



## Executive Summary

# Transit Value Capture Analysis for the Chicago Region



Chicago Metropolitan  
Agency for Planning



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S. B. Friedman & Company (SBFCo) was engaged by the Chicago Metropolitan Agency for Planning (CMAP) to research and analyze the potential for value capture financing for transit improvements in the CMAP region. The recently adopted comprehensive regional plan for the Chicago region, Go To 2040 (“The Plan”) delineates eight “fiscally constrained” transit projects that have been evaluated to meet significant regional needs and for which sufficient funds are anticipated to be available. However, the Plan also lists 26 additional transit improvement and expansion projects that are either still in the early evaluation stages or need feasible funding sources to be moved onto the priority (fiscally constrained) list. As a result of the mismatch between available funding and the need for transit improvements, CMAP identifies a significant need to evaluate innovative funding options. The Plan specifically identifies value capture as one of the innovative funding mechanisms that should be further explored. This analysis was commissioned to evaluate the specific potential of value capture to generate funds for transit improvements and new projects.

## Project Background

Value capture refers to the practice of implementing a tax or fee on private property near a public improvement to take back or “capture” some of the monetary benefit that the property owners gain as a result of the public investment. The revenue from these fees or taxes is then used to pay for part, or all, of the cost of the improvement. Value capture has been utilized in various forms in both the United States and internationally to pay for new infrastructure. In recent years, there have been multiple studies that indicate that transit improvements increase the value of nearby properties, with recent studies indicating a 10% to 20% increase in home prices and office rents, and a 5% to 20% increase in apartment rents. Value capture is one mechanism for the municipality/transit agency to utilize a portion of that value increase to pay for the capital investment. This analysis sought to:

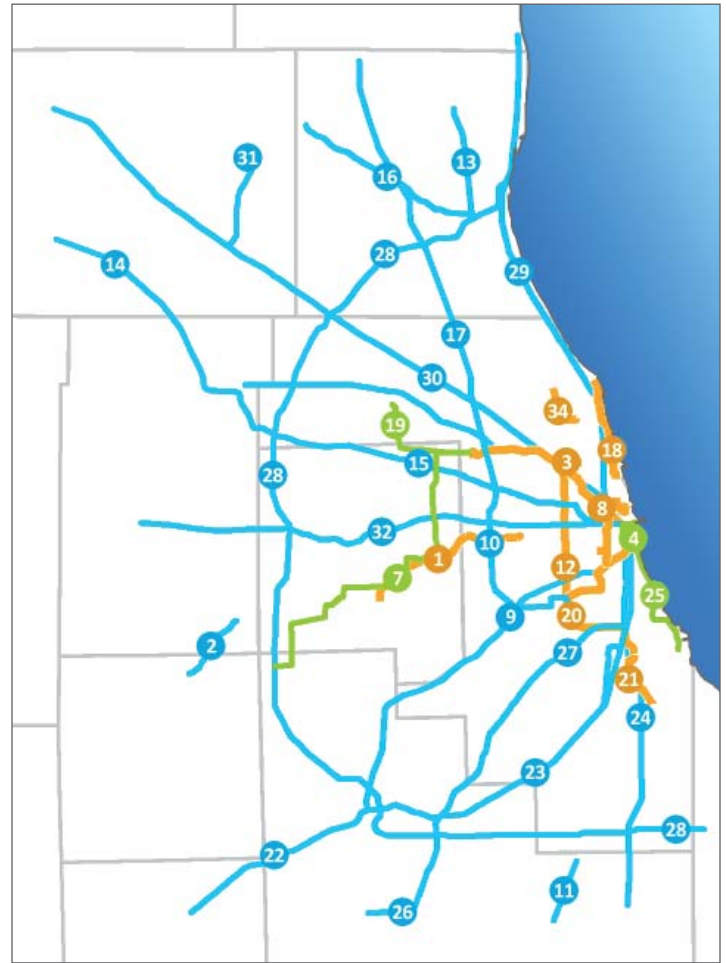
- Review alternative value capture mechanisms and identify those most appropriate for Illinois and the CMAP region.
- Evaluate the financing potential of each mechanism for a planned station in the region.
- Evaluate the potential effect of each of these mechanisms on the private development economics of a hypothetical transit-supportive project in the vicinity of the station.
- Provide overall conclusions and insights from the analysis regarding implementation of transit value capture mechanisms.

