

1995-96 SESSION
COMMITTEE HEARING
RECORDS

Committee Name:

Joint Committee on
Finance (JC-Fi)

Sample:

Record of Comm. Proceedings ... RCP

- 05hrAC-EdR_RCP_pt01a
- 05hrAC-EdR_RCP_pt01b
- 05hrAC-EdR_RCP_pt02

➤ Appointments ... Appt

➤ **

➤ Clearinghouse Rules ... CRule

➤ **

➤ Committee Hearings ... CH

➤ **

➤ Committee Reports ... CR

➤ **

➤ Executive Sessions ... ES

➤ **

➤ Hearing Records ... HR

➤ **

➤ Miscellaneous ... Misc

➤ 95hrJC-Fi_Misc_pt99

➤ Record of Comm. Proceedings ... RCP

➤ **



State of Wisconsin • DEPARTMENT OF REVENUE

125 SOUTH WEBSTER STREET • P.O. BOX 8933 • MADISON, WISCONSIN 53708-8933 • 608-266-6466 • FAX (608) 266-5718

Tommy G. Thompson
Governor

Mark D. Bugher
Secretary of Revenue

November 1, 1994

The Honorable Joseph Leean, Co-Chair
Joint Committee on Finance
State Capitol, Room 115 South
Madison, WI 53702

The Honorable Barbara Linton, Co-Chair
Joint Committee on Finance
State Capitol, Room 127 South
Madison, WI 53702

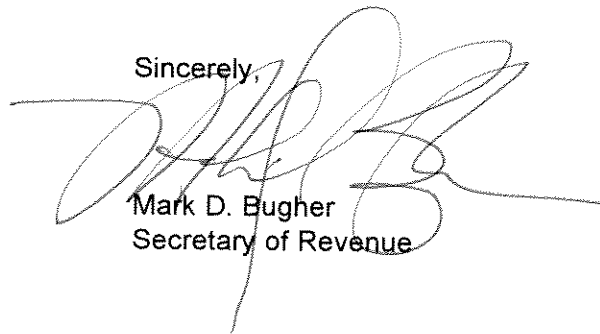
Dear Senator Leean and Representative Linton:

State law requires the Department of Revenue annually, on November 1, to certify to the Joint Committee on Finance the appropriate percentage change in the Consumer Price Index (CPI) for determining a municipality's eligibility for a payment under the expenditure restraint program payment. The Department certifies that the percentage change for 1995 payments is 2.6%.

Sec. 79.05 (1)(am), Wis. Stats., provides that the inflation factor for the expenditure restraint program be the average annual percentage change in the CPI for all urban consumers (CPI-U), U.S. city average, for the 12 months ending on September 30. The Department's certification of this percentage change is required in sec. 79.05 (2m).

The calculation of the inflation factor is shown in the attached table. If you have any questions about our calculation, please contact me.

Sincerely,



Mark D. Bugher
Secretary of Revenue

MDB:BB:skr
c:\unit\cpi94.ltr

Attachment

Consumer Price Index for All Urban Consumers (CPI-U):
 U. S. City Average, All Items, Not Seasonally Adjusted.
 (1982-84=100)

	1992-93	1993-94
October	141.8	145.7
November	142.0	145.8
December	141.9	145.8
January	142.6	146.2
February	143.1	146.7
March	143.6	147.2
April	144.0	147.4
May	144.2	147.5
June	144.4	148.0
July	144.4	148.4
August	144.8	149.0
September	145.1	149.4
Sum	1721.9	1767.1
% Change		2.6%

Source: U.S. Department of Labor, Bureau of Labor Statistics.



State of Wisconsin • DEPARTMENT OF REVENUE

125 SOUTH WEBSTER STREET • P.O. BOX 8933 • MADISON, WISCONSIN 53708-8933 • 608-266-6466 • FAX (608) 266-5718

Tommy G. Thompson
Governor

Mark D. Bugher
Secretary of Revenue

November 1, 1994

The Honorable Joseph Llean, Co-Chair
Joint Committee on Finance
State Capitol, Room 115 South
Madison, WI 53702

The Honorable Barbara Linton, Co-Chair
Joint Committee on Finance
State Capitol, Room 127 South
Madison, WI 53702

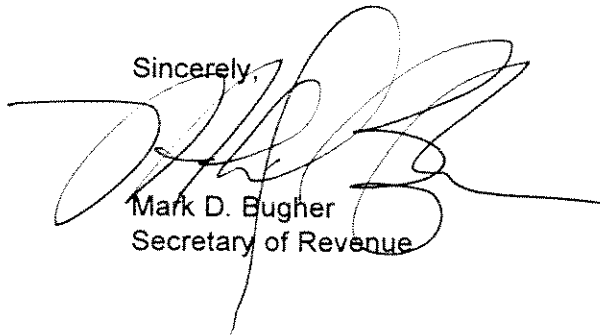
Dear Senator Llean and Representative Linton:

State law requires the Department of Revenue annually, on November 1, to certify to the Joint Committee on Finance the appropriate percentage change in the Consumer Price Index (CPI) for determining a municipality's eligibility for a payment under the expenditure restraint program payment. The Department certifies that the percentage change for 1995 payments is 2.6%.

Sec. 79.05 (1)(am), Wis. Stats., provides that the inflation factor for the expenditure restraint program be the average annual percentage change in the CPI for all urban consumers (CPI-U), U.S. city average, for the 12 months ending on September 30. The Department's certification of this percentage change is required in sec. 79.05 (2m).

The calculation of the inflation factor is shown in the attached table. If you have any questions about our calculation, please contact me.

Sincerely,



Mark D. Bugher
Secretary of Revenue

MDB:BB:skr
c:\unit\cpi94.ltr

Attachment

Consumer Price Index for All Urban Consumers (CPI-U):
 U. S. City Average, All Items, Not Seasonally Adjusted.
 (1982-84=100)

	1992-93	1993-94
October	141.8	145.7
November	142.0	145.8
December	141.9	145.8
January	142.6	146.2
February	143.1	146.7
March	143.6	147.2
April	144.0	147.4
May	144.2	147.5
June	144.4	148.0
July	144.4	148.4
August	144.8	149.0
September	145.1	149.4
Sum	1721.9	1767.1
% Change		2.6%

Source: U.S. Department of Labor, Bureau of Labor Statistics.



123 West Washington Avenue
P.O. Box 7970
Madison, Wisconsin 53707
(608) 266-1018

Tommy G. Thompson, Governor

December 7, 1994

The Honorable Joseph Leean
State Senator
115 South, State Capital
Madison, WI 53702

The Honorable Barbara Linton
State Representative
127 South State Capital
Madison, WI 53702

RE: DEVELOPMENT ZONE APPLICATION PROCESS

Dear Senator Leean and Representative Linton:

The Department of Development has received your letter of November 7th, which indicated that there were no objections to the proposed boundaries for areas nominated for development zone consideration.

However, we thought it best to notify the Joint Committee on Finance, for information purposes, that during the Department's review of the applications to insure that the minimum requirements for nomination were met, it became necessary for several of the applicants to modify their boundaries.

The City of Kenosha in order to meet the assessed valuation requirement reduced the size of their proposed zone by one block. Lafayette County in order to meet the UDAG criteria eliminated the Towns of Shullsburg and Darlington and will proceed with the two cities as separate areas. Marinette County in order to meet the unemployment criteria eliminated the Towns of Niagara and Dunbar from their proposed area.

If you have any questions or need additional information, please contact me at 267-2045. Our intent is to send out the letters of invitation to the communities by December 16, 1994.

Sincerely,

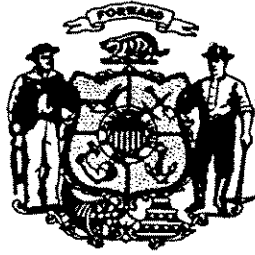
A handwritten signature in cursive script that reads 'Bill Wheeler'.

