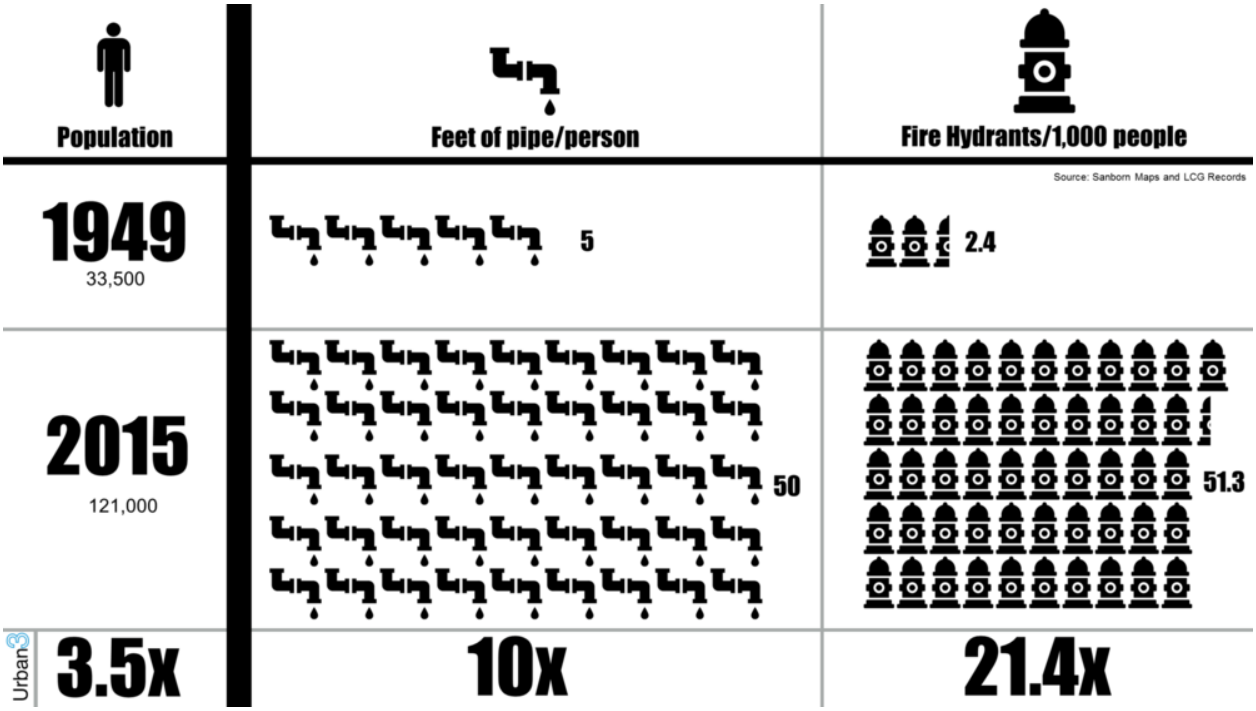
**Value capture**—In its simplest form, this is “value given” for “value received.” In other words, value capture represents a payment to a jurisdiction for the receipt of a benefit or to compensate for the imposition of a cost. “Value capture” describes several techniques that return a share of infrastructure-created value to the public sector that created it or that compensate the public sector for adverse development impacts upon it.

# Appendix. Impacts of Sprawl

## Infrastructure Liabilities Outpacing Population and Income

The following graphics were created by Joe Minicozzi of Urban3. They compare the growth in population, infrastructure and average income for Lafayette Louisiana from 1949 until 2015.