As noted, the Go To 2040 plan delineates 26 new transit or transit improvement projects in the unconstrained category, the designation for projects that are either still in the planning stages or lack funding. In addition to this current lack of funding sources, the federal government requires a minimum of a 40% match from local funds for the New Starts Program, the primary federal funding source for locally-driven transit projects. In order to remain competi-



GO TO 2040 Fiscally Constrained Transit Projects

- 1 Red Line Extension (South)
- 2 UP North Improvements
- 3 UP Northwest Improvements
- 4 Rock Island Improvements
- 5 West Loop Transportation Center
- 6 Southwest Service Improvements
- 7 North Red / Purple Line Improvements
- 8 UP West Improvements



GO TO 2040 Proposed Major Transit Projects

- 1 Blue Line Extension
- 2 BNSF Extension
- 3 Brown Line Extension
- 4 Central Area Transitway
- 5 Circle Line North
- 6 Circle Line South
- 7 DuPage J Line
- 8 Express Airport Train Service
- 9 Heritage Corridor Improvements
- 10 Inner Circumferential Rail Service
- 11 Metra Electric Extension
- 12 Mid-City Transitway
- 13 Milwaukee District North Extension
- 14 Milwaukee District West Extension
- 15 Milwaukee District West Improvements
- 16 Milwaukee District North Improvements
- 17 North Central Line Service
- Improvements
- 18 North Red/Purple Line Improvements
- 19 O'Hare to Schaumburg Transit Service
- 20 Orange Line Extension
- 21 Red Line Extension (South)
- 22 Rock Island District Extension
- 23 Rock Island Improvements
- 24 SE Service
- 25 South Lakefront Rail Corridor
- 26 Southwest Service Extension
- 27 Southwest Service Improvements
- 28 STAR Line
- 29 UP North Improvements
- 30 UP Northwest Improvements
- 31 UP Northwest Extension
- 32 UP West Improvements
- 33 West Loop Transportation Center
- 34 Yellow Line Enhancements and Extension



tive in the application process, a local match should be able to cover between 40% to 60% of anticipated project costs. While municipalities and transit agencies can also seek state funding to assist in meeting the local match requirements, transit funding in Illinois has been severely affected by the State's larger budget concerns. Illinois does have a Transit Bond Program, but there is currently a significant backlog of approved projects for which the state has not yet issued bonds. This analysis focuses on the ability of each potential value capture mechanism to generate a competitive local match for transit projects.

## Value Capture Mechanisms

As noted, value capture utilizes a tax, fee or other mechanism to recapture a portion of the increase in private property value due to public infrastructure investments. There are a number of types of value capture, but the most commonly utilized value capture mechanisms include:

**Land Value Tax:** This is an additional tax solely on the land value of a property, without regard to improvements on the property.

**Special Assessment:** This is an additional tax or assessment on the full value of a property, usually paid by property owners within a defined district that benefit from the improvement. Although most value capture literature refers to the special assessment as a single mechanism (Value Capture SA), Illinois has two types of very distinct special assessment districts: Special Assessment district (Illinois SA) and Special Service Area (SSA). An Illinois SA requires a detailed establishment process and demonstration of a specific benefit to the property owner, while an SSA is easier to establish but requires the support of property owners.

**Tax Increment Financing:** Tax Increment Financing (TIF) assumes that redevelopment will not occur in an area without public investment/intervention. Funds accrue to the district via tax increment—the equalized assessed value (EAV) of the district at its establishment is set as the base EAV of the district, and all taxes on property EAV above that base EAV are diverted to the district to fund improvements. A TIF-like value capture mechanism would capture some portion of the growth in property value due to the installation of the transit improvements, but Illinois law would need to be modified to allow creation of a TIF district based on adjacency to existing or planned transit centers as opposed to other factors. Furthermore, given the current political climate and concerns of underlying taxing districts, it is likely that a new type of TIF district will redistribute some portion of increment to underlying districts or work within some other, as yet undeveloped, limitations on increment.

**Development Impact Fees:** This is a one-time fee charged to a development based on a justifiable relationship between the impact of the proposed development and the transit improvements being constructed. In the context of value capture, the fee charged would likely be required to relate to potential transit trips generated or some similar measure.

**Joint Development:** In this scenario, a municipality or transit agency utilizes land it owns, often in the form of surface parking lots or excess rail right of way, for a transit-sup-

portive redevelopment project in which it shares profit from the development through a variety of forms of financial participation in the real estate project.

