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Legislative
Analysis
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BENTON HARBOR ENTERPRISE ZONE

House Bill 5419 (Substitute H-2)
First Analysis (3-19-90)

Sponsor: Rep. Lad Stacey
Committee: Taxation

THE APPARENT PROBLEM:

In 1985, the legislature authorized the creation of an "enterprise zone" in Benton Harbor, an economically devastated city of under 15,000 people in southwestern Michigan. The concept of the enterprise zone became popular during the 1980s as an alternative method of stimulating economic development, a method that emphasized the removal of suspected barriers to development rather than programmatic intervention. The underlying argument was that reducing taxes and government regulation in a special targeted area would produce increased economic activity there. (Obviously, this was a controversial idea.) Although the Enterprise Zone Act was drafted in general terms, only Benton Harbor met the criteria for a city to participate: an unemployment rate over 25 percent; median family income less than 55 percent of the state average; an average millage rate over 30 mills; and a state equalized valuation (SEV) of under \$4,000 per capita. The act granted to qualified new or expanding businesses in the enterprise zone a 60 percent reduction in local property taxes, and two companion acts granted them a credit against the single business tax, and an exemption from sales and use taxes for certain purchases. Originally, the city had two years from the date the zone was created (July 31, 1986) to certify businesses, but this deadline was extended for another two years in 1988.

The Enterprise Zone Act also, among other things, created a seven-person authority to provide assistance and to conduct evaluations. The authority's membership includes representatives of the Departments of Treasury and Commerce, as well as members from outside state government. The authority's first analysis of the effects of the enterprise zone experiment was due in October of 1989. That analysis said the enterprise zone program in Benton Harbor should be continued and recommended a number of changes be made to increase the effectiveness of the program, some of which require amending the enabling act. (An official of the Michigan Enterprise Zone Authority has said that while the first two years of the zone's operation were very disappointing, there is currently a sense of momentum in the city that leads the authority to believe a turnaround is happening.) Legislation has been introduced to extend the program for four more years and to implement the authority's other recommendations, which include lowering the property tax rate for existing business property (which get no benefit now) to the statewide average rate with all the revenue to go to the city for infrastructure improvements, and to reduce the amount of investment an expanding business must make to qualify for enterprise zone benefits.

THE CONTENT OF THE BILL:

The bill would amend the Enterprise Zone Act to do the following:

- Extend the program for four more years, by allowing the certification of businesses for up to 8 years after the zone was approved (that is, until July of 1994).

- Reduce the amount an existing business must invest in an expansion to qualify for enterprise zone benefits from 100 percent of current true cash value to 50 percent of true cash value. (The act currently says that restoration, alteration, or renovation of a property only constitutes a "new facility" if the increase in true cash value of real and personal property is equal to or greater than the true cash value before the work was done. An existing business can only get benefits currently if it constructs a "new facility.")
- Allow the property tax rate on existing commercial and industrial property in the enterprise zone to be reduced to the statewide average property tax rate. An existing business could reduce its property taxes by the sum of: the amount spent in a year to restore, alter, renovate, or improve real property in the enterprise zone; fifteen percent of wages paid during the year to residents of the enterprise zone hired after the bill's effective date; twenty-five percent of wages paid during the year to residents of the zone who had been unemployed for at least six months prior to being hired; and cash and in-kind contributions made during the year and accepted by a taxing unit located in the zone. (Tax officials say the statewide average property tax rate was 57 mills in 1989, whereas the tax rate in Benton Harbor is 82.75 mills.) The bill would accomplish this end by exempting existing property from ad valorem real and personal property taxes; imposing a specific tax at the same rate as current real and personal property taxes; and reducing that tax to the statewide average property tax rate by granting credits.
- Specify that revenue from the new specific tax on existing commercial and industrial property (taxed at the statewide average rate) be distributed to the taxing units in the same proportion as property taxes are currently, except that the revenue that would otherwise be disbursed to a local school district for operating purposes would be paid instead to the city in which the enterprise zone is located. (The share that the city would have captured from other taxing units under a tax increment financing plan would still be captured from those units.) The city could enter into agreements to share revenue with a taxing unit that has lost revenue due to the reduction in tax rate and to share revenue with a downtown development authority or tax increment financing authority to make up lost revenue.
- Condition the reduction in property taxes for existing businesses on the city's doing the following: developing a comprehensive development plan that addresses the city's needs and that includes a spending plan approved by the enterprise authority for new revenue resulting from the provisions of the bill; hiring an enterprise zone assistant to oversee development of the spending plan and to aid in other economic development efforts; and using at least ten percent of the money distributed under the spending plan to create a revolving loan fund for small businesses that have difficulty obtaining financing in existing markets.

