TIF at a Turning Point: Defining Debt Down

by Joan M. Youngman

Joan M. Youngman is senior fellow at the Lincoln Institute of Land Policy in Cambridge, Mass.

The proposal by California Gov. Jerry Brown (D) to end tax increment financing (TIF) initiatives in that state1 signals a dramatic change in the fiscal landscape of a region with a long history of tax innovations, often with national repercussions. That was certainly true in the case of Proposition 13, and it was also true when California introduced TIF in 1952. That new instrument spread across the country, adopted in some form in almost every state,2 and is now “the most widely used local government program for financing economic development in the United States.”3 Whatever the outcome of Brown’s proposal,4 the suggestion that TIF initiatives are no longer sustainable in California marks a turning point worth careful consideration. Moreover, municipal experience with TIF may shed light on larger issues of debt finance now facing many state and local governments.

In theory, TIF creates a perfect closed system of self-sustaining finance, a textbook example of “value capture.” There are important differences among state approaches,5 but some common elements form the basic pattern. Generally, a municipality identifies a specific geographic area for redevelopment. The redevelopment initiatives may be directed by the municipality or by an economic development agency that is typically under municipal control. They may be funded on a cash basis or, more commonly, by issuance of bonds. The crucial feature is the earmarking of taxes on future increases in property values in the TIF district to pay for redevelopment costs.

TIFs can be invisible to taxpayers, because the assessor continues to value property as before and the taxpayer continues to pay taxes in the same way. But tax collections are now divided between the portion attributable to values in place at the time the TIF district was established and the portion that represents value increases since then. For the life of the TIF district, which may be 20 to 30 years, or even longer,6 taxes on value increases are earmarked for TIF spending or repayment of TIF debt.

In theory, the TIF project requires no new taxes, and it pays for itself by increasing the tax base. Because a finding of blight in the redevelopment

1Jessica Garrison, “Jerry Brown’s Bid to Kill Redevelopment Agencies Sets Stage for a Fierce Battle,” Los Angeles Times, Jan. 15, 2011. In California, tax increment financing is undertaken by redevelopment agencies, or RDAs, and Brown’s proposal is discussed as a plan to eliminate those entities. For example, “California Redevelopment Agencies Need a Complete Overhaul,” Editorial, The Oakland Tribune, Mar. 12, 2011 (“Gov. Jerry Brown . . . has been willing to offer some highly controversial changes in state finances. None is more contentious than his bold proposal to eliminate redevelopment agencies”).


5For example, some states allow limited use of sales tax proceeds to fund TIF initiatives. See Lauren Ashley Smith, “Alternatives to Property Tax Increment Finance Programs: Sales, Income and Nonproperty Tax Increment Financing,” 41 The Urban Lawyer 705 (2009).

6For example, Wisconsin last year extended the potential life of TIF districts to 40 years. John Buhl, “Governor Signs TIF Expansion for Distressed Localities,” State Tax Notes, May 24, 2010, p. 576, Doc 2010-10837, or 2010 STT 94-36. See also text accompanying note 29, below.
area is often required to establish a TIF district, the government investment is considered targeted to a region that would not otherwise attract private capital. From that perspective, TIF is, as Prof. George Lefcoe of the University of Southern California has written, a “win-win-win for the city, the private developer and the taxpayers.” It is no wonder that Sacramento Mayor Kevin Johnson, in opposing Brown’s plan to end TIFs, called these projects “magical things.”

In appropriate situations a TIF can produce exactly those results. A formerly blighted area may blossom, tax valuations may increase as a result, and a strengthened tax base may permit expanded future public services. In other cases, government investment could fail to improve local conditions, while the freeze in future tax base growth could restrict services during the period for repayment, further diminishing the jurisdiction’s economic prospects.

In theory, the TIF project requires no new taxes, and it pays for itself by increasing the tax base.

The promise and popularity of TIF have placed it in a position of enormous fiscal importance. Brown’s proposal signals the need to consider both its risks and potential drawbacks.

Risks and Incentives

The risk of poor performance is inherent in any situation calling for financial judgment. An absence of private investment, which is the justification for government intervention, may also be a signal that the market has not identified development opportunities. In that situation, a number of unsuccessful investments might be the price for undertaking any ambitious redevelopment initiative. A more fundamental concern involves legislative provisions and larger institutional factors that could actually encourage unproductive investments. That constitutes what economists term “moral hazard,” an incentive for misallocation of resources. In 1952 TIF was seen as a means of raising matching funds for federal urban development grants. Several decades later, resourceful local governments facing an era of tax limitations were able to use this tool to support expanded spending in the face of those constraints.

