FAQs:

Tax Increment Financing (TIF) Program

August 2022

The purpose of this document is to address various questions about the TIF program and process. The TIF program is very complex, and we recommend including Cabinet staff from the outset of any discussions regarding a potential project. TIF projects require considerable time, energy and resources. Cabinet staff is available and happy to discuss any potential project to determine if the TIF program is the best approach and which TIF program aligns with the potential project.

What is TIF?

- Tax Increment Financing (TIF) is an economic development tool to use future gains in taxes to finance the current public infrastructure improvements for development that will create those gains. But what exactly does that mean?
- When a development project occurs, there is usually an increase in the property taxes generated as well as a potential increase in the sales taxes and withholding taxes generated for that area – resulting in a potential increase in tax revenues. The increased tax revenue is the "tax increment" that may be available to assist with funding the approved public infrastructure elements of the development (such as a road, sewer, utility, etc.).

What is approved public infrastructure costs?

- KRS 154.30-010 - "Approved public infrastructure costs" means costs associated with the acquisition, installation, construction or reconstruction of public works, public improvements and public buildings, including planning and design costs associated with the development of such public amenities.
- "Approved public infrastructure costs" includes but is not limited to costs incurred for the following:
  - Land preparation, including demolition and clearance work
  - Public buildings
  - Sewers and storm drainage
  - Curbs, sidewalks, promenades and pedways
  - Roads
  - Street lighting
  - The provision of utilities
  - Environmental remediation
  - Floodwalls and floodgates
  - Public spaces or parks
  - Parking
  - Easements and rights-of-way
  - Transportation facilities
  - Public landings
  - Amenities, such as fountains, benches and sculptures
  - Riverbank modifications and improvements

Is a parking garage considered “approved public infrastructure costs?”

- If all spaces in the garage are available for use by the public and not reserved, then 100% of the costs of the parking garage may be considered eligible approved public infrastructure costs.
- If the parking garage includes reserved spaces, such as for an office building or hotel, then the percentage of the parking spaces NOT reserved may be applied to the cost of the parking garage to determine potential eligible approved public infrastructure costs.

Have there ever been project costs considered public infrastructure improvements by an applicant that were not deemed approved public infrastructure costs under the TIF program?

- Yes, the following do not qualify as approved public infrastructure costs:
    - » Community centers
    - » Non-public buildings
    - » Solar farms
    - » Utility upgrades, such as installations of generators, telephone lines, etc., to private office buildings
    - » Storm shelters not available for use by the public
    - » Stadium where admission is charged
    - » Buildings/improvements to private colleges/universities
- Public buildings should be open and available for public access.

If a project is interested in establishing a TIF, where does it need to start?

- All TIF projects begin at the local government level. Local government must approve a development area and is usually the applicant for the State TIF program.

What is a Development Area?

- The Development Area is set and established by the local government entity in accordance with KRS 65.7049, 65.7051 and 65.7053 to encourage investment and reinvestment in and development, use and reuse of areas of the city or county.
- If local participation is pledged to a local TIF project, the participation is pledged from activities occurring within the development area.

What is a Footprint?

- KRS 154.30-010 – “Footprint” means the actual perimeter of a discrete, identified project within a development area. The footprint shall not include any portion of a development area outside the area for which actual capital investments are made and must be contiguous.
- If a state TIF project occurs, the state increment pledged to the project is from new taxes generated within the footprint.
- The local government will request the proposed footprint, but the footprint is set and finalized by the state. The state’s footprint will include full parcel boundaries and will exclude any partial parcel boundaries.
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- The development area can be the same size or bigger than the proposed footprint. However, the footprint is never larger than the established development area.

Are all local TIFs eventually approved as State TIFs?

- No, not all local TIFs qualify as a State TIF and/or submit a request for approval of a State TIF.

Do you have to have a local TIF to apply for a State TIF?

- Yes, all State TIF projects must first have a local TIF established.

What are the three State TIF programs?

- Real Property Ad Valorem Tax Revenues
- Mixed-Use Redevelopment in Blighted Urban Areas
- Signature Project

Who is the applicant for the State TIF?

