# AN OVERVIEW OF ARKANSAS TAX INCREMENT FINANCING DISTRICT LAW

Tax increment financing districts, otherwise known as "redevelopment" or "TIF" districts, are used in many states as an economic development tool. While fairly new in Arkansas, TIF districts have enjoyed an eventful existence. This article discusses the brief history of TIF districts, the fundamental structure of TIF law, and recent changes to TIF law enacted in the 2005 Arkansas General Assembly.

## Arkansas Constitutional Amendment 78

Arkansas voters adopted Amendment 78 to the Arkansas Constitution in the 2000 general election. This constitutional amendment granted cities and counties the authority to form TIF districts, and to issue bonds in order to finance redevelopment projects.[1] Redevelopment projects are defined in Amendment 78 as any project "for eliminating, or preventing the development or spread of, slums or blighted, deteriorated, or deteriorating areas, for discouraging the loss of commerce, industry or employment, or for increasing employment".[2]

Under Amendment 78, all or a portion of ad valorem taxes (referred to herein as "property taxes") levied by taxing units with property located in the TIF district may be diverted to the TIF district to pay for redevelopment bonds. The amendment sets forth the primary intent of tax increment financing – only property taxes levied against the increase in the assessed value of property located in the TIF district are eligible to be used for redevelopment projects.[3]

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[1] ARK. CONST. AMEND. 78, §1(a), (b).

[2] ARK. CONST. AMEND. 78, §1(a).

[3] ARK. CONST. AMEND. 78, §1(d).

Notably, Amendment 78 declines to define the term "taxing unit,"[4] and Amendment 78 contains a general repealer clause.[5]

**Act 1197 of 2001**

Act 1197 was enacted by the 2001 Arkansas General Assembly to implement the provisions of Amendment 78. Under Act 1197, cities, counties or any other legislative body governing a local government (a "local governing body"[6]) are granted the ability to create TIF districts, and are given broad powers to achieve the objectives of the TIF law.[7] These powers include: (i) the ability to enter into any contracts or agreements, determined by the local governing body as necessary to effectuate the purposes of the TIF district; (ii) perform improvements to property, or contract for the development, redevelopment or rehabilitation of property; (iii) construct public facilities or improvements in connection with a redevelopment project, such as water or sewer facilities, private or public roads, or other public improvements; and (iv) construct capital improvements to be leased or sold to private entities in connection with the objectives of the redevelopment project.[8]

To establish a TIF district, the local governing body must first designate the boundaries of the TIF district.[9] The local governing body can make this designation on its own initiative,

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[4] Id.

[5] ARK. CONST. AMEND. 78, §1(f).

[6] Ark. Code Ann. §14-168-301(7).

[7] Ark. Code Ann. §14-168-304.

[8] Id.

[9] Ark. Code Ann. §14-168-305(a).

upon the request of affected property owners, or upon the request of the city planning commission.[10]

After the local governing body selects the boundaries of the district, it must hold a public hearing to take input from the public about formation of the district and the proposed boundaries.[11] Notice of the hearing must be sent to the chief executive officer of any governmental entity who has power to levy taxes on the property within the proposed district boundaries, and to any school district owning property within such boundaries.[12] After all notices are sent, the local governmental body must also publish notice of the hearing at least fifteen (15) days before the hearing.[13]

After the hearing, if the local governing body determines the property will be benefitted by redevelopment, the local governing body must pass an ordinance that establishes the TIF district, sets forth the pertinent information regarding the district and its boundaries, and establishes a separate fund for deposits of tax increment revenues and payment of project costs.[14] Act 1197 contains several items which fall under the definition of "project costs," such as the cost of constructing public improvements, as well as any work associated with such improvements, such as demolition of existing buildings, parking and landscaping, site clearing

[10]Ark. Code Ann. §14-168-305(a).

[11]Ark. Code Ann. §14-168-305(b)(1).

[12]Ark. Code Ann. §14-168-305(b)(2)(B).

[13]Ark. Code Ann. §14-168-305(b)(2)(A).

[14]Id.

and preparation.[15] Project costs also include financing costs (i.e. interest paid to noteholders or bondholders, and expenses related to issuance of bonds), and professional service costs (i.e. architectural, legal and engineering expenses).[16] In addition to the items statutorily defined as project costs, the local governing body has the power to perform all actions set forth in Ark. Code Ann. §14-168-304, the statutory provision granting local governing bodies powers with respect to TIF districts.

The local governing body then has to prepare (or cause to be prepared) a project plan for approval by the local governing body.[17] As set forth in Act 1197, requirements of the project plan include an economic feasibility study, descriptions of the costs and financing of the project, details regarding redevelopment bonds, and certified information from the county tax assessor on property values and ad valorem tax rates in the TIF district.[18] The local governing body must hold a public hearing to allow public input on the project plan, with notices provided in the same manner as for the TIF district boundary hearing.[19] After the hearing, the local governing body must approve the project plan by passage of an ordinance, stating the project is economically feasible.[20]

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[15] Ark. Code Ann. §14-168-301(9).