Three structural elements of TIF are especially problematic: the interpretation of blight, the assumption that future increases in property value are caused by the TIF project, and above all the ability of a TIF district to appropriate the future tax base growth of other, overlapping jurisdictions, most notably school districts.

Blight

Many states require a finding of blight for the establishment of a TIF district. Yet, as Lefcoe has noted, truly blighted neighborhoods offer the fewest possibilities for easy increases in property value. Citing an Iowa study that found TIFs to be most successful in “booming suburbs and metropolitan areas,” he commented, “After all, that is where costly new developments have the best chance of being financed, built, and adding greatly to the property tax rolls. . . . TIF funded redevelopment built in distressed areas would seldom boost property values enough for the project to pay its own way.” Nor would an instrument drawing on future value increases be able to support even a successful intervention in truly blighted areas if that project achieved only reduced rates of decline, or even stabilized values — however heroic that accomplishment might be in fact. Over time, blight requirements have been all but ignored in many cases, with cities, courts, and consultants ready to accede to almost comical expansions of that term. Use of TIF as a general funding device and not as a means of assisting blighted neighborhoods is the first step away from its theoretical justification.


See Lefcoe, “After Kelo, Curbing Opportunistic TIF-Driven Economic Development,” supra note 9, at 15-22. One attorney is quoted as saying, “States’ definitions of blight are so broad and vague that they could apply to practically every neighborhood in the country. (‘Blight’ can include such things as a home not having two full bathrooms or three full bedrooms).” Id. at 15. A 2011 audit by the California state controller’s office found that “Even though redevelopment agencies must spend their money on improving ‘blight,’ Palm Desert dedicated almost $17 million in redevelopment dollars to improve a luxury golf resort.” Tracy Seipel, “California Redevelopment Agencies Blasted in State Review,” Mercury News (San Jose), Mar. 7, 2011. “Near San Diego, Coronado’s redevelopment area covers every privately owned parcel in the city, including multimillion dollar beachfront homes.” Judy Lin, “Audit Faults California Redevelopment Agencies,” The Boston Globe, Mar. 7, 2011.

Grimes, supra note 4
Causation

About 20 states require a finding that new development would not take place in the TIF district “but for” government intervention. That has been treated as even more of a formality than a finding of blight. Blight, however subjective, at least refers to an observable physical attribute. The counterfactual prediction of what would happen but for establishment of a TIF district is so open to conjecture as to invite disregard. Because this finding is often left to the municipality establishing the TIF district, there is no incentive for an independent review. As Prof. Richard Briffault has written, “The conceptual heart of TIF is that the TIF expenditure is the but-for cause of subsequent economic growth in the TIF district. . . . But for the most part, as TIF has spread the but-for requirement has fallen away.”11

Tax Base Growth

The inability to predict what would happen in the absence of TIF undermines its theoretical basis as a self-financing device that does not raise taxes. The assumption that tax base growth is caused by TIF justifies earmarking the tax base increment to pay for that development, and lies behind the claim that TIF allows new spending with no tax increase. But it is extremely difficult to prove a specific cause for any change in property value. A municipality may have an incentive to draw the boundaries of the TIF district as widely as possible, including development that may be unrelated to the TIF investment. And value increases resulting only from general growth or inflation cannot be attributed to the TIF. If tax base growth that reflects inflation is allocated to the TIF district, the jurisdictions that depend on the property tax for basic funding may have to raise their tax rates or face budget shortfalls. Many local government budget items, such as health insurance for public employees, can rise at rates well above that of inflation.

The assignment of future valuation increases to the TIF district can encourage municipalities to target undeveloped land or other property with low assessed values, particularly agricultural land eligible for preferential farmland programs. Those areas may not be blighted or underserved by private developers, but they may offer dramatic increases in assessed value simply by being reclassified as commercial or industrial. “A 1999 study found that 45 percent of Wisconsin’s 661 TIFs have been used to develop open space — primarily farmland — including, most famously, a Wal-Mart Supercenter built on what had been an apple orchard. . . .”12 Moreover, many jurisdictions reassess property on a multiyear basis. For example, in Illinois, Cook County uses a three-year cycle, reassessing the northern suburbs one year, the southern suburbs the next, and the city of Chicago in the third year. In this situation, designation of a TIF district just before reassessment can ensure an increment that has nothing to do with the TIF investment.