- The local government agency is the applicant and submits a State TIF application to the Cabinet for Economic Development.

What are the potential fees associated with a TIF project?

- Application Fee = $1,000, due with application
- Legal Fees (drafting legal documents) – for BOTH preliminary approval and final approval
- Consultant Fee – fee for the independent consultant report, due prior to engaging independent consultant (funds are placed in escrow until report is complete)
- Administrative Fee = Incentive Amount x .0025 (maximum of $50,000), due prior to presenting project for final approval

How do I access/receive the State TIF application?

- Contact the Cabinet to discuss the project to determine if the State TIF program is the best fit. Further conversations and meetings may also occur to fully understand the potential magnitude of the project. Cabinet staff will provide the latest version of the application if the TIF program is identified as a method of assistance for the project.

What steps are required prior to preliminary approval occurring?

- Introductory meeting with Cabinet staff, applicant and other appropriate parties to discuss the project and the Cabinet's understanding of the application/project. Additional meetings/calls may occur to confirm the Cabinet's understanding of the project.
- Cabinet staff reviews TIF application for completeness and evaluates whether, based solely on information submitted by the applicant, the project is likely to meet the minimum requirements for the program. Cabinet staff also determine if all of the information and supporting documentation has been provided and is consistent.
- Application fee of $1,000 must be paid.
- Memorandum of Agreement is drafted by Cabinet legal counsel and must be signed prior to presenting the preliminary approval request to KEDFA.

May I spend any funds prior to preliminary approval?

- Any costs incurred prior to preliminary approval are not considered eligible for the program.
- Only costs incurred after preliminary approval are eligible for the TIF program.

When will I know how much the state is willing to pledge for my TIF project?

- The Cabinet will determine its recommendation of pledged taxes, pledged percentage and pledged approved increment and present its recommendation to KEDFA at final approval of the project.
- Per statute, the total negotiated tax increment is the lesser of the three following amounts:
    - Approved public infrastructure costs
    - Projected state tax incremental revenues
    - Net new fiscal impact to the Commonwealth

Will projects locating in our TIF project be eligible for other incentive programs?

- Once a tax has been pledged to a TIF project, the tax may not be pledged for another incentive program.
- KBI ELIGIBILITY IN TIF PROJECT: If the withholding tax is pledged to a TIF project, then the withholding tax of the KBI Program is not eligible to be pledged. This scenario comes up a lot with office buildings in a TIF project.
- There are multiple factors in determining eligibility of incentive programs. More information is needed to provide an accurate response.

What happens after preliminary approval?

- Cabinet staff will provide a fully executed copy of the Memorandum of Agreement to the applicant.
- The Cabinet has multiple consultants on contract to complete and prepare the required statutory analysis/report. Cabinet staff will work with the consultants to identify the firm to complete the work.
- Cabinet staff will provide an invoice to the applicant for the work to be performed by the independent consultant.
- The acknowledgement included on the invoice must be signed and returned by the applicant. Additionally, the funds must be paid to the Cabinet before any work may begin. The Cabinet places the funds in escrow and will remit them to the consultant after the work is completed.

What does the independent consultant report entail?

- The consultant researches the TIF project and projections submitted by the applicant as well as market data, benchmark information, etc., related to the project. The consultant will determine if the project is feasible, if the project will result in a net positive impact for the Commonwealth and if the project will not occur if not for the granting of incremental revenues.
- A kickoff meeting with Cabinet staff, the independent consultant, applicant and other appropriate parties to discuss the project usually occurs at the project site location at the beginning of the process. A tentative calendar of events is drafted for the working group to help manage expectations.
- The independent consultant will request market studies, benchmark data, contracts/agreements in place, hotel flags identified, listing of interested vendors/occupants, visitor information, and other data/information to support the project.
- Telephone calls and emails will occur so the independent consultant is able to gain a thorough understanding of the project, its potential for the region/state and to address questions from the independent consultant.
- If the consultant's report reflects a net positive impact to the Commonwealth, the report is presented to KEDFA during closed session.

