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Lower Hill Development No Longer Using a TIF: So What Now?

Redeveloping the Lower Hill District, where once stood the Civic Arena, or in its later years the renamed Mellon Arena, has taken an interesting new twist. Instead of relying on the creation of a tax increment financing (TIF) district, the City has decided instead to create a tax abatement district. The latter is made possible via the local economic revitalization tax assistance act of 1977 (Act 76), commonly known as a LERTA. Why the change?

As we wrote in a *Policy Brief* last fall (*Volume 14, Number 48*), with a TIF, a bond (or bonds) would have been issued against the future property tax payments from the completed development. Any subsequent increase in tax payments resulting from the project, compared to payments from the development area prior to the project, would have been used to pay off those bonds. The downside is that if the development fails to generate enough of an increment in property taxes to satisfy the debt issue, taxpayers would then be on the hook for those bonds, or bond insurance would pay, possibly resulting in a downgrade of the issuing body's credit rating that could affect the cost of future projects.

This happened to the City when the Lazarus department store TIF project failed. To refresh a distant memory, the Lazarus development project used $56 million in public funds yet had a market value of only $21 million upon completion (see *Policy Brief, Volume 1, Number 2*). Not only did this not generate enough property tax to satisfy the bond repayment, the store performed poorly, Lazarus's parent company declared bankruptcy and closed the store just a few years after opening.

Nonetheless, TIF areas have been a popular way for governments to finance "infrastructure components" of economic development projects. So why did the City change its mind about using TIF?

The Mayor's vision for the Lower Hill Development presented a problem. Bear in mind that the scheme was not only to develop the 28 acres comprising the former Civic Arena and parking lots, but also to use TIF revenue in a program to pump money into the rest of the Hill District (Middle and Upper) for programs such as job training and capital improvements. Inconveniently for the City, incremental property taxes realized after the development is completed must be used to pay off the bonds issued for the project's costs, or if there is a surplus beyond the amount required for debt service it must be returned to the taxing bodies. The language of the Tax Increment Financing Act of 1990 (revised 1992), Section 7 part (c) states; "(t)o the extent that any moneys remain in the fund after all forgoing costs have been paid or satisfied, the remaining moneys shall be distributed on an equal basis to all municipalities and school districts which participated in the tax increment district." Clearly, a TIF would not accomplish the Mayor's goal—so it was abandoned and replaced by a LERTA.

LERTA provides for property tax abatements for individual parcels within the development area. The guidelines are laid out in Act 76. A tax exemption can be granted by the local taxing authority; however, the length of the abatement shall not exceed ten years, applies just to that parcel and is transferable. It is done to encourage development in an economically depressed community.

The local taxing authority has some leeway in setting its own guidelines. The City of Pittsburgh has put together a table outlining the real estate abatement programs available, including those under the LERTA program for both commercial and residential developers effective as of September 2014[1]. For a commercial LERTA, the abatement period is five years and the annual abatement limit is $50,000. *This represents a tax credit as opposed to an assessment reduction*. For a residential LERTA, the abatement period is ten years for a $150,000 per year tax credit.

The Pittsburgh Public School District has also indicated it will participate in the residential abatement in the Lower Hill project for ten years at $250,000 per year. However, according to the table, the School District's abatement decreases over time. Unchanged for the first two years it then declines by ten percent every two years afterward so that in the final two years the abatement is 60 percent of the original amount.

The current table does not list the County as a possible participant. However, in a previous version of the table (effective 12/2012) the County was listed as participating in the residential LERTA, agreeing to abate $100,000 on the same schedule as the School District. Of course for the kind of project the Mayor has in mind, he will need both the School District and County to participate.

According to news reports, the 28 acre project has a planned value of $440 million when completed. As mentioned above, local taxing authorities have leeway in setting the LERTA parameters. The Urban Redevelopment Authority (URA), the agency that will be overseeing the development, was asked to approve an amended LERTA for the Lower Hill Development at a special board meeting on January 26th—it passed unanimously. Under the new parameters the maximum abatement ceiling is now $750,000 per year. However, it is unclear if this is for residential, commercial, or both. The overall LERTA is to last 25 years, even though each individual parcel can use the abatement for only ten years so the project will effectively have to roll out in sections. As of this date, none of the three taxing bodies have officially approved the amended LERTA plan.

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[1] http://apps.pittsburghpa.gov/finance/Current_Abatement_ProgramTable_effective_8-1-14.pdf

However, there is a major wrinkle in this LERTA plan. Interestingly, while property owners will not be required to make real estate tax payments to the taxing authorities, they will have to make annual payments equal to the abatement into two funds: a reinvestment fund for other projects around the Hill District, and a development fund to help out with infrastructure improvements or to subsidize development. The URA is estimating that each fund will accumulate about $20 million. The only exception is for US Steel which has placed $3 million into the reinvestment fund, as opposed to half of the annual abatement, while the other half of their abatement will be used to subsidize their own project. Will that same deal apply to other developers/owners? Will it even be offered? Will the owners demand it?

Assuming the US Steel arrangement is unique, what is the benefit of the LERTA for other developers/property owners? The purpose of the LERTA abatement is to encourage development in economically depressed areas by giving property tax breaks as an incentive. If the property owners are required to pay into special designated funds instead of receiving the tax abatement, where is the incentive from the LERTA for developers? In effect, the taxing bodies will be using a complicated scheme to divert what ordinarily would be tax revenues into funds that could easily become a slush fund ripe for abuse.

But even if that concern is not to be heeded, why not just have the taxing bodies agree to put some tax revenues in the designated funds and avoid the whole LERTA complication? Finally, if the project succeeds in creating many good jobs and large increases in tax revenue for the three taxing bodies, why not let it help the taxing bodies with much needed revenue for municipal operations and education?

If the project is as successful as the promoters say it will be, it will breed more private development that will not require public money. What a novel approach that would be for Pittsburgh.

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