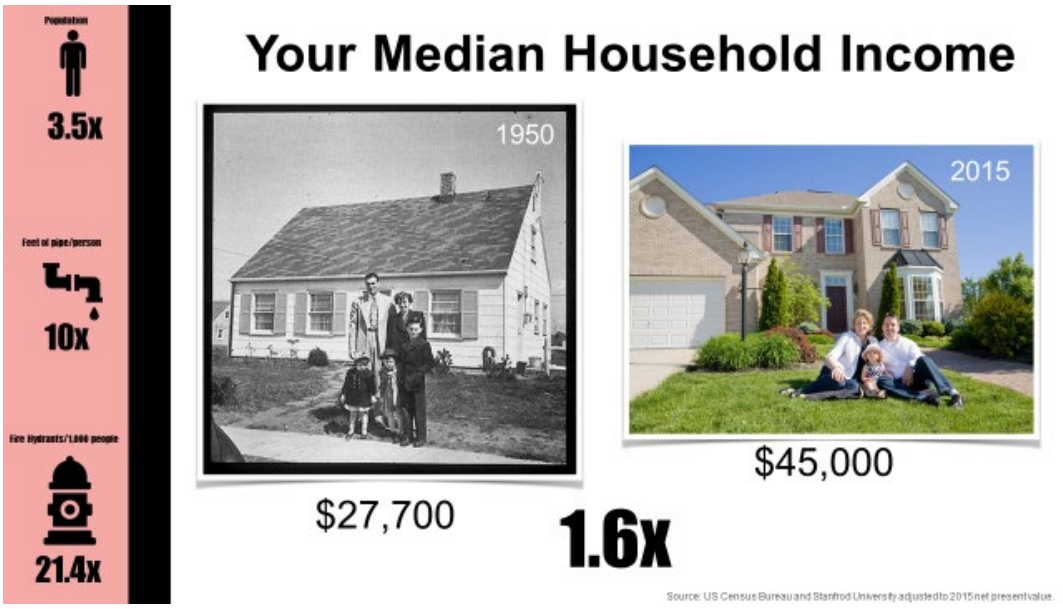
**Figure 4. Lafayette Population, Plumbing, and Fire Hydrants, 1949 and 2015**




*Source:* © 2021 Joseph Minicozzi, Urban3. Used by permission.

In Figure 5, median household income is expressed in constant (inflation-adjusted) dollars.

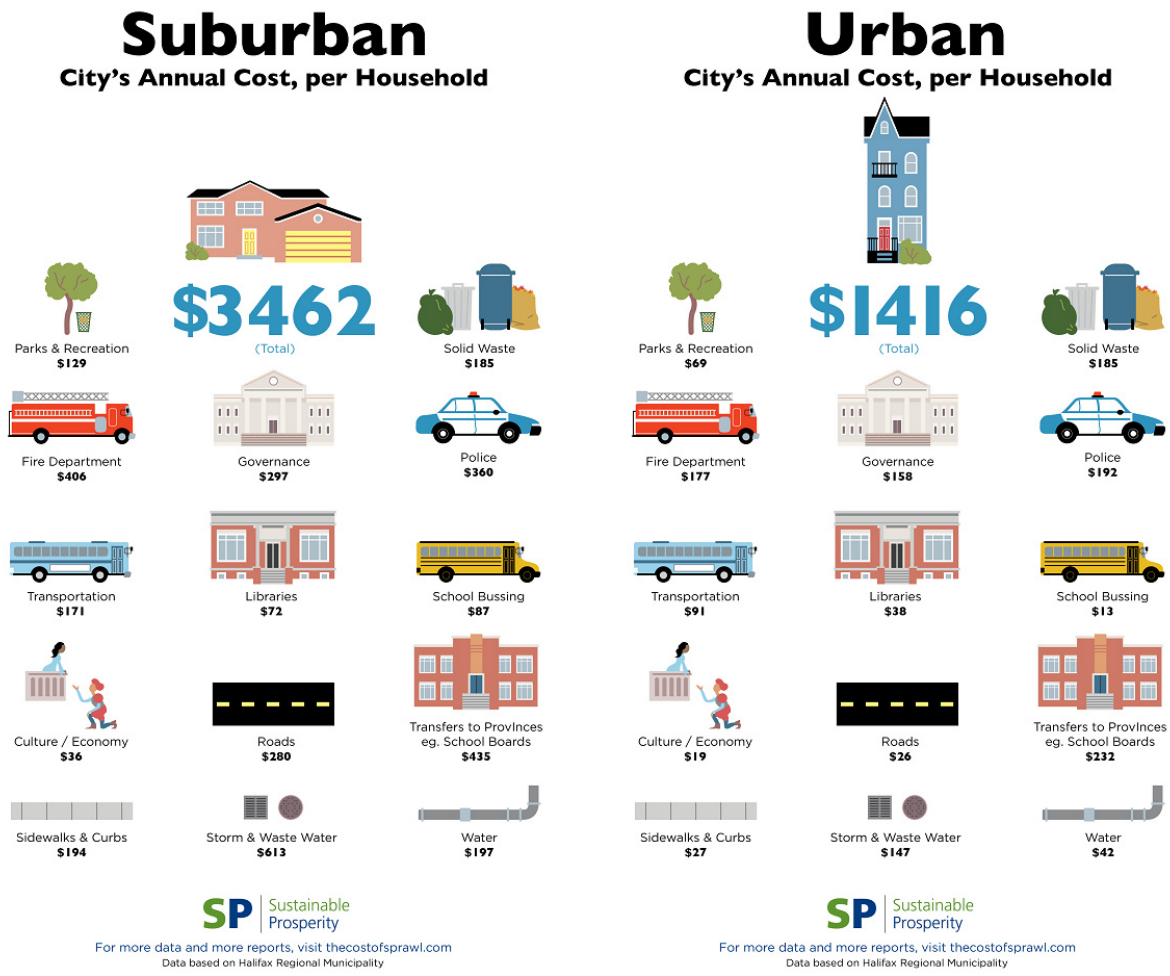
**Figure 5. Growth in Population, Median Household Income, Plumbing Length, No. of Fire Hydrants**