Bill Wheeler
Director, Bureau of Community Revitalization
Development Zone Program Manager

State of Wisconsin

SENATE CHAIR
JOE LEEAN

Room 119 South, State Capitol
P.O. Bo 7882
Madison, WI 53707-7882
Phone: 266-0751



ASSEMBLY CHAIR
BARBARA J. LINTON

Room 127 South, State Capitol
P.O. Bo 8952
Madison, WI 53708-8952
Phone: 266-7690

JOINT COMMITTEE ON FINANCE

November 7, 1994

Mr. Robert Trunzo, Secretary
Department of Development
123 West Washington Avenue
9th Floor
Madison, WI 53703

Dear Mr. Trunzo:

We have reviewed your notification, dated October 17, 1994, under s. 560.723 of the state statutes pertaining to the proposed boundaries for areas nominated for development zone consideration. There were no objections to the proposed boundaries. Consequently, we are not scheduling a meeting to further review the boundaries.

A handwritten signature in cursive script that reads "Joe Leean".

JOE LEEAN
Senate Chair

Sincerely,

A handwritten signature in cursive script that reads "Barbara J. Linton".

BARBARA J. LINTON
Assembly Chair

JL/BJL/ns

cc: Members, Joint Committee on Finance



123 West Washington Avenue
P.O. Box 7970
Madison, Wisconsin 53707
(608) 266-1018

Tommy G. Thompson, Governor
Robert N. Trunzo, Secretary

October 17, 1994

OCT 19 1994
REC'D JK

14 - NOV → 8th Nov
30 = 20th 1th

The Honorable Joseph Leean
State Senator
115 South, State Capitol
Madison, WI 53702

The Honorable Barbara Linton
State Representative
127 South, State Capitol
Madison, WI 53702

Dear Senator Leean and Representative Linton:

The statutory language for the Wisconsin Development Zone Program requires that the Department notify the Joint Committee on Finance of any boundary proposal for an area nominated for consideration as a Development Zone. The statute states that the Department may designate the proposed boundary if, within 14 days after notification, the Joint Committee on Finance does not schedule a meeting for the purpose of reviewing the proposed boundary. If the Joint Committee decides to hold a meeting for this purpose, it shall be scheduled within 30 days after receiving the initial notification from the Department. If a meeting is scheduled, the Department may not approve the boundary without approval of the Committee.

Pursuant to this requirement (s. 560.723, Stats.), the Department is submitting for your review the proposed boundaries of the areas nominated for Development Zone consideration from the following applicants:

City of Madison
City of Mauston
City of Elcho
City of Kenosha

City of Eau Claire
Marinette County
City of Antigo

City of Two Rivers
City of Menomonie
Lafayette County

Concurrent with the Committee's review of the proposed boundaries, the Department will be conducting its review to insure that the minimum requirements for the nomination phase are met.

If you have any questions, please contact Bill Wheeler, Development Zone Program Manager at 267-2045.

