

Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536



Telephone: (517) 373-5383
Fax: (517) 373-1986
TDD: (517) 373-0543

Senate Bill 1356 (as reported without amendment)
Senate Bill 1357 (Substitute S-1 as reported)
Sponsor: Senator Glenn D. Steil
Committee: Finance

Date Completed: 11-9-00

RATIONALE

Like other school districts in Michigan, the Grand Rapids City School District has many elderly facilities that need repair and modernization. Apparently, the average age of the district's buildings is over 50 years, and its newest building is more than 25 years old. Almost three years ago, the district's voters rejected a bond proposal that would have financed the necessary renovations. Rather than attempting to raise tax revenue, the district and others have suggested an approach in which an independent entity would acquire school facilities and sell them to private developers, who would improve the facilities and lease them back to the authority, which in turn would lease the facilities to the district. In order to enable the district to go forward with this plan, and to encourage the involvement of developers and other businesses, it has been suggested that the authority be provided for in statute, and that a single business tax credit be created.

CONTENT

Senate Bill 1356 would amend the Single Business Tax Act to do the following:

- Permit a taxpayer or a "qualified taxpayer" (a taxpayer that owned a public school facility and leased it to a public school facility authority) to claim a credit against the single business tax for tax years beginning after December 31, 2000, and before January 1, 2023.
- Specify that for a qualified taxpayer, the tax credit would equal 10% of the cost of "eligible income" (rental and lease income that the taxpayer received from the authority for use of eligible property) for a tax year.
- Specify that a taxpayer's credit would equal 10% of the amount that the taxpayer contributed during the tax year to the public school facility authority.

Senate Bill 1357 (S-1) would create the "Public

School Facility Authority Act" to do the following:

- Permit a public school district, not including a public school academy, to establish a public school facility authority.
- Specify that a school district would have to be located in a city that had a population over 170,000 and was the most populous city in a county with a population over 500,000.
- Provide for the appointment of a five-member authority board.
- Specify duties of the authority, including receiving public school facilities from the district for a nominal fee; leasing public school facilities to the district for a nominal fee; selling, leasing, or purchasing property for projects involving a public school facility; and, developing a public school facility.
- Create a public school facility authority fund.
- Prohibit the authority from levying a tax.
- Exempt from State and local taxes property of the authority, including property it leased to or from private persons.

The bills are tie-barred to each other.

A more detailed description of the bills follows.

Senate Bill 1356

For tax years beginning after December 31, 2000, and before January 1, 2023, a qualified taxpayer could claim a credit against the single business tax (SBT) equal to 10% of the cost of eligible income received or accrued by the qualified taxpayer in the tax year. ("Qualified taxpayer" would mean a taxpayer that owned eligible property. "Eligible property" would mean a public school facility, as defined in Senate Bill 1357 (S-1), i.e., all or any part of school buildings, including library buildings, structures, athletic fields, and/or playgrounds, that were used or intended to be used by a district for instructional purposes, whose ownership had been transferred to an authority or to a private entity that

had entered into a contract to lease it to an authority. "Eligible income" would mean rental and lease income received from an authority for use of eligible property. "Authority" would mean a public school facility authority, as defined in Senate Bill 1357 (S-1).)

For the same tax years, a taxpayer could claim a credit against the SBT equal to 10% of the amount the taxpayer contributed during the tax year to the authority.

These credits would have to be calculated after all other credits allowed under the Act were applied. If a credit allowed under the bill for a tax year and any carryforward of the credit allowed by the bill exceeded the taxpayer's tax liability for the tax year, the portion that exceeded the tax liability for the tax year could not be refunded but could be carried forward to offset tax liability in subsequent tax years for 10 years or until used up, whichever occurred first.

In regard to a taxpayer or a qualified taxpayer that claimed a credit under the bill, an affiliated group as defined in the Act, a controlled group of corporations as defined in the Internal Revenue Code and Federal regulations, or an entity under common control as defined in the Code, would have to consolidate the eligible income or the contributions of the members of the affiliated group, member corporations of the controlled group, or entities under common control, and could claim only one credit under the bill whether or not a combined or consolidated return was filed.