Is anyone else involved in the methodology and review of the independent consultant?

- KRS 154.30-030 requires the independent consultant to consult with the Office of State Budget Director (OSBD) and the Finance and Administration Cabinet (FAC) in the development of the report.
- OSBD and FAC staff meet with the independent consultant after the kickoff meeting to discuss the project and methodology.
- The report is shared with OSBD and FAC staff for review prior to sharing with the applicant.
- Please note KRS 154.30-030 also require the state budget director and the FAC secretary to provide a certification of net positive impact to the Commonwealth regarding the project.

What is the purpose of the consultant report?

- KRS 154.30-030 requires the independent consultant report.
- State TIF projects that require an independent consultant report are reviewed by an independent consultant to determine the project's feasibility including, financing, appropriateness of the use of the State TIF program and whether the project represents a net positive impact (Net New) to the Commonwealth.

What is Net New impact?

- The calculation is:
  - » Estimated amount of state tax revenues generated by the project over the applicable term
  - » LESS: Estimated amount of state tax revenues that would be displaced (includes revenue that would be lost as a result of the project and economic activity that is diverted to the project that previously took place at existing establishments with the Commonwealth – transfer spending)
  - » LESS: Estimated amount of state old revenues that would have been generated over the applicable term
  - » EQUALS Net Positive Economic/Fiscal Impact

- Net New to the State – many times we discuss exciting and worthwhile projects that are going to have a tremendous impact on the city, the county and the region. The consultant reports are charged with determining the impact a project will have on the state.
- Examples:
  - » MAY BE NET NEW: Kentucky currently does not have an indoor water park, such as Great Wolf Lodge or Wilderness of the Smokies. If an indoor water park was built, then Kentucky citizens may stay at it and spend money at it instead of going to an indoor water park in another state.
  - » MAY NOT BE NET NEW: A new local restaurant is built or another restaurant operation opens a second establishment (first location is in Kentucky). The spending associated with the new restaurant is likely transfer spending because the Kentucky citizen was already planning to eat at a restaurant.

What does final approval entail?

- Cabinet staff negotiate the TIF incentive amount and project requirements that they are willing to recommend to KEDFA for approval as state participation in the TIF project.
- Cabinet staff request legal to draft a TIF incentive agreement detailing the footprint, the specific taxes pledged to the project, amounts of increment available and approved public infrastructure expenditures and reporting requirements.
- Administrative fee equal to Incentive Amount x .0025 must be paid.
- Tax Incentive Agreement is finalized and must be signed prior to presenting final approval request to KEDFA.

What state taxes are eligible for increment recovery?

- For Mixed-Use and Signature TIF Projects, State Taxes eligible for increment = up to 80% of the following state tax revenues may be pledged from the footprint include:
  - » Real property ad valorem tax
  - » Individual income taxes/withholding tax
  - » Corporate income tax
  - » Limited liability entity tax
  - » Sales tax

- Although all of the above taxes are eligible by statute to be pledged, the Cabinet usually only pledges the following taxes:
  - » Real property ad valorem tax
  - » Withholding tax
  - » Sales tax

- For Real Property TIF project, State Taxes eligible for increment = up to 100% of the real property ad valorem state tax revenues may be pledged from the footprint.

Will the state pledge 80% of the state tax revenues for Mixed-Use and Signature TIF projects and 100% of the state tax revenues for the Real Property TIF projects?

- MIXED-USE AND SIGNATURE TIF: The state may pledge up to 80% of the new taxes generated to the TIF project. However, the state continues to recommend a pledge between 40% and 60% of the new taxes generated to the TIF project.
- REAL PROPERTY TIF: The state may pledge up to 100% of the new taxes generated to the TIF project. However, the state continues to recommend a pledge between 80 and 90% of the new taxes generated to the TIF project.

What other requirements/negotiations may be included in the tax incentive agreement?