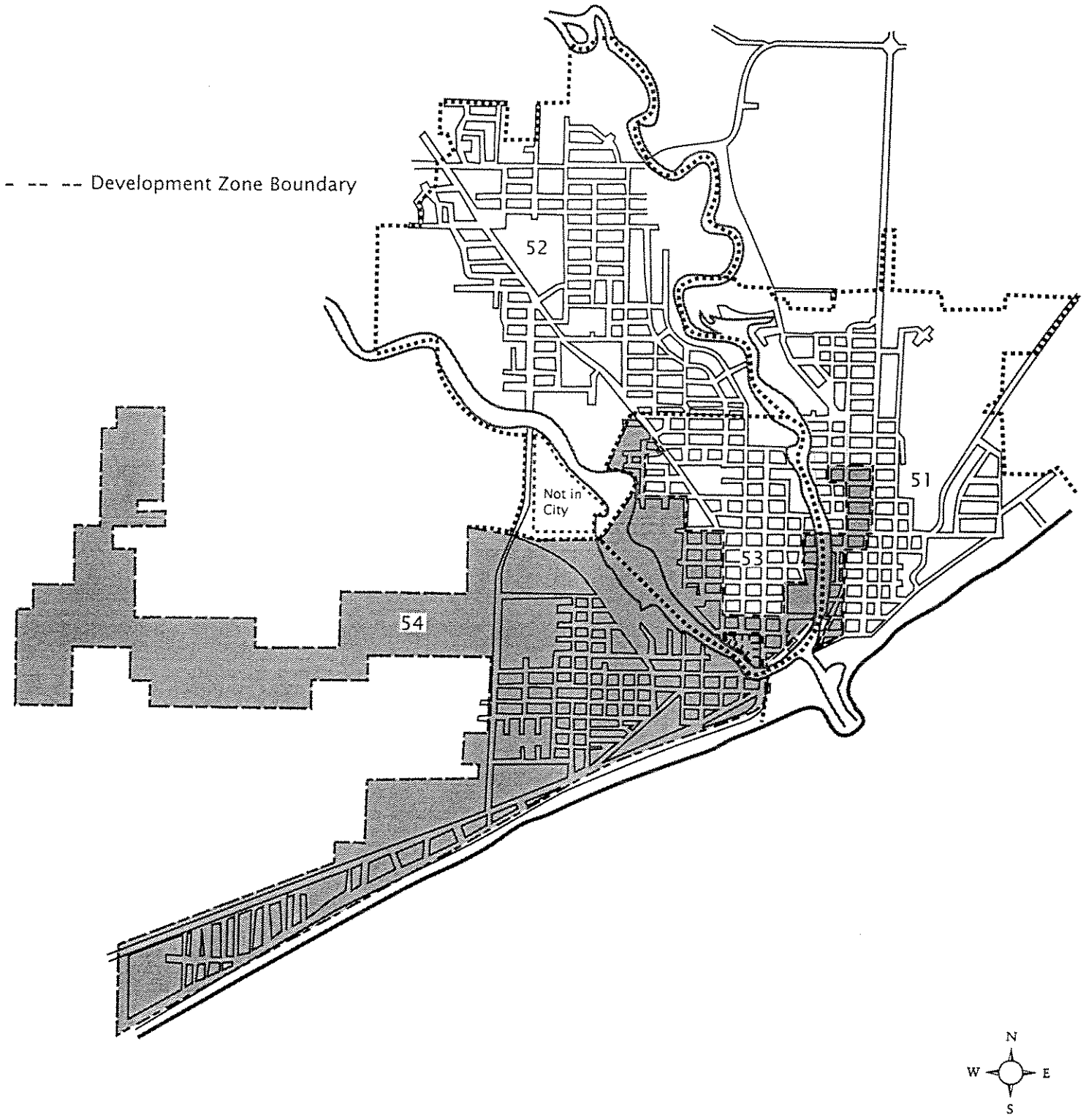
Sincerely,

Robert N. Trunzo
SECRETARY

City of Two Rivers

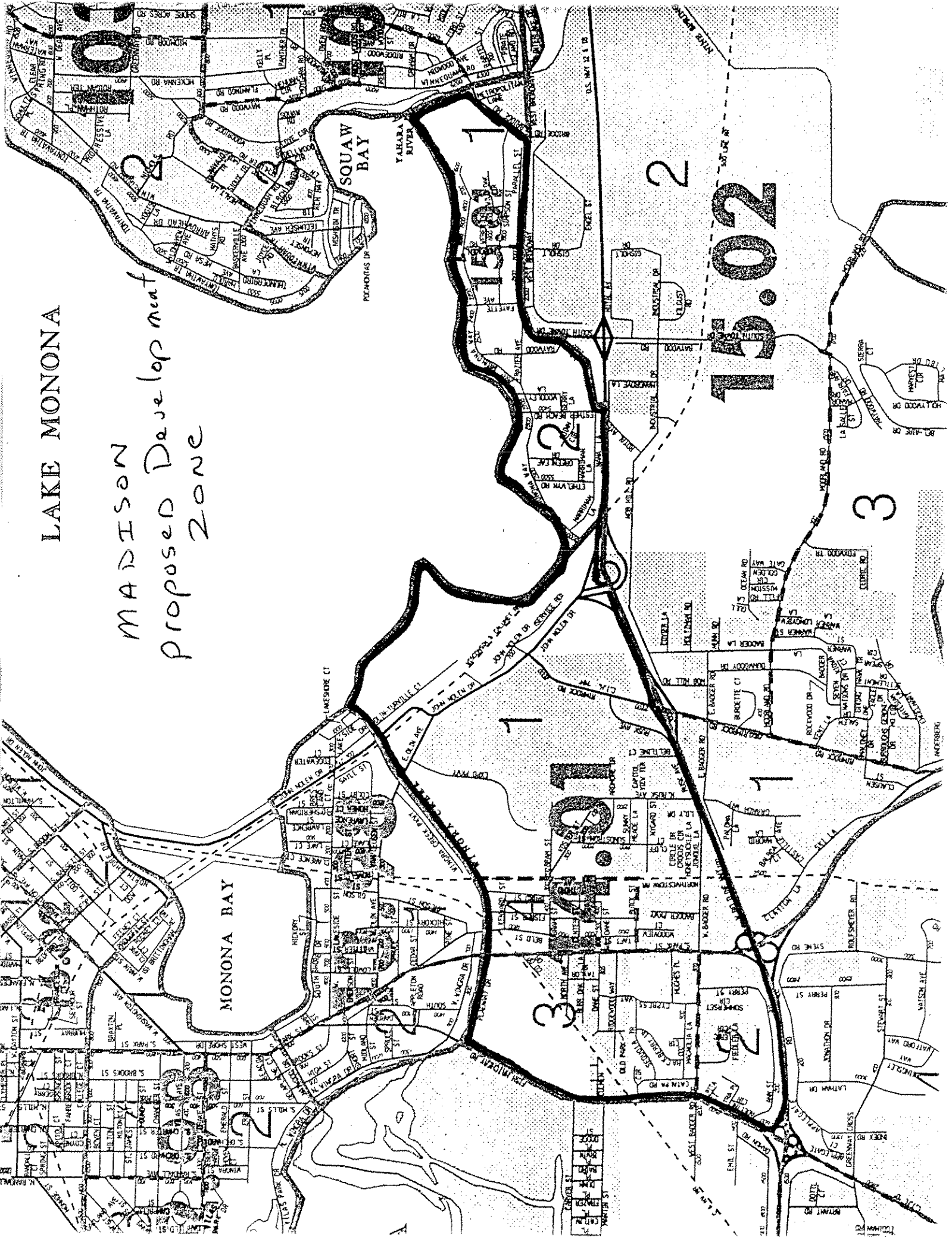
Development Zone Application Map

Census Tracts



LAKE MONONA

MADISON
Proposed Develop ment
Zone



15.02

3

1

3

1