The Department of Treasury would have to develop procedures to implement the bill.

Senate Bill 1357 (S-1)

Creation of Authority

By resolution of the local school board, a district could establish a public school facility authority. On the date on which all of the certified copies of the resolutions establishing the authority were filed with the Secretary of State, the authority would be created. ("District" would mean a public school district located in whole or in part in a qualified city. A district would not include a public school academy. "Qualified city" would mean a city with a population of more than 170,000 that was the most populous city in a qualified county. "Qualified county" would mean a county with a population of more than 500,000 that contained a qualified city and that was not a charter county or a county with an optional unified form of government.)

Authority Board

The powers, duties, and functions of the authority would be vested in a board, which would consist of the following five members:

- Two members who were residents of the qualified city appointed by the local school board of the district, including one who was a member of the school board.
- One member who was a resident of the qualified city appointed by the mayor with approval of the city's legislative body.
- Two members who were residents of the qualified county appointed by the first three members at the first meeting of the board as the first item of business. These two members would have to be selected from a list of five candidates submitted by the board of directors of the chamber of commerce located in the qualified city. At least one would have to have experience in facilities management or construction. Every two years after the first appointment, one member would have to be appointed at the first meeting of the board after the member's term expired.

Board members would be appointed for a term of four years, except that one member initially appointed by the local school board and one from the qualified county would have to be appointed for two-year terms. Subsequent members would have to be appointed for a term of four years.

Notwithstanding a charter provision of the qualified city to the contrary, a member of the legislative body or other city official of the qualified city would be eligible to serve as a member of the board.

Board members would have to serve without compensation. The district would have to provide administrative staff to the authority. The district could receive reimbursement for reasonable and necessary administrative expenses.

Records, material, or other data received, prepared, used, or retained by the authority that related to financial or proprietary information that was identified by the person submitting it and acknowledged by the board as confidential would not be subject to the disclosure requirements of the Freedom of Information Act. The board would be subject to the Open Meetings Act, but could meet in closed session pursuant to that Act to determine whether it acknowledged as confidential any financial or proprietary information submitted and considered by the person submitting it as confidential. ("Financial or proprietary information" would mean information that had not been publicly disseminated or that was unavailable from other sources, whose release could cause the person submitting the information competitive harm.)

Duties of the Authority

The authority could do all things necessary or convenient to carry out the purposes, objectives, and provisions of the bill and the purposes, objectives, and powers delegated to the authority or the board by other laws or executive orders, including soliciting, receiving, and accepting from any source gifts, grants, loans, or contributions of money, property, or other things of value, and other aid or payment, or participating in any other way in a Federal, State, or local government program; receiving public school facilities from the district for a nominal fee; and, leasing public school facilities to the district for a nominal fee.

The authority could hold, clear, remediate, improve, maintain, manage, control, sell, exchange, mortgage, and hold mortgages on and other security interests in, lease, as lessor or lessee, and obtain or grant easements and licenses on property that the authority acquired. A sale, exchange, lease, or other disposition of authority property would have to be to a person for a project involving a public school facility, which would have to be placed on that property in the form of a recordable restrictive covenant effective for not more than 20 years, except for property acquired by the authority and later determined by it not to be necessary for a public school facility, which could be sold or otherwise disposed of. Property being sold would have to be offered first to the district in which the property was located for the nominal fee for which it had been acquired, if the property had been acquired from the district. If property were sold, exchanged, or leased to a person to develop a project involving a public school facility, that person would have to execute an agreement, in recordable form, giving the authority a right of first refusal to reacquire the property for the same amount for which it was acquired from the authority if the property were sold, exchanged, leased, or transferred. Temporary or permanent interests, licenses, or other appropriate interests in property acquired by the authority could be conveyed or granted by the authority for utility, vehicular, or pedestrian traffic facilities, or related purposes not inconsistent with the bill. The authority would not have the power to condemn property.