**Transportation Utility Fee (TUF):** A transportation utility fee treats roads and transit networks in the same manner as other public utilities, such as a sewer system. Using this logic, transit utility, or usage, fees are then applied to all properties district-wide based on a feasible measure, such as street frontage, number of housing units, or trip generation models.

According to a July 2010 Government Accounting Office (GAO) study, joint development is the most commonly utilized value capture mechanism in the United States. However, that same study also provides an analysis of existing projects, indicating that Value Capture SA and TIF appear to have the highest potential to provide funding for project-specific costs. Both of these mechanisms are already available in some form in Illinois, via Special Assessment Districts (Illinois SA), Special Service Areas (SSA) and Tax Increment Finance (TIF) Districts.

All of the potential tools are likely to require new legislation or legislative amendments at the state level to facilitate effective use of the mechanisms and generate the local match component for transit funding. However, some of the value capture mechanisms pose particular difficulty in light of Illinois statutes, are not well-matched to the typical types of transit improvement situations in the CMAP region, or appear to be more suited to funding roads rather than transit. Specifically, the following were removed from the set of mechanisms modeled in this analysis:

**Land Value Tax:** Illinois law does not currently allow for differential property tax rates for land and improvements. Furthermore, because of the lack of vacant, unimproved land in Cook County to provide value comparisons, land assessments vary considerably from property to property. Lack of consistency in land assessment makes creation of a land-value only tax mechanism particularly difficult, even if all statutory blocks to this method were removed.

**Joint Development:** Successful use of joint development is limited to jurisdictions that have ample available land for development in locations where they wish to place new transit facilities. Many suburban communities in the region do have significant land holdings near *existing* stations in the form of surface parking lots, but unless land acquisition for *new* transit lines and/or stations creates significant remainder parcels, the costs of additional land acquisition limit the potential of this tool for jurisdictions without prior land holdings.

**Transportation Utility Fee (TUF):** TUFs are most often used for road improvements, and a direct and equitable connection to the service provided is often proven via trip generation models. TUFs without a sufficiently strong connection between the transportation improvement benefit and the imposed fee have been successfully challenged in court. Given the lack of clarity on their use in Illinois, this option has been excluded.



Based on the above considerations, it appears that a TIF-like mechanism, special assessment (via the Illinois SSA mechanism) and impact fees would potentially be the most viable value capture mechanisms in Illinois and the CMAP region. Each mechanism also has the potential to generate the larger amounts required for a 40% to 60% local match and is already enabled under Illinois statute, although some legislative changes are required to fully realize the potential of each mechanism. Therefore, this analysis focuses on the transit funding potential of the following value capture mechanisms:

- TIF-Like Mechanism
- Special Service Area (SSA) Mechanism
- Development Impact Fees



## Value Capture Analysis

SBFCo analyzed the three value capture mechanisms indicated above in the context of a prototypical new transit project. After reviewing the general market conditions of each project area, the potential for redevelopment, availability of project cost and funding data, applicability to transit improvement scenarios in the broader region, and other area factors, SBFCo chose the planned Oakton Station in Skokie on the Chicago Transit Authority's (CTA) Yellow Line as a prototypical project. For the purposes of this analysis, the total station construction and related improvements cost was estimated to be \$23.8 million, with a local match of 55% (\$13 million).

Once a station was chosen, SBFCo tested three potential value capture mechanisms— a TIF-like mechanism, an SSA, and development impact fees— for their ability to pay for the required local match for the project, its overall value generation potential and financeability. Where applicable, each mechanism was tested for value generation potential based on both a quarter-mile and half-mile district. SBFCo also structured the analysis of each mechanism to account for potential interaction with underlying TIF districts, the need to pay any prior obligations of those TIFs, and the bond required to fund the local match amount. The framework for each value capture mechanism analyzed is summarized below:

### **TIF-Like Mechanism**

- SBFCo assumed that a potential Value Capture District (VCD) received tax increment similar to a conventional TIF district, although actual establishment of this type of district would require new legislation or modification of the existing TIF statute. This would allow for a transit-supportive TIF without a requirement for a finding of blight, but with a requirement to provide a minimum level of transit improvements.
- The analysis framework isolates preexisting TIFs from the VCD and repays existing debt service or redevelopment agreement pledges before returning any remaining increment to the overlapping VCD.
- Tax increment was calculated in the same manner as current Illinois TIFs, with establishment of a base equalized assessed value and calculation of revenues based on new property value above that base.

