Introduction

Wayne R. Wendling

W.E. Upjohn Institute
I. Introduction

Local public school districts rely on property tax revenues to finance their operations even more than cities and counties do. Any action that other governmental units take that affects either the size of the tax base or the flow of revenues from it, is likely to affect the financing of local elementary and secondary education. Whether an action damages the local education financing structure is not inevitable, however. For instance, it is frequently asserted, though the empirical results are inconclusive, that the need for municipalities to provide a broad range of noneducation public services may crowd out education spending, the municipal overburden problem. At issue here is whether two tax programs that local communities in the state of Michigan have used to generate increased local economic activity have adversely affected the local financing of public elementary and secondary education.¹

Both tax programs are designed to facilitate the ability of Michigan communities to compete with communities in other states for industrial and commercial developments. The Plant Rehabilitation and Industrial Development Districts Law of 1974 (PA-198) empowers local government units to establish plant rehabilitation and industrial development districts and with state approval issue certificates which exempt replacement facilities or new facilities from the general property tax for up to a 12-year period and instead subject it to an industrial facilities tax. For replacement (restored, rehabilitated) facilities the industrial facilities tax

¹. The Institute currently is involved in a conceptual study of local tax programs, their effectiveness at generating growth of the tax base, community investment goals and the indirect benefits and costs on industrial and commercial developments. A number of issues that logically could be raised here are dealt with in that study in order to limit the length of this discussion.
is imposed at the same rate as the property tax, but is applied to the state equalized value of the obsolete facility in the tax year preceding the certificate. For new facilities the industrial facilities tax is calculated by applying one-half of the local property tax to the state equalized value of the new facility. Act 255 of the Public Acts of 1978 expanded the creation of rehabilitation and development districts and the issuance of tax exemption certificates to include commercial property.

The potential impact of tax abatements on the financing of local public education in the state of Michigan was recognized in the framing of PA-198. It is stated that the city, county, township or village “shall set forth a finding and determination that the granting of the industrial facilities exemption certificate . . . shall not have the effect of substantially impeding the operation of the local governmental unit or impairing the financial soundness of a taxing unit” (Section 207.559 Compiled Laws of Michigan). Since school districts are the prime competitors for the property tax dollar, conflicts have surfaced in some instances between the district and the unit of government utilizing the tax programs contending that the district’s ability to raise sufficient revenues is being damaged by the granting of abatements.

This article is organized in the following order. Section II is a discussion of the efficacy of tax abatements and alternative operational definitions of “impairment.” Also introduced are the concepts of inherent production technology and fiscal capacity. Both the most recent and the current state of Michigan operating aid for education formulae are presented in Section III. Both are analyzed because the implications of each are different and, as a result, school districts that may have contended that their ability to finance education was being damaged may now view abatements as less harmful. The converse also may hold. The implications of each formula are demonstrated using hypothetical
districts. The specific situation for the nine school districts in Kalamazoo County is analyzed in Section IV. Additional considerations, including the issue of equity, are raised in Section V and the conclusions are presented in the final section.

The focus of the paper is narrow. It concentrates on tax abatements, operating aid formulae, spending levels and changes in state equalized value (SEV). Factors that may be related to the question of impairment, but are not addressed, include (a) the other state funding formulae for schools and (b) other tax issues such as Headlee. Furthermore, only scant attention is paid to the potential service pressures on school districts resulting from new industrial and commercial developments, and declining enrollments.