1

2

2

1

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

2

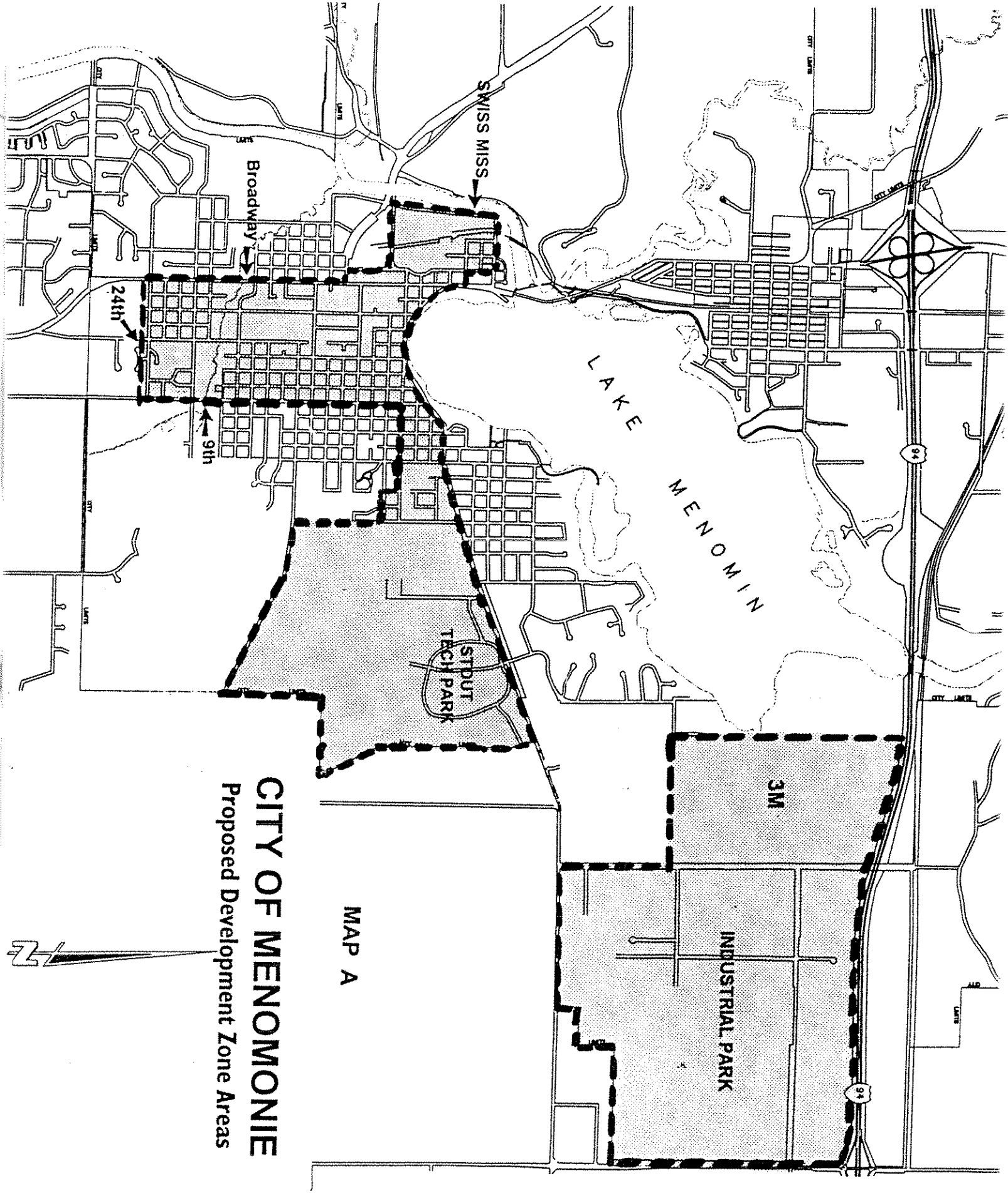
2

2

2

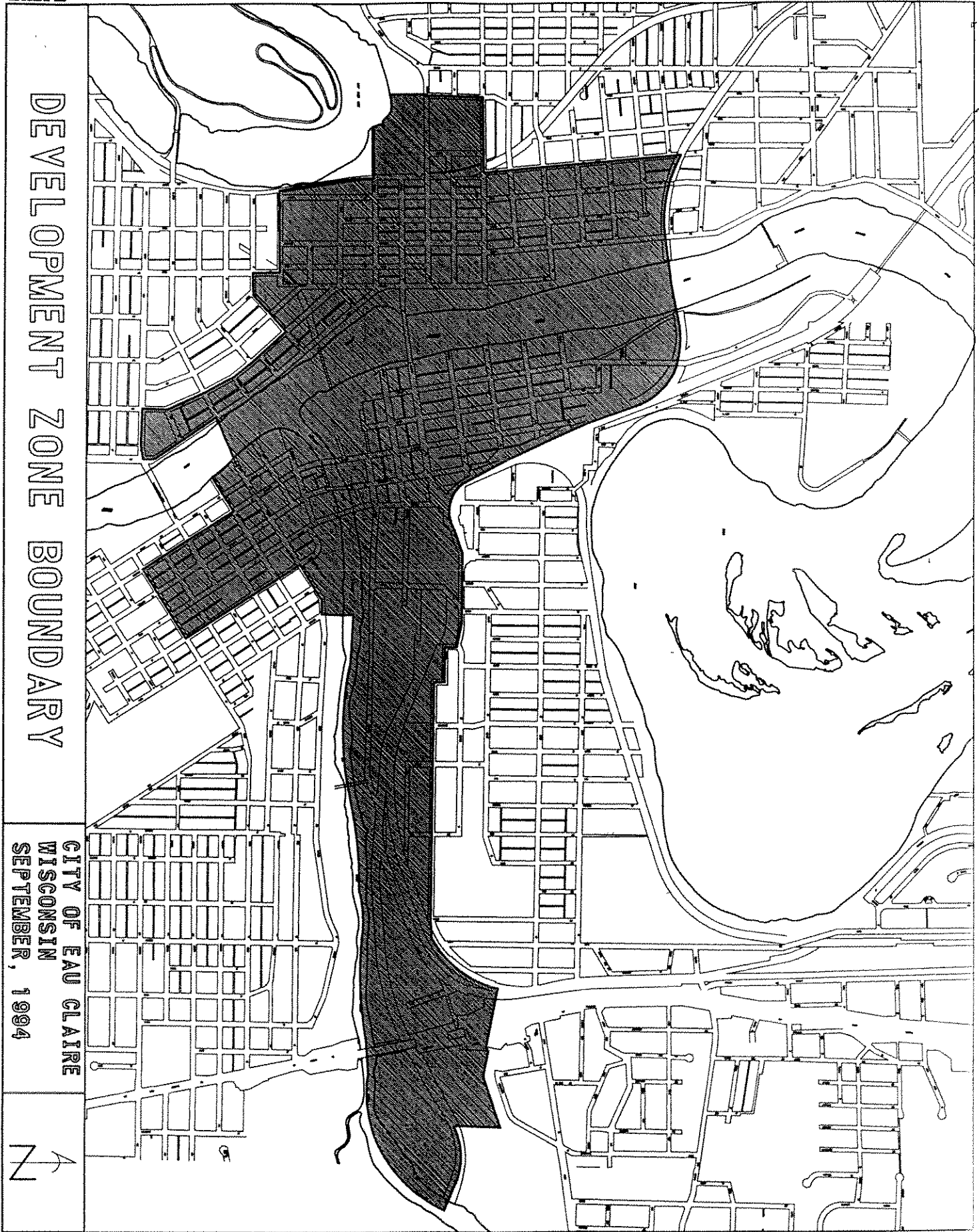
2

2



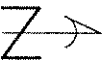
CITY OF MENOMONIE
Proposed Development Zone Areas