*Source:* © 2021 Joseph Minicozzi, Urban3. Used by permission.

Here is a graphic from Halifax Canada, showing the different costs per household for various public facilities and services depending on whether the household was located in the urban core or in the suburbs. On average, the suburban costs per household are 2.5 times more than the urban cost per household.

**Figure 6. Costs per Household for Public Facilities and Services, Suburban vs. Urban**



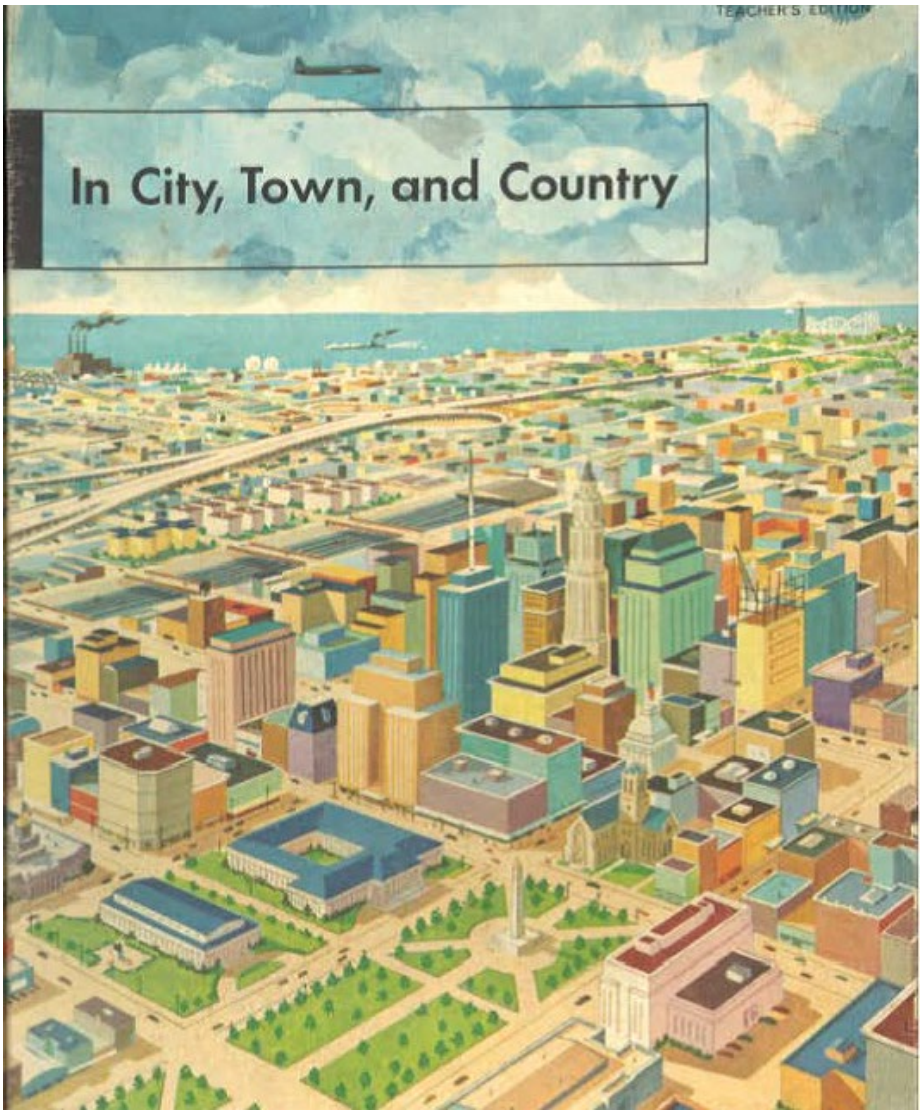

*Source: Sustainable Prosperity Image via streetsblog.org.* https://usa.streetsblog.org/2015/03/05/sprawl-costs-the-public-more-than-twice-as-much-as-compact-development/

The difference in cost is primarily related to differences in density. In other words, for each suburban household, there are more lane miles of road, more feet of water and sewer pipe, more libraries and fire stations than for each urban household.

