House
Legislative
Analysis
Section

Olds Plaza Building, 10th Floor
Lansing, Michigan 48909
Phone: 517/373-6466

RESIDENTIAL ENTERPRISE ZONES

Senate Bill 662 (Substitute H-3)
First Analysis (6-9-92)

Sponsor: Sen. Jon Cisky
Senate Committee: Local Government and Urban Development
1st House Committee: Taxation
2nd House Committee: Housing and Urban Affairs

THE APPARENT PROBLEM:

Many of Michigan's older cities are said to be faced with severe housing problems and deteriorating residential neighborhoods, exemplified by the loss of owner-occupied residences and the increase in rental properties controlled by absentee landlords. In many cities, there is a loss of housing stock and a complete absence of new housing construction, particularly of owner-occupied homes and single-family homes. Property values have grown slowly or even declined. The cycle is all too familiar: as people and businesses move from the city to the suburbs, conditions worsen (yet taxes increase) and encourage more "flight." Not only is this disastrous for the urban centers, but it is wasteful, in that the infrastructure of the city must be built over again in outlying areas. Some people have proposed using tax incentives like those used to influence location decisions by business and industry in order to encourage more housing construction and home ownership in the cities.

THE CONTENT OF THE BILL:

The bill would create the Neighborhood Enterprise Zone Act, under which property owners in designated areas in certain municipalities could receive reduced property taxes for building new housing or rehabilitating existing housing. To qualify, a residential facility would have to be (or include) the principal residence of the owner. Generally, the tax reduction would be achieved for new housing by reducing the tax rate to one-half of the statewide average and for rehabilitated housing by using the property's assessed value prior to its improvement. An owner or developer would need the approval of the local unit of government and the State Tax Commission (based on certain specified criteria, including the amount invested in upgrading a residence) to obtain a neighborhood revitalization exemption certificate that would be good for 12 years. A certificate could not be granted after December 31, 2002.

Eligible Communities. The following are the criteria a city would have to meet to participate:

-- a population of 10,000 or more;
-- an average unemployment rate of 10.7 percent or more (in the most recent calendar year for which information is available from the state employment security commission) or a total millage rate of 84 or more mills levied in the most recent property tax levy;
-- a total millage rate of 65 or more mills or a city income tax;
-- sixty percent or more of the housing units built before 1960;
-- a percentage increase in state equalized valuation between 1970 and 1990 of less than 140 percent;
-- a decline in population between 1970 and 1990 of more than five percent.

A city would have to meet all of these criteria to participate unless it is the largest city in population in a metropolitan statistical area, in which case it would have to meet three of the criteria. (The cities that are said to qualify include Albion, Battle Creek, Bay City, Benton Harbor, Detroit, Ecorse, Flint, Grand Rapids, Hamtramck, Hazel Park, Highland Park, Inkster, Jackson, Kalamazoo, Lansing, Melvindale, Muskegon, Muskegon Heights, Oak Park, Pontiac, Port Huron, River Rouge, Saginaw, and Ypsilanti.)

A village or township would have to meet all of the following criteria:

-- a population of 5,000 or more;

-- an average unemployment rate of 17 percent or more;
-- a total millage rate of 65 mills or more;
-- a decline in population of more than 20 percent between 1970 and 1990.

(The only township said to qualify is Royal Oak Township.)

The Michigan Enterprise Zone Authority would be required to publish a list of local governmental units that it certifies as meeting the criteria no later than 30 days after the effective date of the new act. Local units could be added to the list annually after that, but the authority could make no new determinations after December 31, 1993.

