Gentrification and Tax Increment Financing: The Road to Mixed-Income Communities?

by Ilana Gotz

This paper examines gentrification, its causes and consequences, and illustrates how Tax Increment Financing (TIF) can be used to promote neighborhood change. This process will be analyzed using the Logon and Molotch (1996) theory of the city as a growth machine. The use of TIF has the potential to create successful mixed-income communities; however, it also can be used to displace current residents and create benefits not for the residents, but rather for local elites who stand to benefit from growth.

INTRODUCTION

Gentrification is an issue facing many communities across the United States. Many people now recognize the signs: perhaps a new condominium development, lofts, or even a Starbucks Coffee. Much of the grassroots organizing happening in neighborhoods surrounds this issue, and often neighborhood organizations find themselves fighting to minimize the possible negative outcomes of gentrification once it is occurring. But why is it that urban development may result in gentrification? This paper will examine gentrification as a process of urban development by using the theory of the city as a growth machine, as proposed by Logon and Molotch (1996). I will apply this theory to development and neighborhood change in Chicago, and to the city's frequent use of Tax Increment Financing as a method of achieving growth.

Logan and Molotch (1996) consider the city as a "growth machine." In their view, place-based elites have the power to affect patterns of land use within the city. These place-based elites, including actors such as property owners, real estate developers, the construction industry, banks and insurance companies, promote growth in order to enhance their wealth. According to this theory, urban development is a process that is not controlled by the average people who live and work in communities, but rather by local elites who stand to benefit from neighborhood change through increased property values, rents or development contracts.

In Chicago, neighborhood gentrification has served to enhance the wealth, status and image of local elites. These elites benefit from gentrification and the increased growth and value it brings. This group of local elites, or the "growth coalition," can actually induce gentrification, particularly through partnerships with elected officials. Presently, one of the main tools available for city officials to promote growth is Tax Increment Financing, known as TIF. Through the use of TIF, a municipality can designate an area for reinvestment and subsidize developers and businesses that want to invest in the area. Often, as can be seen in Chicago, once an area is designated as a TIF district, it is highly prone to gentrification and displacement of residents. First I will examine gentrification, its causes and consequences, and then I will illustrate how TIFs are used to promote neighborhood change.

GENTRIFICATION

There are many different definitions of gentrification. Merriam-Webster Dictionary defines it as "the process of renewal and rebuilding accompanying the influx of middle-class or affluent people into deteriorating areas that often displaces earlier, usually poorer residents." Most definitions incorporate the issue of class, and some state that gentrification is a process of physical and social change in a neighborhood. Kennedy and Leonard (2001) define gentrification as "the process by which higher-income households displace lower-income residents of a neighborhood, changing the essential character and flavor of that neighborhood." I believe a combination of these two definitions is appropriate: gentrification is the process of renewal and rebuilding in which higher-income households move into a neighborhood previously comprised of lower-income households. The process often, but not necessarily, displaces earlier lower-income residents and changes the character and flavor of that neighborhood.

Kennedy and Leonard (2001) outline the three stages of gentrification as defined by Berry (1985):

> "In the first stage, newcomers buy and rehab vacant units, causing little displacement and resentment. In the second stage, knowledge of the neighborhood and the rent gap spreads, displacement begins to occur and conflict erupts. Finally, as the effects of rehabilitation are more apparent, prices escalate and

> displacement occurs in force, new residents have lower tolerance for social services facilities and other amenities that they view as undesirable, and original residents are displaced at a larger scale, along with their institutions and traditions."

This process can be seen in action in a number of Chicago community areas. For example in Uptown, as new condominiums are built and single-room occupancy and affordable housing is eliminated, the character of the neighborhood is changing. Many also fear that gentrification will occur in Pilsen, causing this primarily Mexican neighborhood to lose its ethnic character.

Some would say that gentrification is a natural process—neighborhoods go through cyclical change every two or three decades. Others would say that the process is not natural, but rather controlled by those who stand to benefit from growth in particular places, i.e. the local elites, such as those involved in real estate development, construction, and other industries tied to land use. Gentrification benefits these local elites, for it maximizes growth from the land. Logan and Molotch (1996), referring to these local elites, hold that "the activism of entrepreneurs is, and always has been, a critical force in shaping the urban system, including the rise and fall of given places." Historically, we see how the elites who built American cities "strained to use all the resources at their disposal, including crude political clout, to make great fortunes out of place" (Logan and Molotch, 1996).