## Does New Development Cover Infrastructure Costs?

The following illustrations are from the 1959 *In City, Town, and Country* by Paul R. Hanna (Scott, Foresman & Co.). Figure 7 shows the front cover.

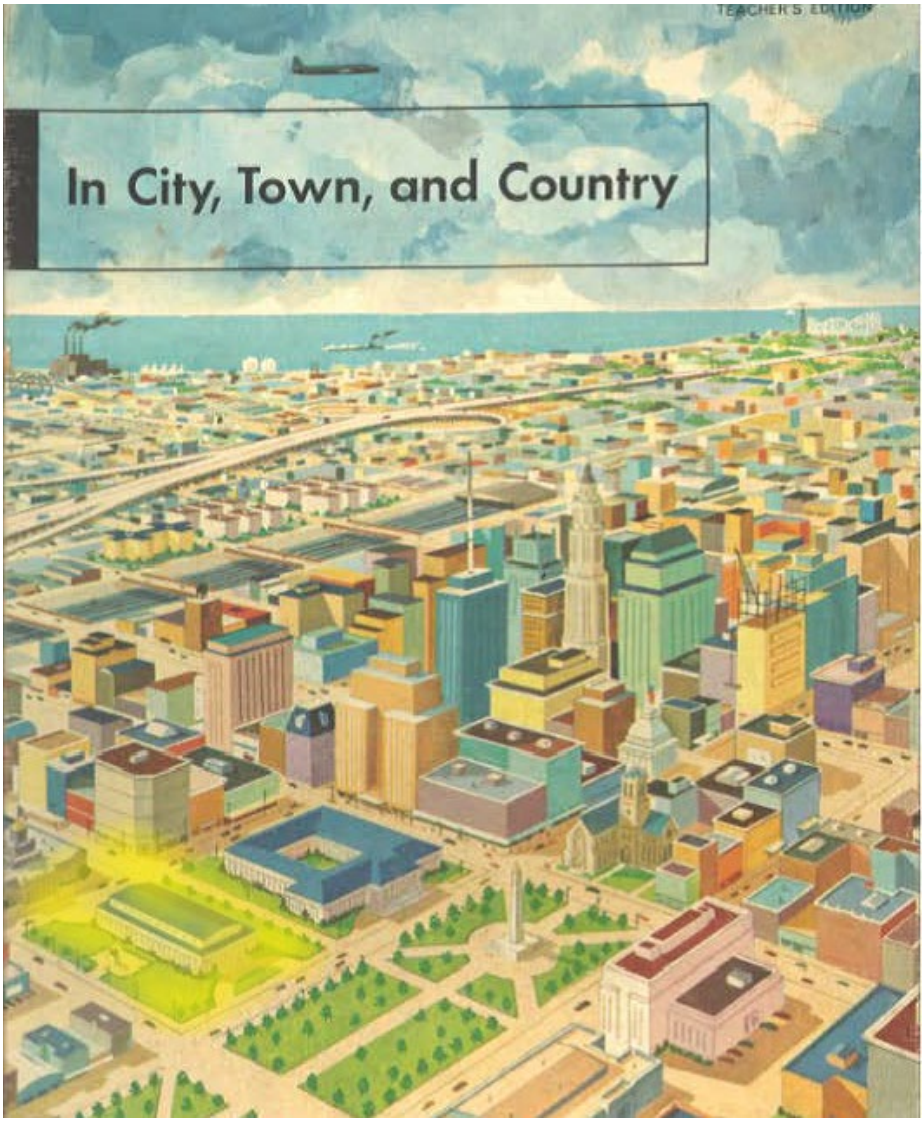
**Figure 7. Downtown**




*Source:* From "In City, Town and Country" © 1959 SAVVAS LEARNING COMPANY LLC. Used by permission. All Rights Reserved. *https://www.savvas.com/*

In the next image, a property in the lower left corner has been highlighted.