In addition, an authority could develop a public school facility; reimburse the district for reasonable and necessary administrative expenses; and, do all other acts and things necessary or convenient to carry out the purposes for which the authority had been established. ("Develop" would mean, unless the context clearly indicated a different meaning, to defray all or a part of the cost of purchasing, erecting, completing, remodeling, or equipping or reequipping school buildings, including library buildings, structures, athletic fields, playgrounds, or other facilities, or parts of or additions to those facilities; furnishing or refurbishing new or remodeled school buildings; and acquiring, preparing, developing, or improving sites, or parts of or additions to sites, for school buildings.)

The development of a public school facility under the bill would be subject to Public Act 306 of 1937 and not to the Single State Construction Code Act. (Public Act 306 regulates the construction and remodeling of school buildings, and requires plans and specifications to be approved by the State Superintendent of Public Instruction.)

An authority established under the bill could not levy a tax.

The authority's accounts would be subject to annual audits by the State Auditor General or a certified public accountant selected by the authority. Copies of the audits would have to be forwarded annually to the State Treasurer, as provided in the Uniform Budgeting and Accounting Act. Records would have to be maintained according to generally accepted accounting principles. The authority would have to prepare and adopt an annual budget.

Other Provisions

The bill would create a public school facility authority fund for the authority, which would have to deposit all money received into the fund.

The bill states that property of the authority would be public property devoted to an essential public and governmental function and purpose, and income of the authority would be for a public purpose.

The authority's property, income, and operations would be exempt from all taxes of the State or a political subdivision of the State. Property of the authority that was leased to private persons would be exempt from any State or local tax. Property of the authority and property leased by the authority for use as a public school facility would be exempt from any ad valorem property taxes collected under the General Property Tax Act.

If the authority completed the purposes for which it was organized, it would have to be dissolved by resolution of the board. The authority's property and assets remaining after the satisfaction of the obligations of the authority would belong to the district in which the property was located.

Proposed MCL 308.39d & 308.39e (S.B. 1356)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

This legislation proposes an innovative approach to financing public school facility improvements. Unlike its suburban neighbors, the Grand Rapids City School District is a relatively poor district, where the infrastructure is deteriorating and at least 60% of the students are considered at-risk. Reportedly, most of the classrooms have only one electrical outlet, which means that computers cannot be installed. In view of the district's demographics and the failure of a previous bond proposal, the approval of another proposal appears unlikely. While this legislation would not preclude any future bonding, it would

provide an immediate solution for the district's pressing needs.

Essentially, under the bills, the district would create an independent authority that could acquire school facilities for a nominal sum. The authority then could sell the property to private developers, who would renovate the facilities and lease them back to the authority. The authority then would lease the property to the district for a nominal amount. In return, the developers could claim a credit against their SBT liability for 10% of the rental or lease income they received from the authority. In addition, other taxpayers could claim an SBT credit for 10% of the amounts they contributed directly to the authority, which also could develop the facilities on its own. Once the authority completed its purpose and dissolved, the property would revert to the district.

Businesses already have a stake in an educated workforce, and this proposal would give them a financial incentive to help improve school facilities. In addition, renovated school facilities would enhance the value of surrounding neighborhoods. At the same time, the creation of an independent entity would get the district out of the remodeling and revenue-raising business, and enable it to concentrate on educating students. While individual residents would not be asked to pay higher taxes, which they cannot afford, their children would benefit from modernized classrooms, libraries, playgrounds, and athletic fields. In sum, this legislation proposes a community-wide public-private partnership that could generate a significant infusion of revenue for essential school renovations.

Opposing Argument

It is not clear why this legislation is needed. School districts already may enter into lease-back arrangements with private entities, and businesses already may reduce their SBT base--and thus their tax liability--by making charitable donations. In addition, taxpayers may receive a credit for contributions to community foundations, which can make grants to support public schools.

Response: The proposed authority would be an independent entity representing the interests of the city and the chamber of commerce, as well as the school district, and would relieve the district of the responsibilities of financing and organizing renovations. The authority also could make financial arrangements that would continue despite future changes in the school board. The authority would retain the proceeds received from the sale of school facilities, and would use the funds to make lease payments to the developers once the facilities were renovated.