While growth inducement strategies that lead to gentrification are mainly in the hands of local governments, Logan and Molotch (1996) argue that the growth coalition has the means to apply pressure on local officials to mobilize growth to their benefit. They say these local elites play a large role in electing local politicians and this, in turn, gives them systemic power. Local elites support candidates with campaign contributions resulting in "candidates of both parties of whatever ideological stripe, hav[ing] to garner the favor of such persons, and this puts them squarely into the hands of growth machine coalitions" (Logan and Molotch, 1996). The growth coalition holds that growth benefits everyone, for it "strengthens the local tax base, creates jobs, provides resources to solve existing social problems, meets the housing needs caused by natural population growth, and allows the market to serve public tastes in housing, neighborhoods, and commercial development" (Logan and Molotch, 1996). But it is precisely this growth that leads to gentrification and the displacement of low-income residents in favor of the middle and upper class.

The extensive, targeted investment that leads to and intensifies gentrification can be detrimental to the previous residents of the neighborhood. As an area begins to gentrify and property values increase, property owners are faced with increased property taxes. If a homeowner cannot afford to pay the increased property tax on his home, he is forced to sell and move to a less costly neighborhood. Or if a property owner with rental units finds that area rents have increased, she will renovate the units and begin to charge higher rents, forcing previous residents out if they cannot afford the new rents. Additionally, gentrification brings people who want to buy homes in the neighborhood, especially in the earlier stages of the process when prices are still low. This creates a large incentive for apartment owners to convert to condominiums and sell the units, thereby decreasing the availability of affordable rental units in the area.

Businesses that operate in a gentrifying area face similar challenges. Rental rates increase, often driving out small businesses that once characterized the neighborhood. New businesses that cater to the middle- and upper-class residents of the neighborhood enter the commercial district and compete with the existing businesses. As businesses that once characterized the area leave, so do the jobs they provided. The businesses that enter may not replace the lost jobs, or they may have jobs that require a different level of skills. Many times, as land becomes more and more valuable in the area, businesses supplying manufacturing and industrial jobs also will leave, taking away jobs from the low-income residents of the neighborhood.

Significant changes also may occur in the political landscape of the area. Kennedy and Leonard (2001) point to gentrification bringing change to a community's power structure and elected leadership as well as political, religious, and social-services institutions. New residents may bring contacts and political clout, leading to improved public services. To everyone's benefit, "newcomers advocate for improved schools, lower crime and improved public services" (Kennedy and Leonard, 2001), yet their interests may not always be in line with long-term residents, which can lead to conflicts over priorities and strategies.

As Kennedy and Leonard (2001) show, gentrification is intensified in cities with tight housing markets. As the demand for housing outpaces the supply, the cost increases and the low-income residents no longer can afford to pay the price to live in that neighborhood, and they are displaced. The same authors also point to rapid job growth in a particular area (i.e., jobs requiring a high skill set that attract middle- and upper-income employees), proximity to city amenities, frustration with increased traffic and long commutes, and targeted public sector policies as factors leading to gentrification of city neighborhoods. It is primarily such public-sector policies as tax incentives and subsidies through which gentrification directly benefits the growth coalition.

Gentrification clearly benefits those elites who make up the growth coalition and those who move into the neighborhood when the housing cost is still low. Yet, while it has the potential to create negative outcomes for residents who lived in the neighborhood prior to development, it also can benefit these long-term residents. New development can bring jobs to the community, particularly in housing construction and rehabilitation, and it also brings increased amenities and commercial developments. If businesses are able to stay in the neighborhood, they may benefit from increased consumers and spending. And as Kennedy and Leonard (2001) point out, some original homeowners "may welcome price appreciation and the increased financial equity it brings."

If low-income residents are not displaced by gentrification, mixed-income communities that benefit everyone can be achieved. Concentrated poverty is expensive for cities and for social service provision. Deconcentrated poverty, on the other hand, has a number of benefits, including reduction in crime rates and enhancement of social capital. The city of Chicago is currently attempting to achieve mixed-income communities through the transformation of public housing and the construction of housing developments that contain market rate, affordable and public housing units.

The key to achieving successful mixed-income communities and minimizing the harmful effects of gentrification is ensuring that lower-income residents are not displaced by the influx of investment, capital and new residents. However, it is not in the growth coalition's interest to do this, for it means fewer immediate profits. The elites instead push for increased gentrification and growth. One of the main tools the growth coalition can use to do this is Tax Increment Financing (TIF), an economic development tool that allows for targeted investment in a specific area. In Chicago, TIFs have been used in ways that spur gentrification, thereby benefiting the local growth coalition. However, this tool could instead be used in ways that minimize the costs of gentrification imposed on long-term neighborhood residents and promote the development of mixed-income communities.