- The TIF projects include a Percentage of Completion requirement in the incentive agreements, meaning 100% of the projected investment must be completed for the project to be eligible for 100% of the approved tax incentive pledged to the project. If 100% of the projected investment is not completed, then the actual percentage of the completed investment is applied to the approved tax incentive amount to determine the amount of tax increment available for recovery. If the project exceeds 100% of the projected investment, the tax increment will not increase – it is capped at the amount of approved increment.
- Most projects include multiple forms of approved public infrastructure. The tax incentive agreement may limit the eligible approved public infrastructure cost to one or a few items, such as a sewer improvement or parking garage, to guarantee the needed public infrastructure is completed for the project.

What is the first step after final approval?

- The applicant will need to establish the base/old revenues using Exhibit H from the tax incentive agreement.
- The Cabinet provides a questionnaire to each applicant for assistance in the process of establishing the base/old revenues. This questionnaire should be provided to all existing occupants of the TIF footprint for completion. It's the applicant's responsibility for collecting the questionnaires and providing them to the Cabinet (which shares them with the Department of Revenue). If the information is not provided, it may take the Department of Revenue more time to establish the base/old revenues.

When does the increment begin?

- The increment may begin at the Activation Date of the project as outlined in the Tax Incentive Agreement.
- The project must have met the required minimum capital investment before any increment may be disbursed.

What is the minimum capital investment requirement (MCI) and when is it required to be met?

- The minimum capital investment requirement is the required amount of capital investment incurred within the Development Area. The minimums for each TIF program are as follows:
    - » Real Property - $10 million
    - » Mixed-Use - $20 million (but not to exceed $200 million)
    - » Signature - $200 million

- The minimum capital investment must be achieved by the Activation Date as outlined in the Tax Incentive Agreement, or the project will automatically terminate and no longer be eligible for incentives.
- After preliminary approval, the applicant may start recording capital expenditures related to the project to work towards achieving the minimum capital investment threshold. An example of an acceptable capital expenditure is the purchase of land because it is a fixed asset. Administrative costs associated with the land acquisition are not considered capital expenditures.

What is the Activation Date?

- The date established any time within a two (2) year period after final approval, and it may be extended to no more than four (4) years upon written request for the extension and approval by KEDFA.
- For all projects, the Activation Date is the date on which the time period for the pledge of incremental revenues shall commence.
- To implement the Activation Date, the minimum capital investment must be met or else the agreement will automatically terminate.

What is the increment process and when is the increment received?

- Per the terms of the Tax Incentive Agreements, an Increment Request exhibit is required to be completed and submitted to Cabinet staff (who share them with the Department of Revenue). As an attachment to the exhibit, the Cabinet provides a questionnaire to each applicant for assistance in the process of calculating the annual increment. The questionnaire should be provided to all occupants of the TIF footprint during the year for completion. The applicant is responsible for collecting the questionnaires and providing them to the Cabinet with the required exhibit. This information is shared with the Department of Revenue. If the information is not provided, it may take the Department of Revenue more time to calculate the increment.
- Additionally, the Tax Incentive Agreement includes required reports/exhibits that are submitted to the Cabinet's compliance staff semi-annually and/or annually for review.
    - One exhibit requires an independent CPA as contracted by the applicant to review and verify the investment amounts included in the exhibit are accurate at three different intervals throughout the term of the incentive agreement.
- The Department of Revenue is responsible for calculating and disbursing the increment. Prior to disbursement of any increment, the Department of Revenue will confirm compliance with the incentive agreement with Cabinet staff.

Is annual reporting required for the TIF program?

- Yes. Please refer to the response to the increment process question – it includes information about reporting requirements.

What happens if the scope of the project changes after final approval?

- Please contact Cabinet staff to determine if the TIF project is impacted by the change. An amendment to the incentive agreement may be necessary.

What if the TIF project has financing that dictates a certain timed increment payment?

- TIF projects with financing aligned to the increment should stagger/lag increment payments to financing payments. The Department of Revenue is not able to issue an increment to correspond with debt payments.

Fact Sheet

See https://cedky.com/cdn/1740_tif_fact_sheet.pdf for the TIF Fact Sheet.

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