MAP A

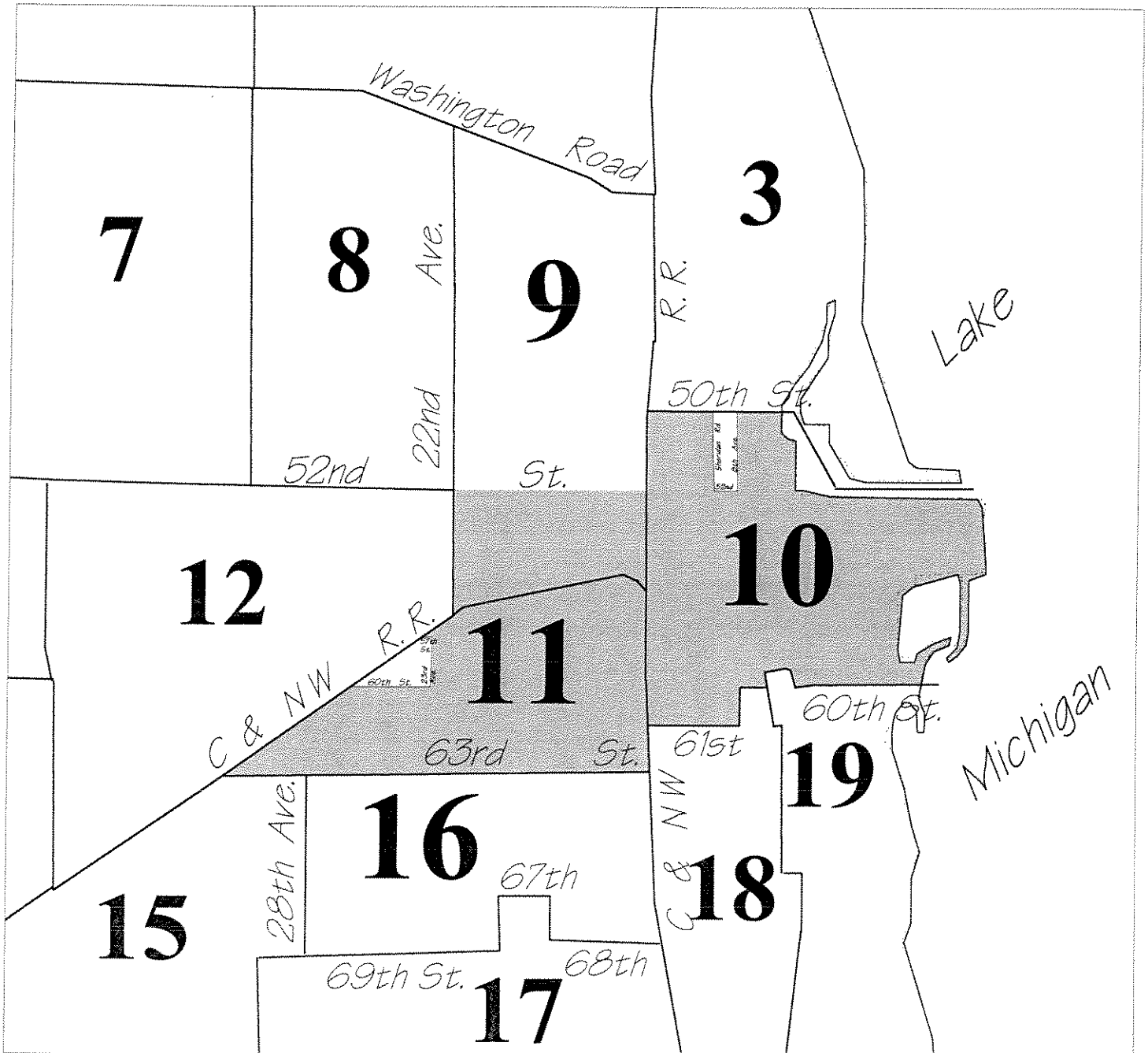


DEVELOPMENT ZONE BOUNDARY

CITY OF EAU CLAIRE
WISCONSIN
SEPTEMBER, 1994



Map A
Development Zone
Kenosha



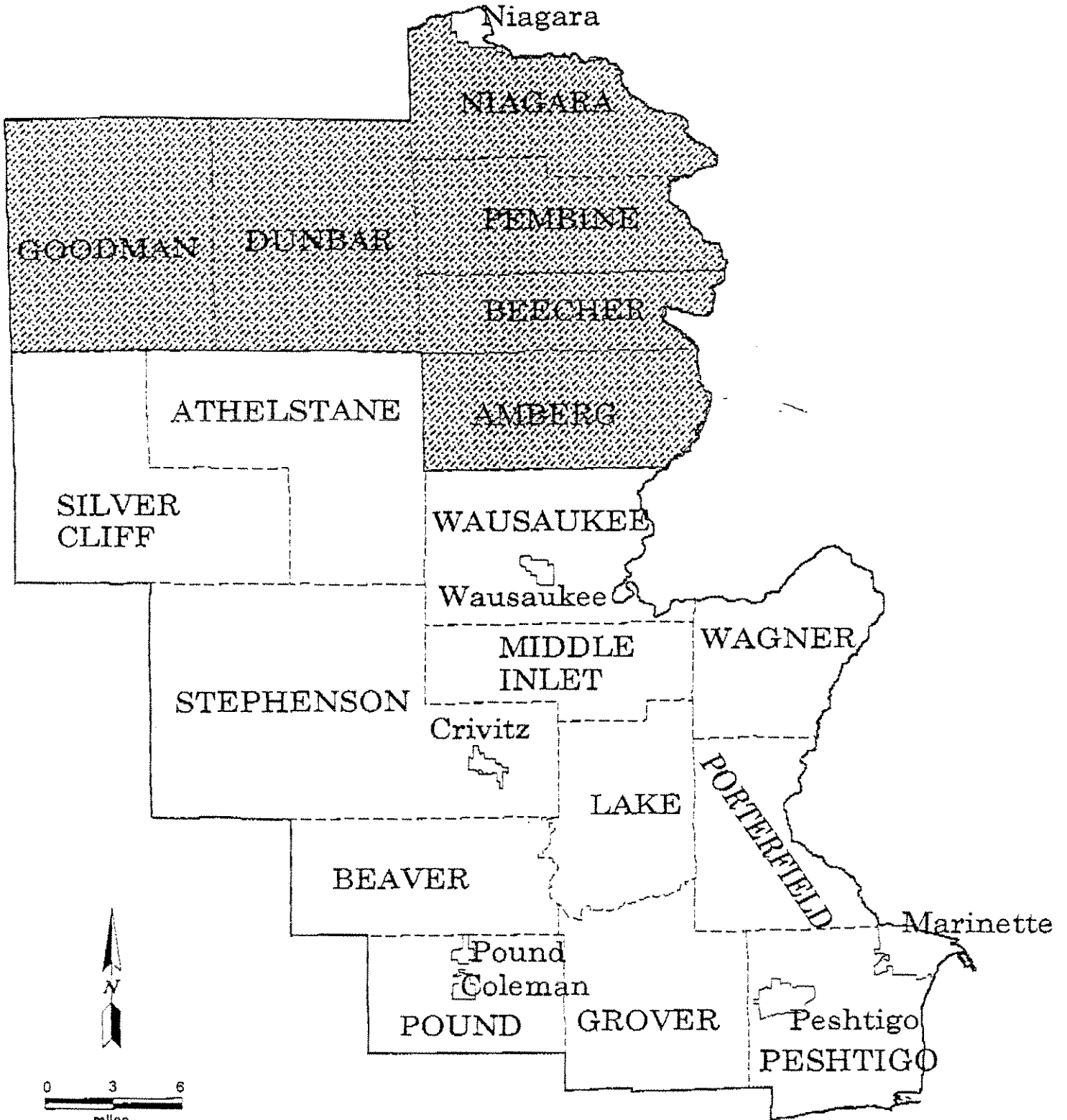
Nominated Area

NORTH



Scale: 1" = 2000'