TAX INCREMENT FINANCING

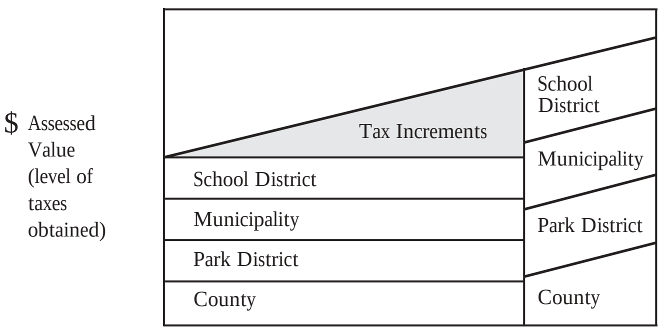
Tax Increment Financing (TIF) is a policy tool that can be used to stimulate gentrification and benefit the growth coalition. However, it does not have to be used solely to benefit the local elite and those who buy property in an area just beginning to gentrify. If community interests are integrated into the TIF plan, it can create long-term benefits for everyone. Unfortunately, in Chicago, TIFs have been used as means to gentrify neighborhoods and increase the wealth of local elites. To see how this occurs, we must first examine what a TIF is and how it functions.

What is a TIF?

TIF is an economic development tool that is made available by state statute and is implemented by city government. The Chicago Department of Planning and Development listed 124 different TIF districts as of October 2002 (DPD Web site, 2002). The TIF statute has been on the books since 1977, though the number of TIFs being created has increased substantially in the past few years. Between 1998 and 2000 alone, the city designated 56 TIF districts (Neighborhood Capital Budget Group (NCBG), 2001).

A TIF is created for a specific geographic area. It allows the city to capture any new property tax from within the TIF district and reinvest it directly into that area for 23 years. When a TIF district is established, the level of taxes divided between all taxing districts in the area (e.g. school districts, park districts, the city, the county) is essentially capped at its current level. For 23 years, any additional tax, or increment, received above that amount goes into the TIF account and is to be used within the TIF district. After 23 years, property taxes are again divided between all the taxing districts. Graph 1 shows how the tax increment is captured. When the TIF district is created, in year one, the level of property taxes collected by the school district, municipality, park district and county are frozen at current levels. For 23 years, as property taxes increase, these taxing bodies continue to receive the same amount of money while additional tax revenue, or increment, is placed in the TIF account (the shaded portion of the graph) to be used for projects within the TIF district. After 23 years, the TIF account is no longer used and all property taxes, which have risen since year one, are again divided among all taxing districts.

GRAPH 1: HOW A TIF CAPTURES REVENUES



Adapted from REDCOOP, "Development and Taxes: Nightmare or Sweet Dreams?"

Illinois' TIF law "requires that municipalities only create TIF districts in areas that show significant signs of 'blight' and in which no significant private investment is occurring, or is likely to occur, without a TIF subsidy" (Statewide Housing Action Coalition (SHAC), 2002). To qualify as "blighted," an area must show signs of five out of 13 blight categories outlined in the TIF legislation. Some of these include: deterioration, inadequate utilities, building code violations, overcrowding structures, and vacant buildings (NCBG, 2001). Once this is established and the TIF is created, the idea is to spur investment to increase the value of the area, thereby increasing property taxes, and then to continue using the tax increment to sponsor development in the area. Therefore, a TIF is only successful if it is able to attract investment and raise property values in the area.

What can TIF funds be used for, and how is development created?

According to the Neighborhood Capital Budget Group (NCBG) (2001), TIF funds can be used for the following purposes: infrastructure and other public improvements (including schools, parks and other public buildings); planning expenses, such as studies and surveys, legal and consulting fees, accounting, and engineering; acquiring land and preparing it for redevelopment; job-training and day-care expenses for companies located within or planning to locate within the TIF district; renovation and rehabilitation of existing buildings; and financing and interest subsidies for the loans a developer takes out to pay for a project.