[16] Id.

[17] Ark. Code Ann. §14-168-306(a)(1).

[18] Ark. Code Ann. §14-168-306(b)-(c).

[19] Ark. Code Ann. §14-168-306(e)(1), (2).

[20] Ark. Code Ann. §14-168-306(e)(2).

A local governing body may issue redevelopment bonds to pay for project costs.[21] The redevelopment bonds shall be repaid from the tax increment deposited in the TIF district's special fund.[22] Other funds in addition to tax increments, such as payments in lieu of taxes, can be contributed to the special fund for bond repayment.[23] Issuance of such bonds must be authorized by ordinance.[24] Under Act 1197, the maturity date of redevelopment bonds issued by a TIF district must not exceed the earlier of: (i) twenty five (25) years from the date of issuance; or (ii) the termination date of the TIF district.[25]

Act 1197 outlines how property taxes are to be divided among taxing units and a TIF district. Act 1197 defines a "taxing unit" as any city, county, school district or community college district. The tax assessor distributes property tax revenue among taxing units and the TIF district as follows:

(i) The tax assessor determines the total millage rate of all taxing entities (for example, 50 mills). This millage rate is multiplied by the assessed value of the property within the TIF district, as of the most recent assessment prior to formation of the TIF district (the "base value").[26] The taxing units continue to receive this amount of property tax revenue even after creation of the TIF district. Therefore, if the property tax revenue received by taxing units was

[21] Ark. Code Ann. §14-168-315.

[22] Id.

[23] Ark. Code Ann. §14-168-313.

[24] Ark. Code Ann. §14-168-316.

[25] Ark. Code Ann. §14-168-317(b)(1).

[26] Ark. Code Ann. §14-168-312(a)(3)(A).

$1,000.00 prior to formation of the TIF district, taxing units would continue to receive $1,000.00 per year for the life of the TIF district;

(ii) The tax assessor then determines the portion of the total millage rate that has been pledged for debt service payments on or before January 1, 2001 (for example, 5 mills). This millage rate is multiplied by the assessed value of the property within the TIF district, as of the most recent assessment after formation of the TIF district (the "current value").[27] The applicable taxing unit which receives such mills for debt service continues to receive this amount of property tax revenue until the preexisting debts are satisfied; and

(iii) The tax assessor then determines the difference between the total millage rate and the millage rate for debt service (i.e. 50 mills - 5 mills = 45 mills). This millage rate is multiplied by the difference, or increment, in the base value (assessed value prior to district formation) and the current value (most recent assessed value after district formation).[28] The TIF district receives this amount of property tax revenue. Therefore, if the property tax revenue was $1,000.00 prior to formation of the TIF district, and the net property tax revenue for the year after TIF district formation was $10,000.00, the TIF district would receive $9,000.00 for that tax year.

**Arkansas Attorney General Opinions**

Until early 2005, attorney general opinions provided the only interpretations of TIF law. In December 2001, Attorney General Mark Pryor issued Opinion No. 2001-295, which discussed whether any portion of the twenty five (25) mills levied by Amendment 74 could be used to

[27] Ark. Code Ann. §14-168-312(a)(3)(B).

[28] Ark. Code Ann. §14-168-312(a)(3)(C).

repay TIF district obligations.[29] Amendment 74, adopted in the 1996 general election, established a "uniform rate of tax" of twenty five (25) mills to be remitted to the state, and then distributed back to school districts solely for the maintenance and operation of schools."[30]

Attorney General Pryor's opinion recognized an argument could be made that property taxes levied pursuant to Amendment 74 are levied by the state itself.[31] Since Act 1197 did not include the state in its taxing unit definition, it was debatable whether Amendment 74 taxes were protected from Amendment 78 uses.

On the other hand, Attorney General Pryor noted Amendment 78 did contain a general repealer clause, which could have the effect of repealing the protections of Amendment 74. In addition, the Attorney General questioned the argument that tax revenues intended for schools should not be used for TIF districts, since school districts are specifically included in the "taxing unit" definition in Act 1197.[32]

Attorney General Pryor declined to provide a conclusive answer on the issue. However, the opinion did state that Amendment 78 authorized the diversion of "all or a part" of property taxes, and concluded that the General Assembly simply had not clarified its intent in current legislation.[33]

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[29] Op. Ark. Att'y Gen. No. 2001-295 (Dec. 1, 2001).

[30] ARK. CONST. AMEND. 74, §1(b).

[31] Op. Ark. Att'y Gen. No. 2001-295 (Dec. 1, 2001).