**Figure 8. Downtown with Highlighted Property**



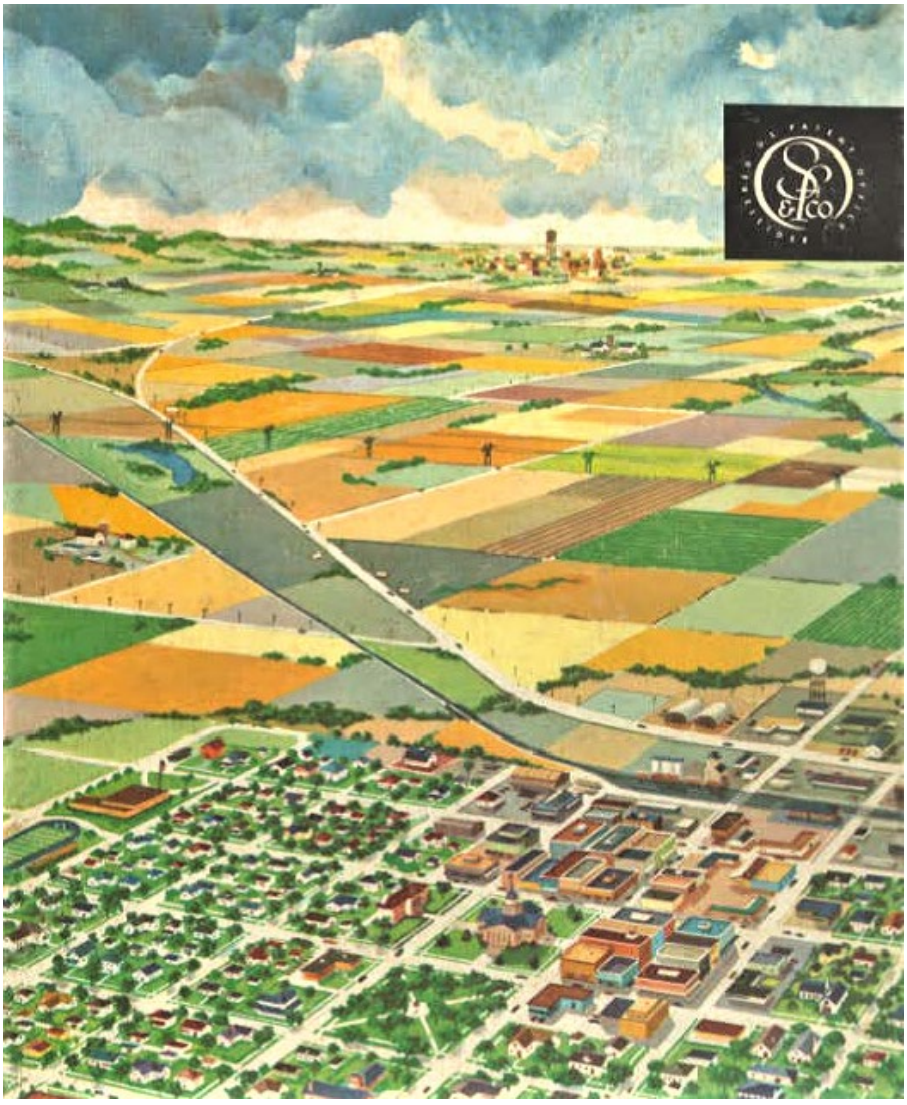

*Source: From "In City, Town and Country" © 1959 SAVVAS LEARNING COMPANY LLC. Used by permission. All Rights Reserved.*
https://www.savvas.com/

The highlighted property occupies an entire city block. It appears to be an institutional use with substantial open space all around. On one side, across the street, there is a memorial park complex. Assume that this property is privately owned, and the owners decide to raze the building and construct a new set of office and retail buildings to replicate the development immediately above it in the illustration. In other words, several buildings of greater height and density, no setbacks and no open space. Such new development will intensify the use of this site. Users will consume additional public resources related to transportation, water, sewer, police and fire protection. But the water pipes are already there. The streets are already there.

The police and fire department are already nearby. Transit buses are probably already operating nearby if not on one of the adjacent streets. The new development will pay more taxes, and that should cover the additional operating expenditures associated with the new development.