The inability to predict what would happen in the absence of TIF undermines its theoretical basis as a self-financing device that does not raise taxes.

A plethora of economic studies have reached no consensus as to the effect of TIF on economic growth. That is unsurprising, given the enormous variety of circumstances, regions, and types of projects at issue. Some studies have even found negative effects for TIF designation. For example, Profs. Richard Dye and David Merriman undertook a major analysis of 235 Chicago-area municipalities and concluded that “property values in TIF-adopting municipalities grew at the same rate as or even less rapidly than in nonadopting municipalities.” They reported that a second study three years later did not find “the earlier provocative result of a significantly negative impact of TIF adoption on growth, but we still find no positive impact of TIF adoption on the growth in citywide property values. Any growth in the TIF district is offset by declines elsewhere.”13 Analysts who have reviewed the voluminous literature on that point generally agree that “research on the effects of TIF has raised more questions than it has answered.”14 “The effect of TIF on property value growth at the municipal level thus remains unresolved,”15 Prof. Paul Bryne wrote. Briffault concluded, “There is little clear evidence that TIF has done much to help the municipalities that use it, while it is a source of intergovernmental

11Briffault, supra note 3, at 77.
12Id. at 72, citing Greg LeRoy, “TIF, Greenlands, and Sprawl: How an Incentive Created to Alleviate Slums Has (Footnote continued in next column.)
15Byrne, supra note 2, at 319.
tension and a site of conflict over the scope of public aid to the private sector.”

**Overlapping Jurisdictions**

By far the greatest moral hazard posed by TIFs concerns the ability to freeze the assessment base of overlapping jurisdictions, such as school districts. The municipality establishing the TIF district may be able to appropriate value increases, including those resulting only from inflation, from independent districts with no power to block that transfer. Just as tax credits and deductions can make it rational to construct an otherwise uneconomic building, the ability to draw on the tax base of separate jurisdictions provides an incentive for expenditures that would not be approved if funded by the municipality itself. In fact, a municipality may have an incentive to set up a TIF even if it reduces growth. As Profs. Richard Dye and Jeffrey Sundberg explain:

> With a positive pre-TIF rate of growth, the district is able to "capture" that portion of the growth in property value for use in TIF financing.

This points out what we consider to be one of the gravest flaws in TIF. If property values would grow at a high rate in the absence of TIF, even a project that results in a permanent reduction in the growth rate would be easy to finance. Policy makers unused to the concept of opportunity cost might be susceptible to making a poor decision if financial viability is confused with efficiency.17

The importance of tax base capture is such that, as Lefcoe said:

> In states where local governments have no opportunity to pledge tax increments from other taxing entities such as counties and school districts, there is very little TIF... Why have so few states granted schools, counties and other taxing entities the right to opt out of sharing their tax increments? The short answer probably lies in an analysis of the lobbying effectiveness of redevelopment agencies, schools and counties.18

---


---

**By far the greatest moral hazard posed by TIFs concerns the ability to freeze the assessment base of overlapping jurisdictions, such as school districts.**

The effect on school districts provided a major impetus for Brown’s proposal to end TIFs in California. As Prof. Tracy Gordon wrote, “The catch is that the money has to come from somewhere. In California, the state is on the hook for property taxes that would have otherwise gone to schools.”19 Even 10 years ago, California TIF districts were estimated to receive 10 percent of all property tax revenue in the state, or $2.1 billion annually, and to have accumulated $51 billion in bonded indebtedness.20

---


18Lefcoe, supra note 7, at 25, 32.


the failure of these systemic protections is of perhaps even greater concern than a wishful legislative rationale for new enactments. At the most general level, clarity and transparency are essential to citizen oversight, but many TIF programs are largely hidden from taxpayer notice. At a very specific level, debt limits and a requirement of voter approval constitute a deliberate check on municipal borrowing, but legislatures, courts, and local officials have generally circumvented those measures by agreeing that bonds secured by tax increment financing do not constitute debt for those purposes.