[32] Id.

[33] Id.

Attorney General Beebe has issued several opinions which interpret certain areas of TIF law. In Opinion No. 2003-103, the Attorney General opined that an undeveloped area could qualify for a TIF district under Act 1197.[34] In providing this opinion, the Attorney General noted the broad scope of Amendment 78, and stated there was no limitation set forth in the constitutional language which inferrred an exclusion of undeveloped property for use as a redevelopment project. Attorney General Beebe also cited the definition of a redevelopment project in Act 1197, which included the development, redevelopment, revitalization or conservation of a project area.[35]

Opinion No. 2004-095 was issued in response to an inquiry whether impact fees could be used in conjunction with TIF funds for repayment of redevelopment bonds.[36] Because Act 1197 provides that local governing bodies are able to receive contributions from other sources to defray project costs, Attorney General Beebe opined that generally impact fees could be used to repay redevelopment project debts.[37]

On January 11, 2005, Attorney General Beebe issued Opinion No. 2004-359, which, like Opinion No. 2001-295, discussed whether the twenty five (25) mills authorized by Amendment 74 could be diverted for use by a TIF district.[38] Contrary to Opinion No. 2001-295, Attorney General Beebe opined that, under the then current legislative framework, Amendment 74

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[34]Op. Ark. Att'y Gen. No. 2003-103 (Apr. 21, 2003).

[35]Id.

[36]Op. Ark. Att'y Gen. No. 2004-095 (May 27, 2004).

[37]Id.

[38]Op. Ark. Att'y Gen. No. 2004-359 (Jan 11, 2005).

property tax revenue could not be used for Amendment 78 purposes. Opinion No. 2004-359 stated that Amendment 74 taxes were a state, rather than a local, tax. Attorney General Beebe opined that Act 1197, with a "taxing unit" definition which only included cities, counties, school and community college districts, only allowed TIF districts to utilize local property tax revenue.[39] However, as Attorney General Pryor did in Opinion 2001-295, Attorney General Beebe did leave open the possibility that the General Assembly possesses the authority to expand the definition of "taxing unit" to include the state.[40]

**Act 2231 of 2005**

In response to Atty. Gen. Opinion 2004-359, the Arkansas General Assembly enacted Act 2231 of 2005. While this legislation contained many revisions to TIF law, the primary purpose of the legislation was to expressly provide that the state was included in the definition of "taxing unit."[41] Act 2231 also states that, for purposes of tax revenue distribution to taxing units, the total millage rate expressly excludes mills dedicated to libraries, county hospitals, and police/fireman pension funds, and increases in the total millage rate occurring after TIF district creation, if the additional mills are pledged for specific debt service.[42]

During the 2005 General Assembly, many groups expressed concerns that several proposed TIF districts were inconsistent with the intent of Amendment 78. To prevent abuses,

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[39]Neither Opinion No. 2001-295 nor Opinion No. 2004-359 mention Arkansas Constitutional Amendment 47, which simply states, "No ad valorem tax shall be levied upon property by the State."

[40]Id.

[41]2005 Ark. Acts 2231, §1 (2005).

[42]Id.

Act 2231 provides several safeguards to ensure consistency with the intent of Amendment 78. First, Act 2231 provided that prior to creation of a TIF district, the local governing body must determine that the property in the proposed TIF district is in a "blighted area." There are several factors included in Act 2231 which provide guidance as to what constitutes a blighted area.[43]

If a TIF district is being created on wholly undeveloped property, then the Act limits the use of TIF funds to "capital improvements of a public nature." This term includes, by definition, streets, water and sewer improvements, and similar public improvements.[44]

Act 2231 adds to the list of items required to be included in a project plan. For example, instead of a feasibility study, as was required in Act 1197, Act 2231 mandates an independent, detailed economic analysis on the proposed TIF district. This analysis must include a comparison of projected property taxes coming into the TIF district against the projected property, sales and income taxes received or recaptured by taxing units as a result of the TIF district. The Arkansas Department of Economic Development is required to review the analysis and provide comments to the local governing body in 30 days. Additionally, the project plan must provide an estimate of the number, types and timing of jobs to be created by the TIF project.[45]

Act 2231 also amends the termination date of TIF districts, to ensure that TIF districts do not extend their duration for more than twenty five (25) years.[46] Finally, Act 2231 provides if a

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[43]2005 Ark. Acts 2231, §2 (2005)

[44]Id.

[45]Id.

[46]Id.

TIF district issues redevelopment bonds, and the TIF district generates funds in excess of the funds necessary to meet scheduled bond repayments, then those excess funds can only be used for: (i) prepayment of redevelopment bond obligations; or (ii) distribution to a taxing unit, as determined by the local governing body.[47]

[47] 2005 Ark. Acts 2231, §6 (2005)