Designation of a Neighborhood Enterprise Zone. The governing body of a local governmental unit could by resolution designate one or more neighborhood enterprise zones within the unit. A zone would have to contain at least ten platted parcels of land, and all the land within a zone would have to be compact and contiguous. The total amount of acreage within all zones in a local unit could not exceed 10 percent of the total acreage of the local unit if the unit met all the criteria for eligibility, five percent of the unit's total acreage if not all criteria were met, or 500 acres in a local unit that has already established an enterprise zone under the Enterprise Zone Act of 1985. (A zone could be designated that would be limited to new facilities if each new facility was part of a development of ten or more units. The total acreage of such a zone could not exceed one percent of the local unit's total acreage.) The acreage limit would increase one percent for each one-half of one percent reduction in the property tax rate, up to a limit of 25 percent of acreage. It would also subsequently decrease one percent for each one-half-of-one percent increase in the millage rate, but not below the initial limit. A decrease would not affect any existing certificate.

At least 60 days before acting on a resolution designating a zone, the clerk of the local unit would have to give written notice to the assessor and to the governing body of each taxing unit that levies property taxes in the zone. (The assessor would be required to furnish to the governing body of the local unit the amount of the true cash value of the property located within the proposed zone.) Before acting on the resolution, the governing body of the local unit would have to: make a finding that the proposed zone was consistent with its master plan and its neighborhood preservation and economic development goals; adopt a statement of goals, objectives, and policies relative to the maintenance, preservation, improvement, and development of housing for all persons regardless of income level living within the proposed zones; and pass a housing inspection ordinance that at a minimum requires that an inspection be made of any units with enterprise zone certificates prior to a sale and that a sale could not be finalized until local construction and safety codes were met. The local unit would have to hold a public hearing before acting on a resolution; the hearing would be held no later than 45 days after the notice was sent out by the clerk.

Eligible Residential Facilities. To qualify for an exemption certificate, a "new facility" would have to be a primarily residential structure of one or two units, with one of the units occupied by the owner as his or her principal residence. It could also be a new individual condominium unit, in a structure of one or more condominium units, that was or would be occupied by the owner as his or her principal residence. Apartments would not be eligible as new facilities. An eligible "rehabilitated facility" would be an existing structure consisting of one to eight units with a current true cash value of $60,000 or less per unit. The owner would have to be proposing improvements that would cost, if performed by a licensed contractor, over $5,000 per owner occupied unit or 50 percent of the true cash value, whichever was less, or $7,500 per nonowner-occupied unit or 50 percent of the true cash value, whichever was less, and that would bring the structure into conformance with minimum local building code standards for occupancy or would improve the livability of the units while meeting minimum local building code standards. A condominium unit could also qualify as a rehabilitated facility if it met the same criteria. A facility rehabilitated with the proceeds of an insurance policy for property or casualty loss would not qualify.

Neighborhood Enterprise Zone Tax. A residential facility that is issued an exemption certificate would be subject to a specific tax (rather than the usual property tax) called the neighborhood enterprise zone tax. The tax would be on the facility only and not on the land, which would continue to be subject to the regular property tax. For new housing, the tax would be determined by multiplying the structure's state equalized valuation (SEV) by one-

half of the statewide average millage rate. (The average millage rate in 1989 was said to be 57 mills.) For rehabilitated housing, the tax would be determined by multiplying the SEV of the structure for the tax year immediately preceding the effective date of the exemption certificate by the total mills levied by all taxing units within the city.

The enterprise zone tax would be paid in the same manner and the revenues disbursed in the same manner as the property tax. However, if an intermediate or local school district was receiving state school aid, the amount that would be paid to the district would be paid to the state treasury to the credit of the state school aid fund (unless the State School Aid Act was amended to take the zone tax into account). If the amount a school district received in state aid was less than the combined revenue from the enterprise zone tax, the industrial facility tax (under Public Act 198 of 1974), and the commercial redevelopment act (under Public Act 255 of 1978), the treasury department would pay the district the amount of the difference.