Transparency

Lefcoe observes, “Development agencies often keep the public in the dark about their transactions.”21 The concept of self-financing can lend legitimacy to politically expedient nondisclosure. If in theory taxpayers are not required to make any new payments for those projects, lack of public participation or even awareness becomes less problematic. In the same way, the assumption that all future tax base growth is due to TIF investment helps justify the exclusion of overlapping jurisdictions from the decision to earmark that growth for TIF development. That theory presents the TIF process as a closed circuit: “The incremental revenues pay for the public expenditures, which induce the private investment, which generates the incremental revenues, which pay for the public expenditures.”22 Yet a frozen tax base is likely to require higher tax rates, new fees, or other mechanisms to fund ongoing government operations.

Judicial Oversight

Although courts can also provide institutional protection against abuse, judicial oversight has played little role in TIF developments. That may reflect the goodwill naturally extended to an apparently self-financing program to assist blighted areas. Also, lack of public awareness reduces the likelihood of taxpayer challenges to TIF programs. When even public officials do not understand TIF provisions, it is extremely difficult for taxpayers to evaluate their impact. The professionals most familiar with these complex structures may have a vested interest in avoiding conflict over them. For example, as Lefcoe says regarding blight determinations, “The attorneys most capable of filing such challenges are jeopardizing their future dealings with the city officials they sue and with officials in other cities who get wind of their whistle-blower-like behavior.”23 And once TIFs became the primary instrument for municipal redevelopment and even development, the sheer magnitude of those investments, and the rise of entire businesses and professions assisting in their implementation, placed an extremely heavy burden on efforts to change their method of operation. A 2007 Florida Supreme Court decision characterizing TIF as debt would have required voter approval of TIF bonds. The court ruled three weeks later that its decision was not retroactive, and it reversed itself entirely the following year.24

What Is Debt?

The Florida decision dealt with the underlying challenge of characterizing debt for legal purposes. Nearly every state imposes statutory or constitutional limitations on the amount of debt municipalities may incur, and most require a voter referendum for such general obligation borrowing.25 Revenue

---


25For a discussion of the 19th-century background to debt ceiling and referendum requirements, including state and local borrowing for railroad, canal, and other commercial projects, see Philip J. F. Geheb, “Tax Increment Financing Bonds as ‘Debt’ Under State Constitutional Debt Limitations,” 41 The Urban Lawyer 725, 732-733 (2009). Note 47 of that article cites work by Prof. M. David Gelfand describing the New York City fiscal crisis of the Boss Tweed era in the 1870s and the resulting twenty years it took for the City to extricate itself from the debts it incurred as a result of corruption and special interest capture.” M. David Gelfand, “Seeking Local Government Financial Integrity Through Debt Ceilings, Tax Limitations and Expenditure Limits: The New York City Fiscal Crisis, the Taxpayer’s Revolt, and Beyond,” 63 Minnesota Law Review 545 (1979). This year Prof. John Wallis told The Wall Street Journal that current state debt provisions can be traced “back to those defaults in 1841, after which legislators amended constitutions to clamp down on new borrowing. Over time, these rules have been perverted by politicians, meaning that constitutional rules have made it harder to raise taxes than to raise expenditures.” . . . When the defaults began in January 1841, investors dumped state bonds, pushing yields above 12% in early 1841, and to nearly 30% by 1842. The consequences of those defaults would last for decades: Among historians, the rule of (Footnote continued on next page.)
bonds secured by a new and segregated source of funds, such as tolls for a highway or bridge to be built with bond proceeds, have long been exempt from those provisions, which are designed to protect general tax revenue. TIF debt has similarly been free of those requirements, most crucially the need for a public vote on bond issues. That can be justified on the theory that it too is secured by a segregated account. But in this case, the account consists of future growth in the basic property tax revenue that supports such general government functions as education, public safety, and transportation.

Criticism of the referendum requirement generally focuses on its costs and the barriers it places in the path of worthy projects. Philip Geheb writes, “In response to these criticisms, state courts have developed judicial doctrines that evade constitutional debt limitations. . . . In the last twenty years, judicial complicity with state and local officials has freed local governments to increase the number of TIF applications and push it from a ‘fringe’ development finance tool to a mainstream public finance method.”26 Yet the public has not been averse to supporting the issuance of debt for specific purposes. For example, Profs. H. Spencer Banzhaf, Wallace Oates, and James Sanchirico studied more than 1,500 local referenda held between 1998 and 2006 dealing with open space conservation, and found that more than three-quarters of them were approved by voters.27

The legal classification of borrowing secured by taxes on value increments as something other than general obligation debt reflects the larger problem of characterizing and accounting for future liabilities. Legislative and judicial interpretation may have excluded TIF claims on future tax receipts from this category of debt, but the effect on local governments...

