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DELETE RETAIL EXCLUSION IN MSF ACT

House Bill 5144 as enrolled
Second Analysis (1-7-88)

Sponsor: Rep. Virgil Smith, Jr.
Committee: Economic Development and Energy

THE APPARENT PROBLEM:

The Michigan Strategic Fund Act was drafted in 1984 as part of a continuing effort by the state to promote economic development and help diversify the state's economic base. The fund was created primarily for the purpose of insuring loans from banks and other state lending institutions to state businesses—specifically, businesses within the industrial, commercial or agricultural sectors—and to help finance certain nonprofit research "centers of excellence" within the state. The program's primary goal from the beginning, of course, has been to provide a fund from which qualifying businesses within the state would be able to borrow (through a participating lender) in order to expand and, accordingly, open the way for more job opportunities.

The language of the act, however, stipulates that money within this fund can only be directed toward economic endeavors "related to industrial, commercial, or agricultural enterprise." Retail businesses are disqualified from participation in the fund. Since much confusion exists in interpreting exactly what constitutes a "retail" business, many banks have shied away from the program because of the potential for bureaucratic involvement. Some people feel that opening the fund to a large portion of the retail sector would work to get more banks involved in the program and, ultimately, would help diversify the state's economic base even more.

Perhaps the most important reason to include a portion of retail business in the program concerns the large percentage of minority owned businesses which are retail businesses. Some feel that current law, however unintentionally, denies a significant number of minorities within the state's business community from participating in the program. Obviously, minority-owned businesses would tend to be located in areas having larger minority populations in general—where unemployment already is unusually high.

The act currently authorizes MSF to provide grants to nonprofit research and development institutions, but limits this financial support to a four year period. With this stipulation, the act undermines the purposes of the Centers of Excellence Program to fulfill commitments made to various research centers, commitments which have required more time for follow-through than originally had been planned.

And finally, the act includes language which is either obscure or ambiguous and also includes procedures which MSF administrators—since the program's inception—have found to be inconvenient or unnecessary to its smooth operation. In order for the program to be administered more effectively, some of the language in the act needs to be clarified and procedures revised, accordingly.

THE CONTENT OF THE BILL:

The bill would amend the Michigan Strategic Fund Act to modify a provision which excludes retail businesses from receiving loans insured through the MSF from various lending institutions throughout the state. The bill would permit the MSF—in addition to other loans it is allowed to subsidize—to insure business loans made through the Capital Access Program from various lenders to any retail business in the state, and to make direct loans through its Minority Venture Capital Program to minority-owned retail businesses.

The bill would amend the act to extend a limit placed on working capital grants to nonprofit research centers of excellence from four to ten years. In addition, the bill would provide that property owned and used or occupied by those non-profit research centers whose total financial aid from the fund is $1 million or more be exempt from real and personal property taxes imposed by the general property tax act. This exemption would only be granted to these centers if their sole purpose is to perform research and development in present and emerging technology and to apply the knowledge gained from this research to business and industry under a non-profit status. (Note: This exemption language is identical to Senate Bill 227, which amended the same section of the act and was enrolled before House Bill 5144. The language must be in both bills to prevent its accidental repeal, depending upon the order in which the bills are signed.

Along with these substantive amendments, the bill would clarify obscure and ambiguous language and revise certain procedures of the MSF. In addition to various technical amendments, the bill would:

- allow the MSF to submit a status report—detailing the activities of the program—annually instead of every three months;
- delete a requirement for an auditor general "program" audit, but maintain a general audit (essentially a technical amendment);
- delete a provision in the original act which attempted to promote the creation of small business lending companies, which has since become obsolete;
- provide that certain tasks pertaining to the MSF be performed by any member of the MSF board as the board, by majority vote, may determine;
- allow the MSF the option to restructure its Seed Capital Funds Program using a combination of "investment" and management subsidies to increase the fund's incentives for raising private capital; and
- amend current language to close a potential loophole allowing a minority venture capital company to skirt an enforcement mechanism within the act.

MCL 125.2004, et al.

FISCAL IMPLICATIONS:

The House Fiscal Agency reports the bill would have minor fiscal implications to the state's school aid fund since the bill would exempt the MSF research centers in three state municipalities from local property taxes. (1-7-88) The

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Department of Commerce also reports that the bill would have no direct fiscal impact on the state. The department, however, reports that it could have a positive impact on the state in the long run by opening up more opportunities for business expansion—both within retail and manufacturing sectors—and ultimately increase job opportunities and tax revenues here. The bill would not grant the MSF more money to work with; it would only help the program use more efficiently the funds it has already been granted. (12-2-87)

ARGUMENTS:

For:

The MSF originally was created to give the state a fund from which it could draw to help insure state lending institutions' business loans to businesses within industry and manufacturing. Drafters of the MSF act originally excluded retail business from the program since it was thought at that time that the retail sector would not contribute as much to state expansion as industrial, commercial and agricultural endeavors. Since the program's inception in 1984, however, MSF administrators have found, indeed, a great potential for contribution from the state's retail "industry" into the state's overall economic expansion. In addition, including retail businesses in the act would tempt more state lending institutions to take part in the program since the current act requires, in many instances, an interpretation as to what constitutes a retail business and what does not—which makes lenders leery of potential bureaucratic involvement.

For:

When the MSF was created in 1984, the program—by default, perhaps—made few allowances for minority involvement. However, because more businesses since that time—particularly within the retail sector—have sprung up under minority ownership, more has been done to promote equity within the program. For instance, in 1985 the state appropriated \$2.5 million for the fund which was to be used only for direct loans to minority-owned business. But there was no language in the act to ensure that the designated appropriation—which, incidentally, amounts to only 2 percent of the fund's total assets—was used to its maximum potential. House Bill 5144 would alter language within the act to aid the program in using more effectively its appropriations set aside for minority-owned retail business.

Against:

Originally, the program's purpose to help subsidize nonprofit research centers of excellence was with the understanding that these research centers would eventually be able to exist without the state's help. The state would help get research centers organized, and the centers would grow to become independent of state subsidization. House Bill 5144 would encourage these centers to continue to rely on state help rather than motivate them to become fairly autonomous. If nothing else, the bill should be amended to accommodate working capital grants of not more than six years.

Response: Although it's true that the program was designed to create and organize these research centers and help them become independent, administrators of the MSF have discovered—through close contact with these centers' directors—that four years is not enough time to get a research center organized to stand on its own. The MSF administrators, in concurrence with the centers' directors, have decided that a ten-year limit on working capital grants would give the centers enough time to establish themselves financially.

Against:

Because the MSF Program is still in its early years and in spite of the program's apparent progress, the state should continue to keep a close eye on the program. Although this bill would still require the MSF to report its activities, changing the reporting time from quarterly to annually could reduce safeguards needed to ensure proper use of funds.