The next image, from the back cover, shows the urban fringe. Residential and modest commercial or industrial properties give way to farms and other rural land uses.

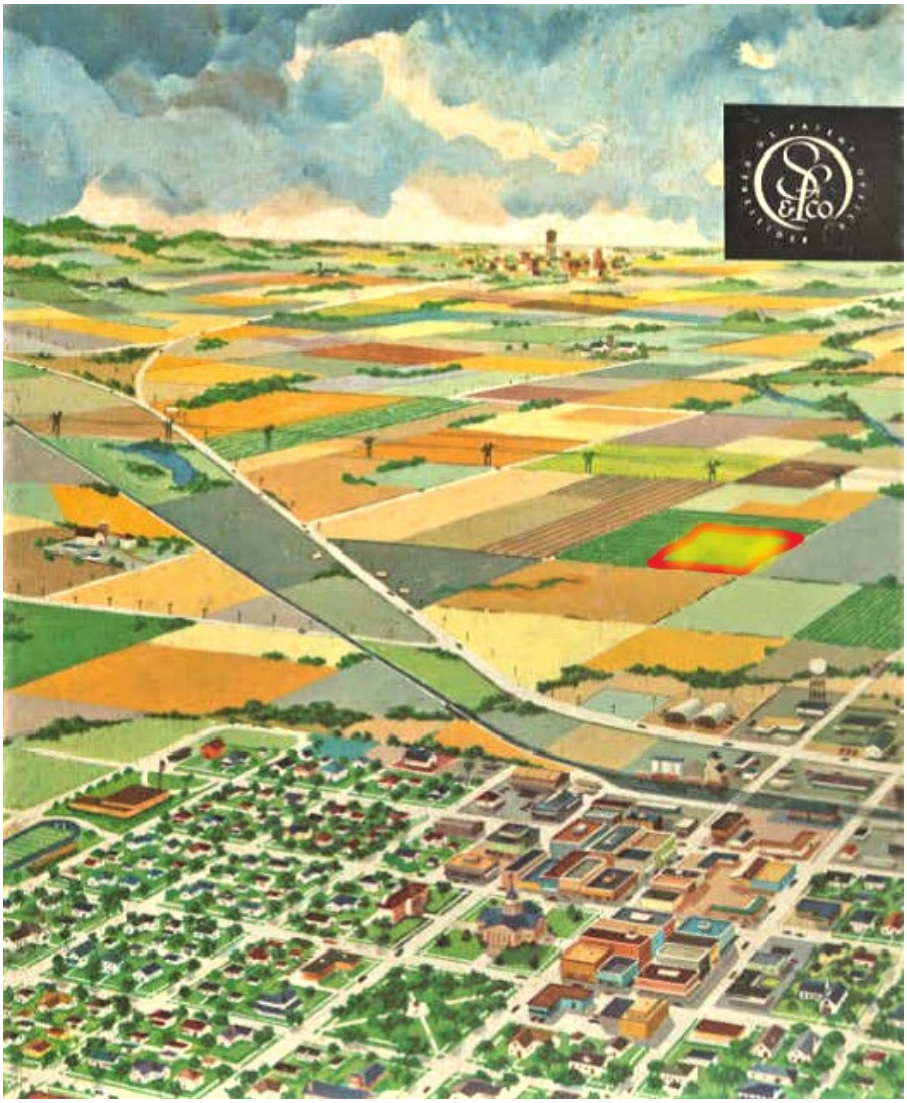
**Figure 9. Urban Fringe**



*Source: From "In City, Town and Country" © 1959 SAVVAS LEARNING COMPANY LLC. Used by permission. All Rights Reserved.*
https://www.savvas.com/

In the next image, part of a farm field in the center right is highlighted.