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OVER

- Set the specific tax on exempted new business property at 50 percent of the statewide average property tax rate rather than 40 percent of the local millage rate, and limit after April 1, 1990, property tax abatements to new investment. A business that requested the revocation of its industrial facilities exemption (under Public Act 198 of 1974) after April 1, 1990, would be subject to the specific tax rather than reduced property taxes.

MCL 125.2103 et al.

FISCAL IMPLICATIONS:

The School Aid Fund would be required to make up about \$1.3 million of revenue lost to the Benton Harbor School District under the bill, according to staff of the House Taxation Committee and Michigan Enterprise Zone Authority. Currently, according to the authority, the enterprise zone costs the state \$350,000 in higher school aid payments, \$25,000 in foregone single business tax revenue, and a small amount of foregone sales and use tax revenue. (3-14-90)

ARGUMENTS:

For:

The bill would implement recommendations made by the Michigan Enterprise Zone Authority for improving the operation of the Benton Harbor enterprise zone. A spokesperson for the authority has said that after a disappointing start, the enterprise zone is gaining momentum. City officials say that in the last two years tremendous strides have been made, including streamlining city government and investing in the city's infrastructure. Some 20 firms certified by the authority and operating in the city will have invested over \$14 million in the city by the end of 1990, creating over 140 new jobs with a payroll over \$2 million, according to the authority's October 1989 evaluation of the enterprise zone. Half of those jobs will go to Benton Harbor residents, says the evaluation. Annual property taxes paid to the city will increase by \$235,000 by 1990. This bill would make the operation of the zone more effective by offering tax reduction incentives to existing businesses that invest in their property or create new jobs or help improve the city's infrastructure; by mandating the adopting of a comprehensive economic development plan for the city; by establishing a revolving loan fund to help small business with financing problems; by generating substantial new revenue for the city by dedicating taxes that would otherwise go the school district to the city (with the state to make up lost school revenue); and by encouraging new and existing businesses to invest in Benton Harbor by reducing the amount of investment necessary for a business to receive enterprise zone benefits.

Against:

Several objections have been raised to specific provisions in this bill. There is opposition to the legislature's requiring the city to hire a special person to oversee the enterprise zone on the grounds that local officials should be allowed to make those kind of management decisions without interference by the state. There is also opposition to the city's operating a revolving loan fund for small businesses, since the extension of credit ought to be a private sector function, or at least ought not to be a function performed by a local unit of government. Some people believe that there ought to be residential property tax relief available in an enterprise zone as well as relief for commercial and industrial enterprises. Representatives of taxing units that

stand to lose revenue under this bill have expressed qualms.

Response: The substitute bill, it should be noted, reduces considerably the amount of revenue lost by any taxing entity (such as the local community college and intermediate school district) and allows the city and another taxing unit to enter into an agreement to make up lost revenue. There has been discussion of extending property tax relief to residential property (although 75 percent of such property in Benton Harbor is said to be rental property), state officials say, but the issue has been deferred.

POSITIONS:

Representatives from the City of Benton Harbor testified in support of the bill before the House Taxation Committee. (3-14-90)