### **SSA**

- SSA tax rates were calculated in the same manner as current SSA tax rates are calculated. The tax rate adjusts based on current district equalized assessed value and the required bond payment, recalculating each year to meet debt service obligations.
- Property-by-property SSA tax amounts were not calculated as part of this analysis. An SSA tax rate is usually equal across all properties and is based solely on property EAV. However, the SSA statute allows for allocation based on reasonable factors such as land area, frontage or other calculations that may be more appropriate for a station area.
- Interaction with underlying TIF districts was accounted for, with an SSA taxing only the base EAV of these areas.

### **Impact Fee**

- Current state statute for transportation impact fees appears to focus on road improvements. However, SBFCo assumed that an impact fee for transit would have the same base requirement as road impact fees in Illinois, i.e., the fee applied must be “specifically and uniquely attributable” to the service demands created by the new development paying the fee.
- SBFCo developed a rough estimate of impact fee per residential unit and 1,000 square feet (SF) of commercial office based on ridership, population and employment projections for the Oakton Station area, provided in the Skokie Swift Station Location Feasibility Study (“Feasibility Study”) completed by Parsons Brinckerhoff in 2003, and typical population and employment generation rates per use type. The estimates of impact fee and the methodology of estimating the fee are shown in the full report.

Based on this analysis framework, the value generation of each mechanism within the quarter- and half- mile areas from the planned Oakton Station in Skokie were quantified. Figure 1 on the following page summarizes the results of this portion of the analysis.





It should be noted that the estimates of value generation are purely for illustration purposes to demonstrate the relative value generating effectiveness of each mechanism, based on the analysis framework conceived by SBFCo for this study. Actual value generation estimates for the mechanism will materially differ depending on the actual format of the mechanism put in place, the taxable EAV and the market conditions around the station area being considered.

**Figure 1: Bonding Capacity of Tested Value Capture Mechanisms in Millions (2010 Dollars)**

	TIF-Like District		SSA-Like District		1/2 Mile
	1/4 Mile	1/2 Mile	1/4 Mile	1/2 Mile	Impact Fee District [4]
Maximum Bondable Amount [1] [2]	\$45.8	\$172.6	\$11.5	\$34.0	Not Bondable – Value generation depends on extent of new development and fees, approx \$0.9 MM per average multifamily building
Local Match for Transit Improvements	\$13.0		\$13.0		\$13.0
Existing Obligations	- Downtown TIF: All funds - Science & Tech TIF: \$10 MM in bonds		None, but SSA tax rate must account for funds diverted to underlying TIF districts		N/A
Excess Fund [3]	\$36.0	\$162.9	None	\$23.7	None
Notes			Average tax rate to fund bond: 1.1%	Average tax rate to fund bond: 0.28%	5,600 new apartment units or 3.7M sf of new office space needed to pay for transit improvements

[1] TIF-like district maximum bondable amount after payment of obligations in underlying TIF Districts. Note that a TIF-like district will likely need to share some portion of its increment with underlying taxing districts, reducing the bondable amount.

[2] Assumes a maximum SSA tax rate of 1% for a quarter-mile district and 0.75% for a half-mile district.

[3] PV of remaining funds in Value Capture District after paying for existing obligations and local match for transit bonds.

[4] Impact fee estimated based on projected ridership generation by use. See full report for details on fee estimate.

Source: Village of Skokie and S. B. Friedman & Company

**TIF-Like Mechanism:** Within a quarter mile, this mechanism generates over one and a third times the bonding capacity as a half-mile SSA, and the half-mile TIF-like mechanism generates over five times the bonding capacity of the half-mile SSA. However, the scale of the district and funds generated is such that some portion of these funds would likely need to be distributed back to underlying tax districts, once debt service obligations associated with the transit improvements are met. While some of the excess funds may be utilized for additional public improvements or transit-supportive redevelopment, some redistribution back to the other taxing districts should be assumed.

**SSA:** In this analysis, while the average required tax rate in the half-mile SSA area is only 0.28%, the average rate sufficient to pay debt service in the a quarter-mile SSA is 1.1%, higher than SBFCo typically sees in a service-only SSA district. Infrastructure SSA rates can range much higher– 3% to 4%, or more– but those rates are related to roads, utilities and other items that property owners are more accustomed to being required to contribute to. Taxpayers do have the ability to stop the creation of an SSA, so any new district will need to be undertaken carefully.