---

...-thumb is that U.S. states would pay interest rates one percentage point higher than Canadian issuers the rest of the 19th century. To this day, Mississippi hasn’t paid back some of those bonds, even after a 100-year English bid to collect . . . . For Mr. Wallis, the lessons of the 1840s are bracingly clear. Taxpayers and politicians have lost the connection between borrowing and costs. So taxpayers must be willing to approve tax rises as a direct part of new borrowing plans. There is nothing wrong with raising taxes to support government services that voters want and are willing to pay for,” he says. But government needs to be set up “so that both voters and legislators are forced to make decisions about taxing, spending, and borrowing simultaneously.” Dennis Berman, “When States Default: 2011, Meet 1841,” The Wall Street Journal, Jan. 4, 2011.


that must deal with reduced future revenue may not be the less constraining for that reason.

The Chicago Example

Chicago presents an important case study of the potential benefits and pitfalls of TIF programs. The city has made use of TIF on an extremely large scale, with Mayor Richard Daley repeatedly calling it “the only game in town.”28 At the same time, its academic community has undertaken major studies of the effect of TIF development, and its investigative journalists have examined the political process of TIF approval and operation in great detail.

The Central Loop TIF, perhaps the nation’s largest, was established in 1984 under Mayor Harold Washington to finance investment in the notoriously hard-to-develop Block 37, a parcel bounded by Washington, State, Randolph, and Dearborn streets. The mayor predicted that the TIF could be closed by 1995. In fact, it was expanded in 1997 to include the area bounded by Wacker Drive, Michigan Avenue, Congress Parkway, and Franklin Street. Before it was terminated in 2008, the TIF brought in more than $1 billion in revenue, including $365.5 million in the final year alone. Meanwhile, the development of Block 37 remained unfinished. That experience is not unique. Gordon has written:

Once redevelopment areas are born, they rarely die. For example, Los Angeles officials created the Hoover Redevelopment Project in 1966 to improve the area surrounding the city’s Memorial Coliseum. In 2004, 35 years before the project was due to end in 2039, state lawmakers extended it to 2051. . . . As a Senate staff analysis noted at the time, “[T]he committee may wish to consider why it should [take] Los Angeles officials a century to redevelop the Hoover neighborhood.”29

In 2006 Chicago established a new TIF, LaSalle Central, in the financial district just west of the Central Loop, projected to accumulate more than $2 billion in revenue before it expires in 2029.30 In 1997 Chicago had 41 TIF districts; in the next four years, it created 86 more.31 At the beginning of 2009, the city had more than $1 billion in TIF funds on hand, compared with an official city budget of $6 billion.32

The large number of taxing entities within Cook County gives the city of Chicago a special incentive to appropriate those jurisdictions’ future tax base...

28Briffault, supra note 19.
29Tracy Gordon, supra note 19.
30Jeremy Thompson, Jason Liechty, and Mike Quigley, A Tale of Two Cities: Reinventing Tax Increment Financing, Apr. 2007, p. iii.
31Id. at 1.
growth through TIF designation. There can be as
many as 15 overlapping jurisdictions in the city,
including the Board of Education, the Chicago Tran-
sit Authority, the Chicago Park District, the Com-
munity College District, the Health and Hospital
Commission, and Cook County itself. Moreover, Illinois legislation allows a municipality special free-
dom in TIF operation. For example, although gerry-
mandering of TIF districts is not uncommon, Illinois
is remarkably lenient in allowing revenue from one
TIF district to be spent in another.

Daley's support for TIFs as the "only game in
town" faced no significant opposition during his
tenure. The institutional factors that diminish over-
sight, such as lack of transparency and the absence
of legal challenges, combined with public approval
for new development and successful downtown revi-
talization, were especially strong in Chicago. Cook
County Commissioner Mike Quigley undertook a
review of TIF procedures, culminating in a major
public report in 2007. None of his recommended
reforms was adopted. His proposal to include TIF
information on property tax bills failed at a county
board meeting presided over by Finance Chair John
Daley, the mayor's brother. When Quigley ad-
ressed Illinois legislators on TIF reform, the mayor
sent several Chicago aldermen to rebut his argu-
ments. After Quigley was elected to Congress, no
other local official took on the challenge of reforming
TIFs in Chicago.