**Figure 10. Urban Fringe with Highlighted Field**



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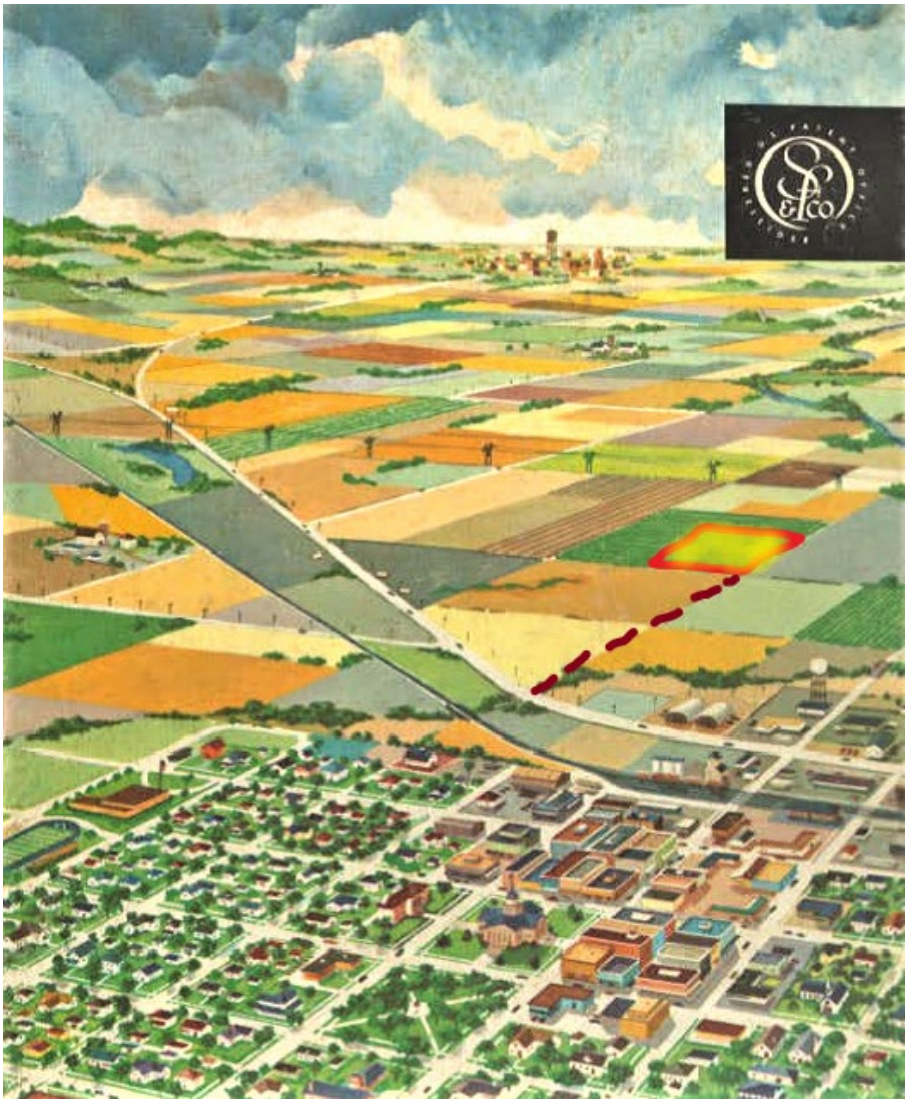
https://www.savvas.com/

Assuming this field is about the same size as the city block in the prior discussion, if the owner wants to put up a complex of office and retail uses identical to those that were proposed for the downtown city block, it will consume the same amounts of police, fire, water, sewer and transportation resources as the urban development. But the water pipes are not there. The roads are not there. The transit isn't there. And, if police and fire services were to respond in a timely fashion, they might require a new station nearby. Although the buildings will be identical (and have the same value and pay the same taxes as their urban counterparts), the value of the farmland is much lower than its urban counterpart. This lower value reflects, to a large degree, the lack of urban infrastructure at the site. Thus, this new exurban development will require not

only an incremental addition of city services, but entirely new facilities. And, while the cost of public facilities and services will be more costly to provide here, this site will contribute less in taxes due to lower land values.

In the next image, the county creates a TIF to pay for a road connecting the proposed development and the existing county road and for a signalized intersection where they meet. The dotted line represents the rough location of the connecting road.

**Figure 11. Proposed Road to Highlighted Field**



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Assuming that the tax increment will be defined in terms of the difference between property tax and sales tax revenues collected from this field before the project and the revenues obtained after the project has been initiated and that the tax increment will be sufficient to pay for the road extension and intersection signalization, where is the revenue to pay for all the other public facilities and services that will be required?

The demand for developed space is finite in an economic region at a given point in time. If the demand for developed space in this metropolitan area is limited and if the greenfield exurban TIF development occurs first, it might not be economically feasible to proceed with the downtown redevelopment project. In other words, the TIF subsidy may have simply shifted development from downtown to the urban fringe. In this example, although the new exurban development will create a tax increment for the county, it does so at the expense of an unrealized tax increment for the downtown.