**Impact Fee:** An impact fee offers significant potential revenue per project, but new development of the scale required would usually not be predictable enough to issue bonds as a front funding mechanism for the transit improvement. The impact fees would have to be placed in a capital reserve fund to be used as front funding for a later project, or used to repay spent funds once sufficient dollars were available for a new station.

## Effect of Value Capture Mechanisms on Development Economics

SBFCo also reviewed the financial effect of the value capture mechanisms (TIF, SSA and impact fees) analyzed in this study on the development economics of a hypothetical project near the proposed Skokie Swift Station. Because a TIF-like mechanism would have no additional tax or fee that would impact the development economics of a project, it has been folded into the scenario that assumes a new transit improvement with no new tax or fee imposition, and not reviewed separately in this analysis. For this analysis, SBFCo assumed the construction of a typical residential apartment project with 250 units and ground floor retail.

SBFCo used a “residual land value” analysis to test the financial impact of the proposed transit station, the SSA tax and an impact fee on the hypothetical project. Residual land value is the amount of money that a developer can afford to pay to acquire land after deducting all other development costs (i.e., hard and soft costs including developer’s fee) from the market price (or capitalized net income, if it is leasable property) that the developer expects to receive for the project. In a redevelopment context, the increased rents and/or prices that a project will achieve due to transit accessibility (a conservative 5% rent increase is assumed for the analysis) will enhance the market price or value of the project, which in turn will allow the developer to

**Figure 2: Summary of Effect of Transit & Value Capture Mechanisms on Development Economics**  
(all numbers are in millions of 2010 dollars)

	Baseline with No Transit	Transit and No New Tax or Fee	Transit & SSA Tax		Transit & Impact Fee (\$3,760 per unit)
			0.28% tax on 1/2 mile district	1.1% tax on 1/4 mile district	
Assumed Apartment Rent Increase Due to Transit [1]		5%	5%	5%	5%
Total Annual NOI	\$2.9	\$3.1	\$3.1	\$3.0	\$3.1
Total Project Value (6% Cap Rate)	\$48.6	\$52.1	\$51.6	\$50.4	\$52.1
% Project Value Increase		7.2%	6.3%	3.8%	7.2%
Net Supportable Project Cost	\$42.3	\$45.4	\$45.0	\$43.0	\$44.4
Supportable Land Acquisition Price (baseline price @\$15,000 a unit)	\$3.8	\$6.8	\$6.4	\$5.4	\$5.9
% Increase in Land Acquisition Potential (Residual Value)		<b>81.3%</b>	<b>71.2%</b>	<b>42.7%</b>	<b>56.3%</b>

[1] Based on literature review of rent increases associated with transit improvements.



pay a higher price for the acquisition of land. Similarly, a value capture SSA tax or impact fee will increase operating costs or initial development costs, respectively, and in turn will decrease the potential residual land value. The summary results of the effect of transit and value capture mechanisms on the development economics of a hypothetical 250-unit apartment project are shown in Figure 2 (see previous page) and discussed below.

The analysis results are as follows:

- The assumed transit access benefit of a 5% increase in rental revenue translates to an approximately 81% increase in residual land value, indicating that a developer could afford to pay approximately 81% more for land acquisition.
- An SSA tax rate of 0.28% (corresponding to a half-mile value capture district) reduces the increase in the residual land value due to transit accessibility from 81% to 71%. The SSA rate of 1.1% (corresponding to a quarter-mile value capture district) reduces the increase in the residual land value due to transit accessibility to 43%.
- The development impact fee of \$3,760 per unit, calculated based on the likely transit ridership generation from the apartment project, reduces the increase in the residual land value from 81% to 56%.
- As previously indicated, a TIF-like value capture mechanism as conceived in this study would have no impact on development economics because it imposes no new taxes or fees on new development. As a result, the increase in the residual land value due to transit accessibility is the full 81%.

The analysis highlights that proper calibration of the SSA tax or impact fee is critical to ensuring that the value capture mechanism does not become a disincentive for transit-supportive private development. The actual effect on development economics is highly sensitive to the actual rent/price increase achieved due to a transit station and the tax or fee levels established. Because a tax or fee does diminish project value, it must be sized correctly such that the entire value enhancement associated with a transit improvement is not eliminated.