Illinois law requires creation of a Joint Review
Board (JRB) composed of representatives of affected
jurisdictions and special districts to vote on TIF
proposals. But as Quigley wrote, "In practice, how-
ever, the JRB barely scrutinizes the TIF proposals
that come before it, and has never voted one down.
With the exception of Cook County, all JRB members
are in effect representatives of the mayor of Chi-

Similarly, all 15 members of the Community
Development Commission (CDC) charged with over-
sight of TIF projects are appointed by the mayor.
The CDC has provided almost unanimous approval
of city proposals. Of the 812 votes cast by its mem-
bers between November 2005 and April 2007, 808
were affirmative, and no item failed to carry a
majority. Quigley's report states, "We have to con-
clude that the CDC functions as a rubber stamp,
exercising little actual oversight. . . . Four commis-
sioners have been present for fewer than half of the
votes taken since November 2005. One commis-
ioner whose name has been read during 95 roll calls
has been present for just three of them. Again,
that situation is not unique to Chicago. In Mary-
land, The Daily Record undertook a detailed exami-
nation of the New East Baltimore development
project, headed by East Baltimore Development Inc.
(EBDI). "The Daily Record's investigation found
that The New East Baltimore's public funding is so
complex and poorly scrutinized that local elected
officials, some of whom serve on EBDI's board, said
they had little grasp of the $108.5 million in city
funds committed to the project."40

Many TIF programs lack transparency, but the
Chicago situation is extreme. Journalists investigat-
ing TIFs reported, "Of the 11 aldermen who spoke
with us about their TIF meetings, none was allowed
to see the entire TIF budget — they were shown the
revenues and expenditures planned for their wards
alone and asked to sign off."41 Quigley's report
states, "The near total lack of public information
readily available on Chicago's TIFs is, in a word,
inexcusable. . . . Why this should be so is perplexing,
but the process one must go through just to get a
minimally clear picture of TIF in Chicago requires
time and fortitude average citizens simply don't
have."42

Without oversight or opposition, it can be hard to
resist the use of TIF revenue for short-term needs.
Chicago TIF funds were used for job training and
street cleaning because, as one alderman said,"Streets and San is being shortened every day."43
This is particularly ironic, because by 2005 the TIF
budget for Chicago was greater than that of the
entire Streets and Sanitation and Transportation
Department.44 By 2005, 10 percent of all property
taxes in Chicago were earmarked for TIF purposes,
and TIF districts covered more than one-quarter of the city’s area, causing overlapping entities to lose hundreds of millions of dollars in revenue. Quigley’s report estimated that TIF caused a 4 percent rise in Chicago property taxes, but a flyer distributed by the city’s Department of Planning and Development, “Tax Increment Financing: Myth/Reality,” stated, “Myth: TIF will increase my taxes. Reality: TIF produces more tax revenue by encouraging growth in the neighborhood and expanding the tax base, but it does not change the way your taxes are assessed or change the way you pay taxes.”

**Borrowing From the Future**

Debt finance has an important place in funding long-term capital projects. However, the TIF experience gives dramatic evidence that the ability to spend against future revenue for unspecified purposes with little oversight presents opportunities for excessive borrowing. Chicago’s recent experience has also offered examples beyond TIF of that danger.

In 2004 Daley decided to lease the Chicago Skyway, a 7.8-mile toll road connecting the western Indiana suburbs with the Dan Ryan Expressway to downtown Chicago. In 2005 a private consortium paid $1.83 billion for a 99-year concession to operate the Skyway and collect its tolls. Political opposition was diminished in part because although the Skyway had been operated as a Chicago municipal department, most of its users were commuters from eastern Illinois suburbs and western Indiana, and not Chicago voters. The proceeds were allocated primarily to repayment of municipal debt and establishment of an $875 million reserve fund, with $100 million spent on current outlays.