The municipality must create a redevelopment plan outlining the goals for redevelopment and the intended uses of the TIF funds in that district. As explained by the Statewide Housing Action Coalition (SHAC) (2002), "Once a TIF is established, the municipality will either borrow money through a bond issue or use general revenue funds to make initial improvements within the TIF area." These improvements should increase property values and generate an increment. This increment can then be used to pay off the initial development expenditures and to fund new projects in the district. NCBG (2002) outlines the three ways to increase property value: "(1) new buildings can be built on vacant land, (2) improvements can be made to existing buildings, or (3) existing buildings without improvements can be assessed at a higher level." The third way is possible when gentrification is occurring and the neighborhood has become more desirable. To allow municipalities to proceed with redevelopment plans, which sometimes require acquiring property in the area, the TIF statute allows the use of eminent domain.

TIF Districting Impact and Outcomes

TIF is an economic development tool that can be used to gentrify an area, thereby displacing low-income residents. Growth coalition members can initiate the consideration of an area as a TIF district to receive subsidies for development. SHAC (2002) explains that TIF districts can be as small as a couple of blocks or as large as an entire municipality, and that “smaller TIF districts are usually created at the initiative of a private developer, or a business that promises to locate in an area (or not to leave an area) if it receives a TIF subsidy.” Such TIFs greatly benefit the local elite and pose threats to low-income residents. But TIFs need not be used solely in this manner. With community participation, TIFs can be used to benefit the entire community. We will now consider some of the outcomes of TIF districting.

TIFs are only successful if property taxes increase, which can lead to displacement of low-income households. SHAC (2002) points out that rarely does low-income housing increase property values; therefore, “those concerned primarily about maximizing the tax revenues generated in a TIF are likely to oppose most low-income housing development.” TIFs have a tendency to promote gentrification by sponsoring development that is attractive to middle- and upper-income residents, resulting in property taxes and rents that force displacement of low-income residents. Further, the possibility of using eminent domain within the TIF district puts residents and businesses at risk of displacement.

However, TIFs are not entirely negative for long-term residents. The community can benefit greatly from TIF funds in a number of ways. First, property taxes generated from a specific community remain in that community and are used to improve that geographical area. If the TIF functions properly, it can increase the quality of life for residents and contribute to the creation of a mixed-income community. NCBG (1999) points to the use of TIF dollars for public works and basic infrastructure, job creation, employment training, career education and rehabilitation of existing homes and businesses as ways in which the community potentially can benefit. However, whether TIF funds are used for these purposes and whether local residents benefit from them depends on the types of projects ultimately supported.

The establishment of TIF districts impacts other taxing districts in the area, since the level of property taxes they receive is frozen for 23 years. In 1995, Chicago property tax dollars were divided in the following manner: 43 percent went to the schools, 21 percent to the city, 10 percent to Cook County, 7 percent to the park district, and the remainder to several other smaller taxing districts (SHAC, 2002). Advocates of TIF districts argue that these districts would not be getting additional revenue had the TIF not been created, since development is only taking place in the area because of the TIF. However, this is only true if the TIF is created in an area that truly would not otherwise have received private investment. Unfortunately, as NCBG (2001) asserts, "the State law does not provide us with a good set of rules for determining whether or not development would take place without the TIF. This has opened the door to widespread abuse of TIFs in some areas."

NCBG conducted a study of 36 TIF districts in Chicago to find out whether these TIFs were created in areas that would have achieved growth without the TIF, and whether the benefits of TIF justify the costs incurred. As the name of the study declares, NCBG (2002) set out to discover "Who Pays for the Only Game in Town?" What they found was that in the lifetime of these 36 TIFs, "The local taxing bodies that draw on Chicago's property tax base will lose $1.3 billion in tax revenues they would have probably collected if these areas had not been declared TIF districts." The danger is that, as costs rise for other taxing bodies and the level at which they collect taxes is frozen, they will not collect enough revenue. Taxing bodies will be forced to increase their tax rates; in fact, "the Chicago Public Schools has raised its tax levy each year for the past five years" (NCBG, 2002). The TIF district itself creates part of the increased cost for Chicago Public Schools, for additional residential development in the area brings in additional demand for school services.