In regard to the proposed SBT credit, it would be in addition to the existing benefits of charitable giving,

and would create another incentive for businesses to help finance school improvement efforts. Also, the proposed credit for 10% of rental income received from the authority is not available under the existing tax breaks for charitable contributions. In addition, school facilities would remain exempt from property taxation after being sold to a developer, while they were leased to the authority.

Legislative Analyst: S. Lowe

FISCAL IMPACT

Senate Bill 1356

The bill would reduce State General Fund revenues by an unknown amount. The bill would affect single business tax revenues through two credits for different activities relating to a public school facility authority: 1) a credit for donations to an authority, and 2) a credit for income received from property leased to an authority. Depending on how property transfers would be handled under the bill, the bill also could increase the State School Aid Fund by an unknown amount. No precise information is available regarding how many taxpayers would use each credit or engage in new business activity with an authority, or the extent to which revenues would be affected.

The credits in the bill would affect business activity in two ways, both of which would reduce SBT revenues: 1) a shifting of current business activities to take advantage of the credits, and 2) new business activity stimulated by the credits. New business activity related to the credit for donations would reduce revenues. In the case of the second credit, although SBT revenues would increase as taxpayers took on new business with a public school facility authority, the structure of the credits ensures that revenues losses would exceed revenue gains.

The Grand Rapids Public School District is the only district in Michigan that would be able to create a public school facility authority under the bill. The following example illustrates the impact the bill could have. A recent proposal from the school district to renovate and expand four school buildings was estimated to cost \$40 million, less \$5.5 million for "value engineering" on the part of the contractors and developers. Furthermore, according to data from the Michigan Department of Education, the Grand Rapids Public School District spent approximately \$5 million in capital outlay in 1998. Assuming: 1) businesses purchasing property from the authority would recoup their costs by leasing the property back over a 10-year period, 2) once the lease was completed, the property would be donated back to the authority, and 3) certain additional factors regarding the relationship between property values

and the construction and renovation costs, the bill would reduce net SBT revenues by \$10.8 million in the first year, approximately \$1.0 million per year afterward until the lease was completed, and an additional \$14.4 million in the year of the donation. In each of the 10 years the property was owned by the business, the State School Aid Fund would receive an additional \$1.1 million in State Education Property Tax, while local units such as the Grand Rapids Public School District and the City of Grand Rapids would receive an additional \$1.7 million in property tax revenues. In the year of the donation, the business also would experience a reduction in Federal tax liability of \$35.8 million.

Single business tax revenues would be reduced in four ways, only two of which are proposed by the bill; the remaining losses would stem from current tax provisions that would apply to the business activity created/altered by the bill: 1) the tax credit on income from the lease, 2) the tax credit from the donation of facilities, 3) the investment tax credit that the business can claim upon purchasing the property, and 4) a reduction in the tax base in the year of the donation because the donation would qualify as a charitable contribution, thus lowering both the Federal corporate income tax base and the SBT base.

The bill also would have an unknown fiscal impact on the Grand Rapids Public School District and the City of Grand Rapids. To the extent that the Grand Rapids Public School District would participate in arrangements with a public school facility authority, the district could experience changes in the timing and/or levels of certain expenses or revenues. The bill does not clearly define how the authority would ensure that it would have sufficient funds to cover the lease payments, given the increase in property values resulting from the improvements; so local units could experience some increase in expenses in the long term if they had to transfer funds to the authority to cover the lease payments. Furthermore, while property was owned by a business, rather than the district or the authority, the property would be subject to local property taxes. The extent to which property tax revenues to the school district or the city would increase is unknown.

This estimate is preliminary and will be revised when more information is available.

Senate Bill 1357 (S-1)

An eligible local school district could experience reduced costs associated with developing public school facilities if the authority proposed under this bill were able to generate more gifts, grants, loans, or contributions than the district otherwise would generate on its own. It is unknown how "successful"

the authority would be in reducing costs of development compared with members of the school district or the district itself seeking such assistance. According to eligibility criteria in this bill, Grand Rapids public schools is the only district that would qualify.

Fiscal Analyst: D. Zin
K. Summers-Coty

A9900\sb1356a

This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.