In 2008 the city sold the rights to collect its parking meter revenue for the next 75 years for $1.15 billion, with the intent of putting the proceeds into a long-term reserve fund whose interest would help replace the $20 million in lost annual parking meter revenue. In fact, nearly all that amount was spent within one year. Daley had “no qualms about raiding reserves he once called untouchable, in part, to dole out $200 grants to hard-pressed homeowners.” That led one alderman to cast his first “no” vote on a Daley budget in 16 years. “The parking meter money was billed as a ‘perpetual replacement fund’ when the 75-year lease was rammed through the council a year ago. We have breached our fiduciary duty to taxpayers. You can’t break a contract in 12 months that’s supposed to last for 75 years. It’s unconscionable. It’s irresponsible. It’s disingenuous. The decision to raid this fundamental asset is mind-boggling.” The budget approved at the end of 2009 left only $773 million of the combined $3 billion realized from the lease of the Skyway and the sale of parking meter rights.

In 2011 David Brunori wrote in *State Tax Notes*, “In 2007, I mentioned that the city of Chicago was considering leasing its parking meters. In 2008 it leased the 36,000 parking meters for 75 years for $1 billion. Morgan Stanley later then sold the lease to Abu Dhabi. The emirate has complete control over the city’s parking meters and has ended free parking on holidays.”

**Illinois**

Chicago’s problematic use of debt is reflected and magnified at the state level. In February Illinois sold $3.7 billion in bonds to “hedge funds, mutual funds, and non-U.S. buyers” to make a legally required payment to its public employee pension plan. The Illinois bond rating is one of the lowest of the 50 states, and those bonds carried an interest rate approximately 2 percentage points greater than would be required from a private company with a similar bond rating. That same month, Gov. Pat Quinn (D) announced plans to issue more than $8 billion in bonds to pay past-due bills, such as amounts owed to state vendors. The governor said, “This is not, not new borrowing. Billions of dollars of existing bills will not go away by magic.” The past-due bills are already in existence, but the declaration that an $8 billion bond offering is “not, not new borrowing” has a through-the-looking-glass quality.

From the mayor of Sacramento to the governor of Illinois, magic seems to figure heavily in considerations of debt. More than 70 years ago, the philosophy of legal realism sought to demystify judicial decision-making by removing it from the realm of

---

46 Id. at 6, 9.
47 Id. at 1, 48.
50 Id.
53 Id.
55 “When I use a word,” Humpty Dumpty said, in rather a scornful tone, ‘it means just what I choose it to mean — neither more nor less.” Lewis Carroll, *Through the Looking-Glass*, chap. 6 (1871).
scholasticism, first principles, and natural law. In his enormously influential article, “Transcendental Nonsense and the Functional Approach,” Felix Cohen mocked the idea of “magic ‘solving words’” such as “property rights,” “fair value,” and “due process.” “Legal arguments couched in these terms are necessarily circular, since these terms are themselves creations of law, and such arguments add precisely as much to our knowledge as Molière’s physician’s discovery that opium puts men to sleep because it contains a dormitive principle.” The magic solving words of “debt” and “borrowing” have been much in evidence in creative finance, including TIF, in recent years.

From another perspective, perhaps Quinn can be interpreted as acknowledging that functional, rather than technical, borrowing does not occur when the state undertakes a bond offering, but rather at an earlier time when it enters an obligation for which it lacks funding. Dye and Merriman term this “implicit borrowing.” They write, “Past choices to implicitly borrow by not putting aside sufficient funds to cover future pension liabilities have made Illinois pension underfunding the worst in the nation.” In this view, debt might include all varieties of payment obligations, whether or not technically subject to legislative and constitutional restrictions and referendum requirements.

After the first generation of tax limitation measures, much spending was supported by borrowing that avoided the magic solving word of “debt.” Leasing parking meters, sale of an expressway, and borrowing secured by taxes on future value increments can avoid classification as debt for specific legal purposes. Unfortunately, the name given to those fiscal instruments does not change the experience of repayment. Motorists paying increased tolls, drivers whose parking fees have quadrupled, taxpayers called on to honor unfunded pension obligations, or property owners facing higher tax rates because of a frozen tax base do not bear less of a financial burden because what they are repaying is not termed “debt.” If the cycle of tax limitations was followed by a cycle of borrowing that was not classified as debt, the next cycle, that of repayment, will require political, legal, and economic expertise to help local governments through this transition without the aid of magic.

———

57Richard F. Dye, Nancy W. Hudspeth, and David Merriman, “Titanic and Sinking: The Illinois Budget Disaster,” The Illinois Report 2011, Institute of Government and Public Affairs, University of Illinois (2011), at p. 29. This report is subtitled, “It is hard to overstate the depth of the fiscal hole the state is in.”

(Footnote continued in next column.)