## Implementation Considerations

Based on the analysis in this study, it appears that a TIF-like mechanism, an SSA and impact fees would potentially be the most viable value capture mechanisms in Illinois and the CMAP region. These mechanisms have the potential to generate the larger amounts required for a competitive 40% to 60% local match for station improvements, but also have key implementation-related considerations:

- Value capture has been utilized for over a century in the United States, but is not well known in the region. It is critical to educate municipalities, taxpayers and underlying taxing districts regarding the need for increased transit, the high competitive local match requirement and the value capture tool.

- Potential value capture districts will require significant intergovernmental cooperation, as each of these tools will require participation of municipalities, transit agencies and other taxing districts to establish them and ensure the proper flow of funds. Each of the evaluated mechanisms is currently only allowable at the municipal or county level, but transit improvements are rarely municipally based. If these tools are to be used for multiple stations or intra-municipal trackage projects, then extra cooperative agreements or higher-level mechanisms will be needed. Therefore, transit agencies will need to work in tandem with municipalities to create the required districts and to educate the public about the potential value capture district.
- While all of these mechanisms are already enabled in a basic form, legislative amendments are required to make them effective as a viable transit value capture mechanism.

## Conclusions

Overall, there is significant potential for transit value capture districts in Illinois to serve as a new source of local match funding. As demonstrated in our study, all of these mechanisms can be calibrated such that they do not have a material impact on development economics. Each situation is likely to require a unique approach and district tailored to its characteristics:

**TIF-Like Mechanism:** As conceived in this study, a TIF-like mechanism generates the greatest bonding capacity, up to five times the bonding capacity of the similarly-sized SSA. However, this capacity is dependent upon the accelerated inflation rate (from normal property inflation, transit access-related value enhancements and new development) anticipated in a new station area, and the level of base EAV. Furthermore, the full capacity is unlikely to be available, as there is a growing concern in Illinois regarding the finances of underlying taxing districts in TIFs. In the context of value capture, the scope of the districts being contemplated is large, and any potential TIF-like value capture district will need to be carefully designed to meet both the requirement for transit funding and the need to provide incremental taxes back to underlying districts.

Additionally, as currently designed, TIF is used by single municipalities for local improvements. Should a transit agency desire to utilize a TIF-like mechanism to fund trackage, rolling stock or other types of improvements that cross multiple municipalities, TIF-sponsored development on a municipality-by-municipality basis to cover all the desired improvement areas will likely be difficult to achieve. An alternative may be to create a limited-purpose type Value Capture District with a limited TIF-like mechanism that only transit agencies can create, and is utilized solely to fund transit improvements. This type of TIF would be similarly limited by the need to share increment with underlying districts or to limit the portion of increment allocated to the value capture district.

**SSA:** An SSA offers a more certain and predictable financing option than TIF, but requires buy-in from district property owners and taxpayers. Therefore, education regarding the benefit of the new transit infrastructure within the potential SSA area is necessary. Strong, organized taxpayer opposition can block creation of a potential SSA district. An SSA mechanism appears to be able to sufficiently fund smaller magnitude transit improve-



ments (station only) with a reasonable tax rate in a half-mile district. However, it is unlikely to be able to produce the amount of funds required if new trackage is required, unless the potential improvement area is densely built and of high value.

Like a TIF district, SSAs are now only sponsored by municipalities or counties for localized improvements. To be truly effective in funding transit, a transit agency-sponsored SSA mechanism may need to be created to allow for streamlined and consistent funding processes. Like the transit-sponsored TIF district above, this district would likely be limited to solely funding transit improvements, without the other types of improvements and services that the current SSA law allows.

**Impact Fee:** Impact fees are the most limiting because the timing and amount of new development is difficult to predict, as well as the fee revenues dependent on that new development. An impact fee offers significant potential revenue per project, but new development of the scale required is not predictable enough to issue bonds, and may only be suitable when entire transit-oriented districts are being contemplated for new construction or redevelopment.

In the course of our analysis, we determined that the preferred value capture tools are generally municipal in nature. This study shows the application of these mechanisms individually on a single, prototypical station area. We believe that the greatest potential arises when multiple new station areas are combined to generate funds. Under current law, these arrangements would be completely voluntary, and it may be desirable to explore county-level, line-level or regional-level variants. In addition, these individual mechanisms can be combined for single station areas to further enhance the revenue-generating potential and fairly distribute costs. In these situations, municipalities and transit agencies will have to weigh the costs and benefits of each mechanism to reach an optimal allocation of funds towards the local match component of the transit improvements and other transit-supportable expenditures.