The fact that the Illinois TIF law does not specifically define how to determine whether development would take place in an area without the TIF is only one way in which the law is vague. Even the requirements for determining "blight" before the creation of a TIF district are not clearly defined and leave room for interpretation. One of Chicago's most controversial TIF districts is the Central Loop TIF, encompassing much of the downtown Loop area, created in 1997 as an expansion of the 1984 North Loop TIF. As SHAC (2002) points out, at the time of its proposal, "many people questioned whether it was credible to claim that no private investment in the area could 'reasonably be anticipated' without the creation of the TIF district." SHAC also notes that there had been recent investment in retail in the area (e.g. the State Street shopping district), a low office vacancy rate, and rehabilitation and conversion of older buildings. This is all hardly what one typically thinks of when hearing that an area is "blighted." But since the TIF law allows for subjectivity in determining "blight" and whether investment is likely to occur, the city was able to TIF most of its downtown area. Additionally, the statute allows TIF funds to be transferred between bordering TIFs but does not specify for what purposes. This allows for money generated in one district to be taken away from that community and given to another.

TIF legislation also leaves room for variation in the amount of community participation allowed throughout the TIF process. Prior to 1999, when SHAC successfully lobbied for changes to the TIF law in the area of community participation, municipalities were able to enact TIF districts without much attention. Now, particularly in districts that include 75 or more units of occupied housing, "The municipality must convene an early public meeting, mail notice of that meeting and main public hearing to every residential address in the district, and it must create an interested parties registry for all individuals and organizations in the municipality who want notice of activities in the TIF" (SHAC, 2002).

However, TIF legislation still does not stand strong on the issue of community participation. It allows for the creation of Community Advisory Panels to oversee the use of funds in a TIF district, but the law does not required such panels. Therefore, TIFs in Chicago are often implemented with no community input, other than the public notice and hearing. In fact, in all of the 124 TIF districts in Chicago, not one has an officially recognized community oversight or advisory committee.

In Chicago, there are communities seeking to have more input into TIF fund usage to ensure that the needs of existing residents are met. The residents impacted by the Wilson Yards TIF organized and even gained the support of their alderman. Although the Organization of the North East (ONE) has hailed the Wilson Yards redevelopment plan as "the most democratized TIF process yet in Chicago" with goals and objectives that are "really representative of how the community wants these dollars spent," the city refuses to grant formal recognition to a community oversight panel (Community Media Workshop, 2001).

These residents and others in Chicago communities affected by TIF districting are coming together to try to ensure that TIFs are used in ways that lessen the displacement that TIF-induced gentrification can cause. Some uses that would reduce negative TIF impact include: using funds for affordable housing, ensuring that TIF funds go to diversified commercial projects, and only subsidizing businesses that will provide jobs for local residents at a living wage. NCBG (1999) emphasized the job component, saying, "New and better jobs are a key element in ensuring that TIFs do not displace existing residents." If there is access to good jobs, then the increase in the cost of living caused by TIF may be more bearable.

TIFs can be a tool for the promotion of equitable development if the city also designs policies to lessen the impact of increased property values on residents at risk of displacement. Such policies could include tax breaks for long-term and low-income residents, incentives not to convert apartments into condominiums, and rent control. But this is difficult to achieve without consistent community participation, for these types of policies would be strongly opposed by the local elites who comprise the growth coalition.

CONCLUSION

In Chicago, TIFs are a tool implemented with little community input. Logon and Molotch's (1996) theory of the city as a growth machine helps us understand how urban development and growth is used to benefit local, place-based elites. In the case of gentrification and TIFs, this translates into not only benefit for the local elites, but potentially negative neighborhood changes for current residents. Though the use of TIFs and the inducement of gentrification can be detrimental to low-income communities by displacing residents and changing the character of neighborhoods, with safeguards in place and community participation, they actually can be beneficial. As noted, de-concentration of poverty, neighborhood improvements, decreased crime, increased social capital and job opportunities are all potential benefits of TIF districting and the creation of mixed-income communities. Displacement of low-income residents from one disinvested neighborhood into another perpetuates the concentration of poverty in cities and results in higher costs for municipalities and social-service agencies.

The key is to ensure that low-income residents are not displaced by the policies intended to improve their communities, for if they are, the communities are no longer theirs to enjoy. The only way to achieve successful mixed-income communities is to implement policies that take into account the interests of community residents and not just those of the local elites who control the growth coalition. This can be accomplished only through consistent community participation and input to challenge the domination of growth coalition interests.

Policies and strategies of urban development continuously must seek community input. This can be gathered through oversight committees, surveys or frequent town hall-style meetings with city officials and aldermen. Eliciting community participation potentially will lead to greater community support and, hence, more effective implementation of development initiatives. If cities pursued this kind of development, the immediate financial benefits of the local elites would not be as great, yet in the long-run they would create healthier and more sustainable communities. ■

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