Proposed Development Zone Marinette County



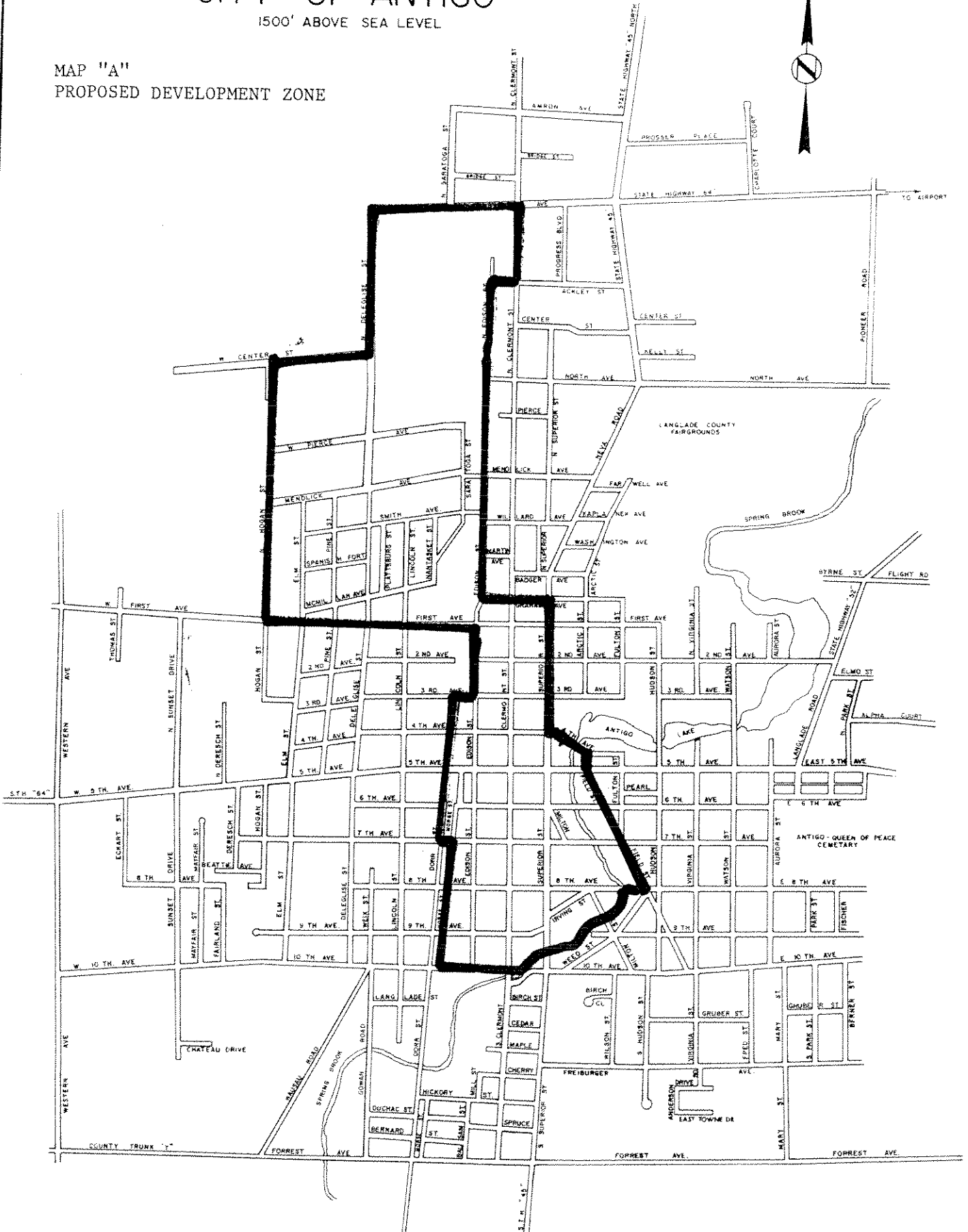


ELCHO

CITY OF ANTIGO

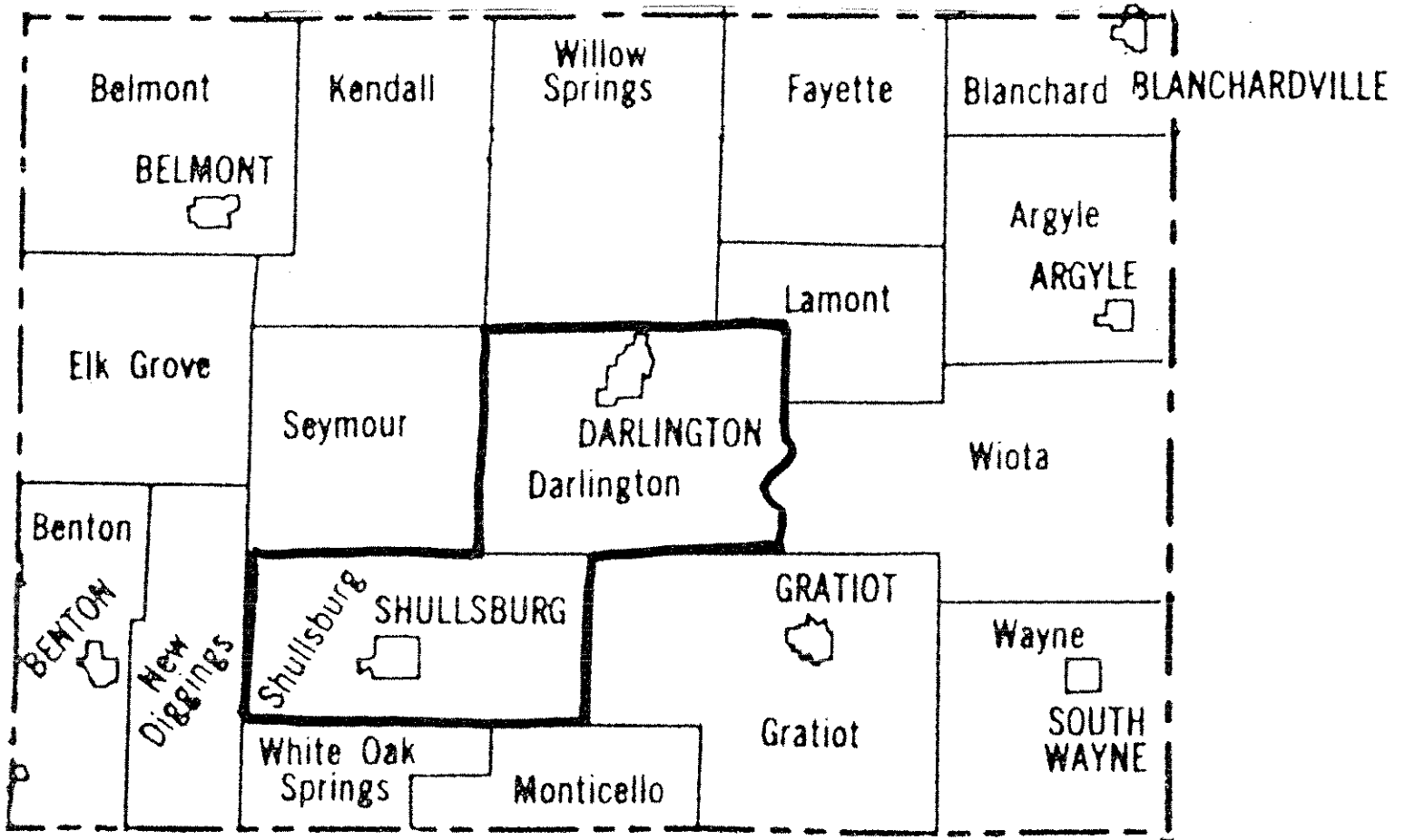
1500' ABOVE SEA LEVEL

MAP "A"
PROPOSED DEVELOPMENT ZONE



Lafayette County
Development Zone

MAP "A"





Map of Proposed Development Zone

- * Orange shaded area represents the City of Mauston
- * Yellow shaded area represents sections of Town of Lisbon, Town of Lindina, Town of Germantown, and Town of Lemonweir. Future business development is likely to occur along the major transportation corridors located in these rural areas adjacent to Mauston city limits and the Mauston - New Lisbon Union Airport (located in Town of Lisbon).

150,000'

Winfield
2,000,000'

To: Joint Committee on Finance

From: Bob Lang, Director
Legislative Fiscal Bureau

ISSUE

GPR Sum Sufficient Reestimates (Other Credits)

[LFB Summary: Page 613, #3 and #4]

CURRENT LAW

The Governor's budget provides \$1,900,000 in 1993-94 and \$2,100,000 in 1994-95 in the GPR sum sufficient appropriation for the development zones jobs tax credit. Similarly, funding amounts in the GPR sum sufficient appropriation for the development zones sales tax credit are \$170,000 in 1993-94 and \$180,000 in 1994-95.

MODIFICATIONS

Decrease GPR sum sufficient estimates for the development zones jobs tax credit by \$1,100,000 in 1993-94 and by \$1,000,000 in 1994-95. In addition, decrease the sum sufficient estimate for the development zones sales tax credit by \$120,000 in 1993-94 and by \$120,000 in 1994-95.

<u>Modification</u>	<u>GPR</u>
1993-95 FUNDING (Change to Gov)	- \$2,340,000

Explanation: A refundable tax credit is provided to employers under the state income and franchise taxes for the amount of the federal targeted jobs tax credit for qualified wages paid to employees who are members of a target group and who work for the claimant in a development zone. The credit is equal to 40% or \$2,400 of the first \$6,000 of qualified first and second year wages paid to each employee who is a member of a target group. A refundable tax credit is also provided for the amount of sales taxes paid on the purchases, leases and rentals of construction

materials and supplies and related materials used to construct, rehabilitate, repair or remodel real and depreciable tangible personal property in a development zone. Through December 22, 1992, a total of \$604,400 in jobs tax credits and \$38,400 in sales tax credits had been claimed since the beginning of the development zones program. Because of the relatively low level of participation in the program and the limited number and amount of credits which have been claimed to date, it is expected that the amount of jobs and sales tax credits claimed in the 1993-95 biennium will be less than the amount estimated when the budget was prepared. As a result, the GPR sum sufficient estimates for these credits have been decreased by \$1,220,000 in 1993-94 and by \$1,120,000 in 1994-95.

Prepared by: Ron Shanovich

To: Joint Committee on Finance

From: Bob Lang, Director
Legislative Fiscal Bureau

ISSUE

Development Zones Jobs Tax Credit (Other Credits)

[LFB Summary: Page 22, #2 and Page 613, #3]

CURRENT LAW

A refundable tax credit is provided to employers for the amount of the federal targeted jobs tax credit for qualified wages paid to employees who are members of certain target groups and who work for the claimant in a development zone. Under the federal targeted jobs tax credit, the credit is equal to forty percent of the first \$6,000 of qualified first year wages paid to each member of a target group. Qualified wages are the wages paid, or incurred, during the tax year to the target group.

The state credit may be claimed for qualified wages paid in the first two years that each employee works for the claimant. The credit can only be used to offset taxes on income attributed to or directly related to income from the claimant's business operations in the development zone. No credit can be claimed if certification for the tax credits is revoked, the development zone ceases to exist or the claimant ceases business operations in the zone.

Federal law defines eligible target groups to include:

- (a) a handicapped individual receiving vocational rehabilitation;
- (b) an individual between 18 and 22 years of age who is a member of an economically disadvantaged family;
- (c) a Vietnam veteran who is a member of an economically disadvantaged family;

- (d) an individual receiving federal Supplemental Security Income payments or state supplements;
- (e) an individual receiving state and local general assistance;
- (f) a youth between 16 and 19 years of age who is a participant in a qualified cooperative education program; and
- (g) a qualified summer youth employe.

State law expands the definition of target group to include the federal Internal Revenue Code definitions of dislocated workers. As a result, eligible target groups also include: (a) persons who have been terminated or laid off, are eligible for or have exhausted their unemployment compensation benefits and are unlikely to return to their previous industry or occupation; (b) persons who have been terminated as a result of a permanent plant closure; (c) persons who are long-term unemployed and have limited opportunities for new employment in a similar occupation in the area, including elderly who face barriers to employment because of their age; and (d) persons who were self-employed, including farmers, and are unemployed as a result of general economic conditions in their area or because of natural disasters. The definition of target groups also includes persons who are unemployed as a result of plant closings or mass layoffs that are subject to the state plant closing law.

In addition to being members of a target group, the employes must either be employed for at least 90 days or complete 120 hours of service.

Federal law requires local agencies designated jointly by the Secretaries of the Treasury and Labor to issue a certificate to each individual who qualifies as a member of one of the target groups or as a member of an economically disadvantaged family. A certificate issued by a designated local agency (in Wisconsin, the local Job Service office) is proof of qualification and relieves the employer of furnishing such proof to the Internal Revenue Service (IRS). Under Wisconsin law, a member of a target group can also be certified by the Job Training Partnership Act organization in the development zone and, in certain cases, the Wisconsin Department of Development (DOD).

It is estimated that the total amount of targeted jobs tax credits claimed will be \$500,000 in 1992-93, \$800,000 in 1993-94 and \$1,100,000 in 1994-95.

GOVERNOR

The Governor recommends creating a development zones credit against income and franchise taxes due, equal to 10% of the wages earned by each employe in the first year of employment, up to a maximum of \$600. To be eligible, the employe would have to be determined to be a resident of the development zone by the Department of Development;

however, the individual would not have to be a member of a target group as defined for purposes of the existing development zones jobs tax credit. The proposed credit could be claimed along with the current jobs tax credit for the first year wages of the same employe if the employe was a member of a target group. The credit would be refundable for amounts in excess of tax liability and would first apply to tax years beginning on or after January 1, 1993.

