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Municipalities mixed on use of sales tax rebates to spur development

Vernon Hills is a case study in the pros and cons of these incentives

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Mary Fontanini, left, and her husband Cesare try out a sofa at Steinhafels Furniture Superstore in Vernon Hills on Friday, Sept. 23, 2011. (Keri Wiginton/Tribune) (Keri Wiginton, ChicagoTribune / September 23, 2011)

By **Kathy Bergen**, Tribune reporter

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As many communities continue to agonize over gaping retail vacancies, north suburban Vernon Hills has reeled in an impressive roster of replacements in the past couple of years.

The village landed Steinhafels Furniture; H.H. Gregg, a purveyor of appliances and electronics; Mariano's Fresh Market; Gordmans, a clothing and fragrance store; **Dick's Sporting Goods**; and TigerDirect, a computer outlet.

But to land these deals and bring its retail vacancy rate back in line, village officials swallowed a bitter pill. They agreed to provide sales tax rebates to the incoming ventures, a step largely avoided in more prosperous times.

"Personally, I want to lose that term from our vocabulary in the future," said Mayor Roger Byrne, whose village gets half its revenue from sales taxes and

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prides itself on not needing to levy property taxes.

Communities throughout the region and the state share sales tax revenues to woo retailers — and they are within their rights to do so under Illinois law. In fact, rebate researcher Geoffrey Propheter found the rebate programs to be more heavily used in Illinois than elsewhere around the country.

For the most part, these programs have flown under the radar until this summer, when the Regional Transportation Authority, the city of Chicago and **Cook County** legally challenged a variation on their use. In lawsuits, they alleged Channahon and Kankakee used sales tax rebate agreements to divert sales tax collections unfairly from metro Chicago to small "sham offices" in their lower-tax towns — allegations denied by both communities.

With a spotlight now directed at sales-tax rebate programs, some observers are quick to say they stand behind the more common use of rebate programs to attract big-box stores and auto dealers.

"We have no concerns about sales tax rebate programs being used if there is real economic development potential, such as jobs being created or construction taking place to build a new business," said Jordan Matyas, deputy executive director at the RTA.

But other observers say the programs can skew economic development efforts toward retail. This can be effective in filling city coffers but may not produce as much regional economic growth as office or manufacturing developments, which tend to have higher-paying jobs and an ability to sell products over a much wider geographic range.

The rebate programs also tend to foster bidding wars between towns, with taxpayers picking up the tab. Propheter, a research assistant at the **George Washington** Institute of Public Policy, found the rebate offers have been used in border skirmishes around the state, from Belleville, outside St. Louis, to southwest suburban Joliet.

"If it's just a move from one municipality to another, then what are we gaining as a region?" asked **Matt Maloney**, deputy chief of staff at the Chicago Metropolitan Agency for Planning. "And are we just spending public resources in the process?"

But, he said, the programs can be effective. For instance, a retailer or developer may use the rebate to pay for roadwork or other infrastructure. "The devil's in the details," he said.

The Illinois sales tax rate is 6.25 percent, and the state returns 1 percent to the cities where the sales occur. This gives towns a powerful incentive to fight for a retailer, even if they have to rebate a portion of the resulting tax growth to attract the store.

"A Costco store averages \$120 million in sales, so 1 percent is a lot of money," said retail consultant John Melaniphy. "So you're prepared to give part of that away to get them."

Or, as Maloney put it, "I'd characterize it as 'winner takes all.'" Some other states, in contrast, distribute sales tax based on population concentrations or to entire counties, he said.

Not all communities go the rebate route. Chicago, for instance, does not use the tool.

"The city already has a wide array of development tools and business incentives that effectively address the major variables developers and stewards consider before investing in a community and it's not something that we're being asked to provide," said a spokesman for the Department of Housing and Economic Development.

And northwest suburban Schaumburg, home to the massive **Woodfield Mall** and **Ikea**, will not entertain such discussions.

"I think we're providing a good location, a stable political climate and a community that cares about its infrastructure and look," said Ken Fritz, village manager. "We can give businesses the kind of thing they are looking for."

And for many years, **Vernon Hills** mostly steered clear of rebate agreements as it developed into the retail nexus for south/central Lake County, anchored by the Westfield Hawthorn mall. With a median household income of about \$90,000 and many affluent neighboring communities, its appeal is obvious.

"We were very attracted to the marketplace in Vernon Hills and the retailers that are now our neighbors," said Gary Steinhafel, president of his family's Wisconsin-based furniture superstore chain, which in August opened its first Illinois store there in a vacant building that formerly housed a Home Expo.

"Really, the (rebate) incentive was a catalyst to move forward now rather than postpone the decision until the housing market improved or the economy picked up," he said. "In the current state of the commercial real estate market, it was highly probable this building could have been vacant another two to three years. We purchased it and opened within nine months."

Some shoppers at the colorful, eclectic furniture emporium, along with others at the recently opened H.H. Gregg, were surprised to learn of the rebate programs. But once informed, they tended to be supportive.

"It just builds the economy, and jobs in this area," said Deerfield resident Anita Breuer, who makes her living sprucing up decor in high-end homes. She was browsing with colleague Jill Golden, also of Deerfield.

"The more and more storefronts that we see empty, that's not going to help turn around the mood in the country," Golden said. "You the need the vitality."

But others had qualms about directing tax dollars to private purposes.

"You'd like to see the sales taxes collected by the villages used for reducing the tax load on the taxpayers, or to see added benefits to the community, such as running trails, bike trails, that kind of thing," said Erik Nyman, an inventory control specialist who lives in Libertyville and was checking out the new H.H. Gregg.

The new arrivals in Vernon Hills, particularly the Mariano's Fresh Market, seem to be causing some nervousness in neighboring Libertyville.

Libertyville Mayor Terry Weppler recently spent time bagging groceries and thanking shoppers at his town's Jewel, and he sent a letter to residents, urging them to shop in town.

The moves were not specifically tied to the arrival of Mariano's, he said, but "the fact is our sales tax revenues have continued to shrink, as they have in most municipalities, and so we wanted to make sure people were aware of the impact of shopping in their own community."

Vernon Hills officials had a sobering experience last year when a joint venture between Oxford Development Partners and Shorewood Development Group purchased a former Circuit City site for \$3.45 million, secured a sales tax rebate deal from the village and a lease with TigerDirect, then resold the property several months later for \$6.1 million.

"There's no question we were taken aback," said Byrne. "But we're part of a free enterprise nation, and we're still getting our money out of it."

Electronics stores are big revenue generators "and the city of Vernon Hills probably will get double what they would have gotten from other retailers in that location," said Bob Brownson, a principal at Oxford.

And, he said, it would be wrong to conclude the developers made \$2.65 million on the land transactions, because that figure doesn't reflect their investment in the project, he said. He declined to say how much was invested.

Still, the village is researching possible changes in its future contracts to better address what would happen when property changes hands, Byrne said. As well, the village doesn't intend to engage in many more rebate agreements, he said.

But the chapter is not yet closed. The village is in preliminary talks with Westfield Hawthorn mall in relation to a potential expansion, village officials said.

"We recognize the mall is the largest single retailer in our community," said John Kalmar, assistant village manager. "Outside of that, we will be very, very selective."