Coates' Canons Blog: What is a Synthetic Project Development Financing (aka Synthetic TIF)?

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Merriam-Webster's online dictionary defines "synthetic," among other things, as "devised, arranged, or fabricated for special situations to imitate or replace usual realities." As the definition suggests, a "synthetic project development financing" (more commonly referred to as a "synthetic tax increment financing" or "synthetic TIF") is a local government borrowing scheme that is "fabricated" to "imitate" a real TIF. If that does not totally clear things up for you read on….

What is a Project Development Financing/TIF?

A project development financing (hereinafter referred to as TIF) is a type of debt financing in which a local government establishes a district and borrows monies to fund public infrastructure projects that will benefit (and incentivize) new private development in the district. The unit pledges as security for the loan (and uses as funds to repay the loan) the incremental increase in property tax revenue generated within the district due to the increase in property valuation caused by the new development. For more information on TIFs in North Carolina click **here**.

How does a Synthetic TIF compare to a TIF?

A "synthetic TIF" is similar to a TIF in that it is type of debt financing in which a local government borrows money to fund public infrastructure projects that will benefit (and incentivize) new private development in a defined area. A synthetic TIF differs from a TIF, however, in the nature of security pledged for the loan. In a synthetic TIF the unit pledges as security for the loan the asset (or a portion of the asset) that is being financed or, in some cases, the unit's full faith and credit (general taxing power.) The unit expects to repay the loan from the incremental increase in property tax revenue generated within the district due to the increase in property valuation caused by the new development. But the unit does not pledge the incremental revenue as security for the loan.

Thus, as I stated above, a synthetic TIF is a borrowing scheme that is "fabricated" to "imitate" a TIF but that is not a TIF. Instead, a unit of government uses one of its other authorized debt financing mechanisms. (As a reminder, North Carolina local governments have five authorized borrowing methods—general obligation bonds, revenue bonds, installment financings, special obligation bonds, and project development financings/TIFs.) A unit may fabricate a synthetic TIF while issuing debt through general obligation bonds or installment financings. The latter is far more common, though.

What are the procedures for establishing a synthetic TIF?

There is no legal process for creating a synthetic TIF. A unit must follow all of the procedures for the particular borrowing mechanism that it chooses (installment financing or general obligation bonds). In the case of an installment financing, that means that the unit structures the borrowing transaction according to, and follows the procedures prescribed by, the provisions in **G.S. 160A-20**. The unit pledges the infrastructure being constructed/improved/purchased (or a portion thereof) as security for the loan. However, the unit anticipates using the incremental property tax revenue generated from the new development that was incentivized by the public infrastructure investment to repay the loan.

Why call an installment financing (or a general obligation financing) a synthetic TIF?

Legally there is no difference between a "regular" installment financing (or general obligation financing) and one that is referred to as a synthetic TIF. The use of the term synthetic TIF is simply a marketing strategy. It is a short-hand way to indicate that a unit intends to repay the loan using new revenue generated from increased property values due to new development in the area, rather than from existing revenue or from new revenue generated through increased property tax rates.

Links

- www.sogpubs.unc.edu/electronicversions/pdfs/lfb36.pdf
- www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_160A/GS_160A-20.html