DISCUSSION POINTS

1. Five different tax credits are available to businesses that locate or expand operations in a development zone:

Jobs Tax Credit. Eligible businesses may claim a refundable credit of up to \$2,400 for each targeted employe that is hired.

Investment Credit. Eligible business may claim a credit against income or franchise taxes due of 2.5% of the purchase price of depreciable tangible personal property placed in service in the development zone.

Location Credit. Eligible businesses may claim a tax credit equal to 2.5% of the amount expended on certified projects to acquire, construct, rehabilitate, remodel, repair and place in service real property in a development zone.

Sales Tax Credit. Eligible businesses may claim a refundable tax credit for the amount of sales taxes paid on purchases, leases and rental of construction materials and supplies and related materials used to construct, rehabilitate, repair or remodel real and investment credit property in a development zone.

Research Credit. Eligible businesses may claim a credit of 5% of specified research expenses incurred in a development zone.

2. The total amount of development zones tax credits that can be claimed by all businesses in the 12 development zones over the life of the statewide program is set at \$18.155 million. The Department of Development allocates a portion of the total statewide credit amount to each development zone based on population, with a minimum allocation of \$750,000 for the smallest zones. The Department then assigns credits to certified businesses within each zone based on plans submitted by the businesses and recommendations by local officials. Current law requires that at least 50% (65% in Milwaukee) of the total credit amounts allocated to each zone be used for jobs tax credits.

3. As of June 1, 1993, a total of \$9.4 million in tax credits had been assigned to 128 individual businesses within the 12 state development zones. Of this total, \$6.9 million was for jobs tax credits.

4. In February, 1993, the Legislative Audit Bureau (LAB) issued a required evaluation of the state development zones program. The evaluation included measures of program participation that were related to use of the tax credits and, in particular, the jobs tax credit. The Bureau's findings were as follows:

- Through December 22, 1992, 114 or 2.4% of an estimated 4,700 businesses located in development zones had been certified for tax credits. A total of \$8.4 million in credits or 46% of the total statewide credit authorization had been assigned to these businesses. (As noted, through May, 1993, the number of business certifications was 128 or 2.7% of the total estimated businesses located in the zones. The amount of credits assigned to these businesses was \$9.4 million or 52% of the statewide credit authorization.)

- As of December 22, 1992, business tax returns for tax years 1990 and 1991 included claims for \$863,883 in development zones tax credits. An additional \$298,792 in tax credits had been verified. The amount claimed was 10% of the \$8.4 million which was allocated to businesses statewide and 4.8% of the total statewide credit authorization. Businesses in five of the 12 zones filed tax returns claiming credits.

- Approximately \$6.2 million or 73% of credits that were assigned to businesses through December 22, 1992, were for the jobs tax credit. (Through May, 1993, about \$6.9 million or 73% of the total amount of credits allocated to businesses were for the jobs tax credit.) Of the total amount of credits claimed, \$604,388, or 70% were for jobs tax credits. Credits were claimed by 19 of 29 businesses which had claimed development zone credits. The jobs tax credits were claimed for the employment of 671 individuals. Another 347 hirings of target group members had been certified. Seventy-nine percent of the individuals hired received starting wages of \$6 or less per hour.

- In some cases, tax credits were assigned to businesses and the development activities were not progressing as planned. In other cases, wages paid to new hires were considerably less than in the business plans submitted for certification.

5. The LAB indicated that the limited program activity in terms of the number of participating businesses, amount of investment and amount of tax credits claimed and the discrepancies between the wages reported in certification plans and the actual wages paid raises questions about the ultimate success of the program. The LAB also noted that it would be increasingly important for DOD to identify nonperforming businesses in order to make unused credits available to other businesses.

6. The relatively small number and amount of development zones tax credits that have actually been claimed raises questions about the need for and desirability of providing another development zones tax credit. Historically, participation in employment subsidy programs, such as the federal targeted jobs and work incentive tax credits, has been relatively low. The state targeted jobs tax credit, which is substantially higher than the proposed jobs credit, has been used by only 19 out of an estimated 4,700 businesses located in the development

zones. In addition, studies have shown that categorizing individuals as economically disadvantaged can cause potential employers to view them as poor prospects for hiring and training. To the extent this is true, the proposed jobs tax credit could create an incentive for businesses to substitute development zone residents for target group members rather than increasing the overall level of employment in the zone. Since the proposed credit is based on a maximum of \$6,000 in wages and is available only for the first year of employment, it would not provide an incentive for hiring individuals to high wage permanent positions. Rather, there could be an incentive for businesses to hire individuals to positions with low wages and high turnover rates.

7. From another view, the level of development zone activities, as reflected in the amount and number of tax credits claimed, is understandable. Generally, economic development programs progress slowly in the early years. It takes time to fully publicize the program, construct or expand business facilities and hire new employees and these activities affect the number and amount of tax credits that are claimed. Because tax credit claims are first received when businesses file their income tax returns, they may lag actual investment in a zone by a year or more, particularly if businesses carry the credits forward to offset future tax liabilities. Moreover, according to DOD, as of June 30, 1992, the 96 businesses that participated in the program had: (a) created 1,765 new jobs; (b) hired 867 target group workers; and (c) invested \$28.7 million in their projects. DOD also indicated that it will fully implement the LAB audit recommendations, including establishing an evaluation process through which unused tax credits can be reallocated.

8. By lowering the price of labor relative to other inputs, such as machines, to the production process of an individual firm, the proposed jobs tax credit provides an incentive for businesses to substitute labor for these other inputs by hiring more workers. The reduced cost of labor can reduce the cost of the goods produced by the business. To the extent the lower costs are passed on to consumers, demand for the firm's products may increase. In turn, the increased demand may cause the business to expand output and hire new employees. Because the credit would subsidize a significant proportion of a low wage, it creates an incentive to hire individuals in these positions.

9. The Administration estimated that the proposed jobs tax credit would have a minimal fiscal effect. Based on utilization of the current targeted jobs tax credit, it is estimated that the proposal would cost \$100,000 GPR annually.

ALTERNATIVES

1. Approve the Governor's recommendation to create a refundable development zones credit against income and franchise taxes due equal to 10% of the wages earned in the first year of employment, up to a maximum of \$600, for each employee who is determined by the Department of Development to be a resident of the development zone in which he or she is employed. Make the credit first applicable to tax years beginning on or after January 1, 1993.

Authorize the credit under both the individual and corporate income and franchise taxes. The credit would cost an estimated \$100,000 GPR annually.

<u>Alternative 1</u>	<u>GPR</u>
1993-95 FUNDING (Change to Gov)	\$200,000

2. Delete the Governor's recommendation.

Prepared by: Ron Shanovich

To: Joint Committee on Finance
From: Bob Lang, Director
Legislative Fiscal Bureau

ISSUE

Development Zones Program Expansion (Other Credits)

[LFB Summary: Page 153, #19 and Page 613, #3 and #4]

CURRENT LAW

Wisconsin has established 12 development zones in areas which have been designated as economically distressed in certain municipalities and Indian Reservations in the state. The 12 zones are located in the cities of Beloit, Fond du Lac, Green Bay, Manitowoc, Milwaukee, Racine, Richland Center, Sturgeon Bay and Superior, Iron County and the Lac du Flambeau and Stockbridge-Munsee Indian Reservations. The state provides five different tax credits to businesses which locate or invest in a development zone--jobs credit, sales tax credit, investment credit, location credit and research credit. A total of \$18.155 million is allocated for tax credits over the life of the statewide program.

GOVERNOR

The Governor recommends increasing the total number of development zones which may be designated by the Department of Development by two to a total of 14. Also, the total amount of tax credits that could be allocated would be increased by \$3,000,000 to a statewide program total of \$21,155,000. It is estimated that these provisions would have no fiscal effect in the 1993-95 biennium.