Exemption Certificate Process. The application for a neighborhood enterprise zone certificate would be filed with the clerk of the local governmental unit by the owner or developer involved. The application would have to be filed in a manner and form prescribed by the state tax commission before a building permit had been issued. (However, an application could be filed if a permit had been issued after September 15, 1991 and before December 31, 1992, if the area in which the new or rehabilitated facility was located was designated a neighborhood enterprise zone by the local unit in the calendar year 1992.) The local legislative body would be required to approve an application and send it to the state tax commission no later than 60 days after receiving it. The state tax commission would have 60 days to determine if an application for a rehabilitated facility complied and 30 days (or 45 days for applications received after October 31) to review a new facility application. If the commission found compliance it would issue the certificate and send a certified copy to the assessor of the local governmental unit and to each affected taxing unit. Notice of the commission's refusal to issue a certificate would be sent by certified mail to the same people. (The commission could only issue a certificate if a facility complied with all requirements.)

Duration of Certificate. A neighborhood enterprise certificate would remain in effect for 12 years, unless revoked earlier. A certificate would take effect the first day of the tax year following the year in which the new housing or rehabilitated housing was substantially completed and (for a new facility) occupied by the owner as a principal residence. An owner of a new facility would have to file with the assessor a certificate of occupancy and an affidavit that the housing was occupied by the owner as a principal residence. An owner of a rehabilitated facility would have to file with the assessor a certificate that improvements met minimum local building code standards issued by the appropriate local officer or a certificate of occupancy if required by local building permits or codes and documentation that the rehabilitation cost requirements had been met. A certificate would expire (having never been in effect) if the documentation was not filed within two years after being issued. A one-year extension could be granted if the owner had proceeded in good faith and the delay in completion or occupancy was beyond his or her control. Upon the request of a local government, the state tax commission would extend the certificate of a new facility that had not been occupied. The "principal residence" affidavit would have to be filed by November 1 of each year the certificate for a new facility was in force. If a new facility was sold, the certificate would continue if the new owner filed the principal residence affidavit.

A certificate would be revoked under several circumstances, including at the request of a certificate holder. If a principal residence affidavit was not filed by November 1 for a new facility, the certificate would be revoked. However, if the affidavit was filed before the revocation was effective, the revocation would be rescinded; and if an affidavit was filed after revocation, the certificate could be reinstated for the remaining period of time for which the original certificate would have been in effect. If a facility owner failed to pay the annual neighborhood enterprise zone tax, the commission would revoke the certificate. But the payment of the tax would lead to reinstatement of the certificate. If a facility ceased to have as its primary purpose residential housing, the certificate would be revoked.

Assessor's Report. A local assessor would be required annually to determine the assessed valuation of properties with certificates; the amount of property taxes that would have been paid on properties with exemptions had the certificates not been in force; and the assessed valuation on which

the zone tax was based for a rehabilitated facility. The assessor would report this information to the Michigan Enterprise Zone Authority, the governing board of each affected local taxing unit, and each certificate holder. The notification would have to be sent by certified mail no later than October 15 and be based on the valuation as of the immediately preceding December 31.

Report by the Enterprise Zone Authority and Treasury. Beginning October 1, 1993, the enterprise zone authority and the treasury department would have to jointly prepare and submit to the House and Senate committees responsible for taxation and housing an in-depth analysis of the costs and benefits of the new act and its impact on neighborhood revitalization. The report would have to include specific recommendations for changes in the act. The report would have to be submitted every two years by October 1.

HOUSE COMMITTEE ACTION:

The House Taxation Committee adopted a substitute H-3, which the Housing and Urban Affairs Committee also approved. This differs from the Senate-passed version in several ways, principally in the criteria that determine which communities are eligible to participate. Reportedly, some 17 cities were eligible as the bill passed the Senate, while 24 would be eligible under the House substitute. The substitute also gives to the enterprise zone authority duties that previously were assigned to the state housing development authority and increases the amount of investment required for a rehabilitated property to qualify for a tax reduction.

FISCAL IMPLICATIONS:

There is no specific information. Obviously, some units of government (community college districts, counties, out-of-formula school districts, etc.) will lose tax revenue under the bill, in the sense that they will be participating in the granting of tax reductions to residential property, but advocates for the bill argue that no existing tax base would be lost, only revenue from economic activity that otherwise would not occur.

ARGUMENTS:

For:

This bill offers a targeted approach to improving the housing stock in distressed or declining urban centers of the state. Many of the state's cities have stagnant SEVs (state equalized valuations) and some have next-to-no new housing being built. Tax incentives have long been in use to influence decisions by business and industry. This bill offers a similar tool to provide incentives for people to build houses, renovate property, and occupy homes in urban areas by providing reduced taxes. The bill does not focus on particular buildings and does not grant tax reductions on a case-by-case basis (like some other tax abatement laws), but requires the drawing of a carefully designated area within a city where incentives could be especially beneficial and where all eligible housing would be treated alike. The aim is to generate new and improved housing that would otherwise not exist (not to reward investment that would have occurred anyway) and stimulate investment in areas where it is unlikely now.

Some advocates for this approach claim it is the only way to make urban areas competitive, by building "cities within cities" where investment is rewarded. The high tax rates in many Michigan cities discourage development and investment and make communities uncompetitive. While reducing property taxes citywide is not feasible, this plan begins the process that will allow urban centers to compete with the lower taxes of outlying areas. With an improvement in housing and incentives for people to live in the cities will come other associated economic activity, including stores to provide for the needs of residents.

Against:

Several arguments have been raised against the bill, some of them conflicting, based on the notion of fairness. The issue is who gets to participate, which communities, which investors? The criteria for eligible communities permit some municipalities to participate and exclude others. A slight adjustment one way or another could expand the list of participating communities or shrink it. Are the criteria justifiable on grounds other than simply keeping a particular set of communities on the list? For example, minor adjustments to two criteria (reducing the millage requirement from 65 mills to 63.5 mills and the average unemployment rate from 10.7 percent or more to 10.5 percent or more) would make the city of Alpena eligible to participate. Questions have also been raised about the limit in value for eligible rehabilitated facilities (currently $60,000 per unit). Shouldn't existing homes of higher value qualify where new investment

would stabilize a neighborhood and maintain property values?

Some people argue that the bill should be more carefully targeted to the most distressed areas and that fewer cities should be allowed to participate. It trivializes the problems of the most troubled cities to continually add areas to the list. The state should concentrate on where the problems are the most severe. Once the approach has been tried for a few years, then it could be expanded to include other cities.

Others, on the other hand, would prefer to see the list expanded, whether to the 44 communities that are eligible under state housing development programs, or to any community, urban or rural, where there is little new housing being built and where significant substandard housing exists. Some people argue that it is precisely in those communities where conditions are just beginning to deteriorate or those that are at a critical juncture where this kind of approach can do the most good and not in the cities with the worst conditions.

Against:

At a time when the state is under criticism for the effect of "tax expenditures" on state and local government budgets, is it wise to legislate yet another? The bill would create a two-tiered tax system in participating cities, whereby housing built within one area would be taxed at a lower rate than housing built elsewhere. Others, both within a participating city and without, will bear the burden imposed by lowering the taxes of those fortunate enough to be able to participate. Will the target population really be the beneficiaries or will it mostly aid developers? Can abuses be avoided? Many questions remain.

Response:

There are those who maintain that a program of this sort will, over time, produce greater tax revenue by stimulating more economic activity and not work to anyone's disadvantage. It will make participating cities competitive in a way they otherwise would not be. It will stabilize neighborhoods and raise property values. Furthermore, the program will be reviewed and a report made every two years, beginning in 1993, on its effectiveness.

POSITIONS:

The Department of Treasury supports the bill. (6-3-92)

The Michigan Municipal League supports the bill. (6-8-92)

The National Bank of Detroit (NBD) has indicated its support for the bill. (6-3-92)

A representative of the ANR Pipeline Co. has indicated support for the bill. (6-3-92)

The Michigan Association of Home Builders has testified in support of the concept (although it would like the list of participating communities expanded). (6-3-92)

Representatives from the City of Grand Rapids testified in favor of the bill. (6-3-92)

The Mayor of Flint has indicated his support for the bill. (5-22-92)