DISCUSSION POINTS

Additional Zones

1. The state development zones program is designed to promote economic growth and development through job creation and investment in economically distressed areas. Designation criteria target areas with high unemployment, low incomes and decreasing property values. The tax credits provide incentives for businesses to locate or expand in these areas.

2. The state development zones program was established by 1987 Wisconsin Act 328. Under the provisions of Act 328, the Department of Development was given authority to designate eight development zones throughout the state and a total of \$14.0 million in GPR was authorized to fund tax credits over the life of the program. The program limits the life of a zone to seven years; however, three 12 month extensions can be granted. The first eight zones were designated in September, 1989. In 1990, the development zones program was expanded to allow for the designation of four additional zones and an additional \$4.155 million in total tax credits.

3. In 1989, 19 different communities submitted applications for development zone eligibility and, subsequently, development zone plans to DOD for consideration. In 1991, nine communities submitted eligibility applications and eight of these communities submitted plans to DOD. Five of the eight communities that submitted plans in 1991 had unsuccessfully competed for designation in 1989. Since the last expansion of the program in 1991, a number of communities have expressed interest in participating in the development zones program.

4. DOD administrative rules require that the communities selected for development zones be distributed as evenly as possible throughout the state. A development zone has not been designated in a community in the west central section of the state.

5. In February, 1993, the Legislative Audit Bureau (LAB) issued an evaluation of the state development zones program. The evaluation included measures of program participation and a review of DOD program management activities. The Bureau's findings included:

- Through December 22, 1992, 114 or 2.4% of an estimated 4,700 businesses located in development zones had been certified for tax credits. A total of \$8.4 million in credits or 46% of the total statewide credit authorization had been assigned to these businesses. (Through May 1993, the number of business certifications was 128 or 2.7% of the total estimated businesses located in the zones. The amount of credits assigned to these businesses was \$9.4 million or 52% of the statewide credit authorization.)

- As of December 22, 1992, business tax returns for tax years 1990 and 1991 included claims for \$863,883 in development zones tax credits. An additional \$298,792 in tax credits had been verified. The amount claimed was approximately 10% of the \$8.4 million which had been allocated to businesses and 4.8% of the total statewide credit authorization. Businesses in five of the 12 zones filed tax returns claiming credits.

- In some cases, tax credits were assigned to businesses and the development activities were not progressing as planned.

- Overall, DOD complied with statutory requirements in providing administrative accountability for the development zone program. However, it was recommended that, to improve the likelihood that the development zones program will meet its goals of increased investment in the zones, DOD should expand its efforts in program management. The Department should also increase its efforts to determine if individual zones and businesses are meeting their plans.

6. The relatively low level of participation in the development zones program indicated by the LAB evaluation calls into question the advisability of expanding the number of zones. Based on the LAB findings, it is not clear that designating two new development zones will lead to a substantial increase in investment and employment in those municipalities. Moreover, the Department's program management responsibilities would increase, making it more difficult for DOD to increase its efforts to monitor the activities in the existing zones. Also, the investment incentive provided by specific development zones credits is, in part, due to their limited availability. Only investment in very limited areas is eligible for the credits. Expanding the areas for eligible investment reduces the attractiveness of the credits.

7. However, from another view, the development zones program is generally performing at an acceptable level. Because of the time needed to fully publicize the program, construct or expand business facilities and hire and train new employees, measuring program performance in terms of tax credits claimed will understate the level of business activity that will be generated when these activities are complete. Moreover, DOD indicates that since June 30, 1990: (a) the number of jobs created has increased 42%; (b) the number of hires from target groups has increased 107%; (c) private investment has increased 123%; (d) the number of certified businesses has increased 92%; and (e) the number of credits has increased 46.4%.

8. DOD has indicated that, in response to LAB recommendations, it will expand its monitoring, assessment and management activities. The Department is conducting on-site evaluations on the status of business projects in each zone. Businesses are being evaluated in terms investment and jobs created compared to project goals. The evaluations for all 12 zones are expected to be completed by October 1, 1993. Thereafter, site visits will continue on an annual basis. In addition, the Department has developed a policy for credit reallocation and will survey businesses to assess the impact of and identify barriers to program participation. The development zone database information system will be consolidated.

9. Since comprehensive site evaluations will be first completed on October 1, it could be argued that program expansion should be delayed. If the Department finds that program performance warrants additional development zones, separate legislation could be introduced to expand the program.

Increasing Total Credit Allocation

1. The total amount of development zones tax credits that can be claimed by all businesses in the 12 development zones over the life of the statewide program is set at \$18.155 million. DOD allocates a portion of the statewide credit amount to each development zone based on population, with a minimum allocation of \$750,000. The Department then assigns credits to certified businesses within each zone based on plans submitted by the businesses and recommendations by local officials. The Department is authorized to reduce credit allocations in cases where businesses fail to meet certification requirements and where the information used to determine the allocation was inaccurate or significantly misestimated. Under the Department's administrative rules, business credit amounts that are reduced must remain allocated to the development zone in which the business is located.

2. Through May, 1993, a total of \$9.4 million in development zones tax credits or 52% of the total statewide credit authorization had been allocated to 128 businesses. As a result, \$8.7 million or 48% of the total statewide allocation had not been assigned to specific businesses.

3. Through December 22, 1992, the total amount of development zone credits claimed by businesses for tax years 1991 and tax years 1992 was \$863,883 or 4.8% of the total statewide credit authorization. Twenty-nine businesses in five of the 12 development zones claimed the credit.

4. In its audit, the LAB found several cases where tax credits were assigned and the development activity was not progressing as planned. The LAB recommended that DOD identify nonperforming businesses in order to make unused credit amounts available to other businesses.

5. Although economic development programs initially tend to progress slowly, three years of the seven-year limit have been completed in eight of the state's 12 development zones. During this period, the number of businesses which have claimed development zones tax credits and the amount of credits actually claimed has been limited. Given the relatively low level of participation in the development zones program thus far, the Committee may wish to direct DOD to reallocate unused credits to businesses in the new development zones. DOD also has a reserve of \$1,143,216 in unallocated credit amounts. Part or all of this amount could be allocated to the new zones.

6. The additional \$3,000,000 in tax credits is recommended for allocation to the two new development zones based on the expected populations of those zones. DOD staff indicate that one zone is expected to be in an urban area and one zone will be in a rural area.

7. The areas designated as development zones are selected by DOD through a competitive process. The area must meet certain eligibility criteria, such as low household incomes, designed to measure economic distress. Detailed development plans are then submitted to DOD, which ranks the plans using criteria such as the expanded employment opportunities that

will be created for the target population. This process is believed to ensure that areas with the most comprehensive development plans will be designated and receive credit allocations.

8. To be certified as eligible for tax benefits, businesses must submit information to DOD, which identifies the specific activities that will be undertaken to qualify for the tax credits. The information must generally demonstrate that the proposed business activities will stimulate economic development and create jobs in the zone. The number of jobs created, retained or upgraded and the amount and type of investment to be made in the development zone must be identified. It is argued that this certification process ensures that tax credits are assigned to business projects that will successfully attain their objectives.

9. In response to the LAB audit, DOD is conducting an on-site evaluation of each development zone. The Department indicates that, based on its reviews, there are only a few cases where business activities are not progressing as expected. In addition, a number of communities have requested additional allocations of tax credit amounts from the Department's reserve allocation. These communities have identified additional business activities that would be encouraged by additional tax credits.

ALTERNATIVES

Additional Zones

1. Approve the Governor's recommendation to increase the number of development zones that may be designated by DOD by two to two total of 14. This provision would have a minimal fiscal effect in the 1993-95 biennium.
2. Delete the Governor's recommendation.

Increase Total Credit Allocation

1. Approve the Governor's recommendation to increase the total amount of tax credits that may be allocated by \$3,000,000 to \$21,155,000. This provision would have a minimal fiscal effect in the 1993-95 biennium.
2. Delete the Governor's recommendation.

Prepared by: Ron Shanovich