

CENTER *for* RURAL POLICY and DEVELOPMENT

Seeking Solutions for Greater Minnesota's Future

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On the Books: Existing Tax Abatement Program is Often Over Looked

Can tax-free zones help rural Minnesota? This economic development tool is getting a lot of attention at the Legislature and around the state. The Job Opportunity Building Zone program is a top priority for Gov. Tim Pawlenty and is the subject of much interest in the House and Senate.

But while the JOBZ bill is being considered in the Legislature, there is already at least one economic development program on the books that uses tax abatement zones to help maintain and improve the economies of rural Minnesota communities.

The current tax abatement program allows a local government to abate property taxes on a parcel of land by resolution. The business(es) receiving the abatement must create public benefits such as job creation, enhancing the tax base, or redeveloping blighted areas. The abatement can be for all or a portion of the property taxes for up to ten years (the term can be extended to 20 years for certain "qualifying businesses" such as manufacturing, mining and high-tech industries), and not all of the local entities governing that parcel need to participate. Governments can put the tax dollars toward public infrastructure projects in the abatement zone, rather than return the money to the business. The local government can bond to make up the difference as long as the bonding proceeds go for certain expenses.

Compared to other types of subsidies to businesses, few dollars are being funneled through this existing program. According to the Department of Trade and Economic Development, from 1999 to 2001, 23 tax abatement districts were created, totaling \$5.7 million, out of a total of nearly \$700 million in business subsidies for those three years (only cities over 2,500 are required to report business subsidies). Tax increment financing and loans were the most commonly used. From 1999 to 2001, 134 tax increment financing districts were issued totaling \$141.0 million, while 138 loans totaling \$35.2 million were granted.

According to Faribault County's economic development consultant Jack Quinlan, the tax abatement program isn't used much in his county simply because most of the businesses they offer assistance to are startups, small entrepreneurial companies without much tax consequence to think about. These firms are much more concerned about financing, Quinlan said.

Tax-free zones policy brief

The Center recently completed a new policy brief analyzing and comparing tax-free zones proposals in the Minnesota House and Senate. The brief also takes a look at similar existing programs in Michigan and Pennsylvania.

For more information on "Understanding Job Opportunity Building Zones," see page 3.

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Coming soon Atlas of Minnesota, 2nd Edition

The second edition of the Atlas of Minnesota is scheduled for publication this May. First published in 2000, the Atlas is a survey of the social and economic characteristics of the state and its counties. The second edition of the Atlas will display approximately 150 maps covering 11 topics, from the demographics of the state to health care, crime and education. The Atlas will be accompanied this time by a CD containing PDFs of Atlas pages and also an interactive mapping software that will allow users to create their own maps using data from the Atlas.

The Atlas is a joint project of the Center for Rural Policy and Development, the University of Minnesota Extension Service and the Blandin Foundation. Check our web site at www.ruralmn.org to find out when it will be available and how to order.



Rural Perspectives

By Tom Renier, President
Northland Foundation, Duluth



Q *What, in your opinion, are the most pressing issues in Northeast Minnesota right now, in economic and human terms?*

A Well, of course, there are those things that have been making the headlines for the past few years. Plant closings in the mining industry and major layoffs and turbulence in the wood products and paper industries are obviously pressing issues in Northeast Minnesota. These industries represent a large portion of our regional economy.

There are also a number of small to medium-sized businesses, which either are, or have the potential to be, very stable and successful in a normal economic environment, that are really struggling to survive this prolonged economic downturn.

Although we seem to have stabilized our overall population loss, we continue to lose our young people to the Twin Cities and other areas where job opportunities are relatively abundant. Our schools have shrinking enrollments, causing major budget problems and prompting conversations that have traditionally been taboo, such as school district consolidations. Our population continues to age at a faster pace than the rest of the state and the nation. This means the issues of health care, long-term care, and housing are perhaps more pressing than in other areas, urban and rural.

Whether you feel that the Governor's budget balancing proposals are fair and equitable or not, the impacts of Local Government Aids (LGA) cuts, elimination of programs in early childhood and after-school programs, programs that help keep seniors independent, and cuts in higher education, all bode serious negative impacts in this region, as they do for many rural communities.

Q *How does the economy of Northeast Minnesota differ from other parts of the state? What are some of the primary forces – positive and negative – affecting Northeast Minnesota's economy?*

A Regardless of our efforts over a generation to reduce the dependence on a few major industries, mining and wood products still represent a disproportionate share of our gross regional product. The reliance in Northeast Minnesota on natural resource-based industries is compounded by the fact that most of those have absentee ownership, presenting challenges for real partnerships with our largest employers. Although we have some very real success stories in replacing lost mining and paper industry jobs, the largest number of job vacancies that currently exist are around \$6 an hour.

Northeast Minnesota clearly is not diversified enough. But simply talking about diversification isn't enough either. We need to focus our efforts on developing solid businesses that create family-sustaining jobs. We need to support and grow businesses that can flourish in a rural environment; businesses that aren't necessarily subject to the old economic barriers, such as transportation, distance to markets, etc. Surely diversification is a goal, but the quality of the development that comprises diversification is really the critical success factor.

On the positive side, there are currently a number of efforts to use technology to our advantage, which will level the playing field for better paying information technology jobs. On the Iron Range and in Duluth, some exciting prospects are taking shape in the technology and software development arenas. Sectors such as health care and aviation are moving into prominent roles in the business community.

Q *Please tell us about the initiatives the Northland Foundation is taking in business development and business assistance in the area.*

A The economic development thrust of the Northland Foundation has always been business finance. The Foundation has tried over the years to adapt and expand our financing tools to reflect the needs of the business community in Northeast Minnesota. In

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Tax Abatement Program ...

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Tax abatement is used somewhat: it has its advantages and disadvantages, said Jim O'Meara, an attorney for Briggs & Morgan in St. Paul who assists cities with economic matters. While it's much more flexible than tax increment financing, it also doesn't bring in as many dollars and people aren't as familiar with it. The tax abatement program, though, has proven very useful in helping cities fund public infrastructure projects in areas that wouldn't otherwise meet the narrow qualifications for tax increment financing, O'Meara said. In some ways this abatement program is similar to the proposed JOB Zones program: it focuses on rural Minnesota, especially distressed areas; the zone must be justified, generally with at least an explanation of how the zone will benefit the area; and it lasts for multiple years.

On the other hand, the existing program only abates property taxes. The proposed JOBZ bill casts a much wider net, abating property taxes, corporate income taxes, individual income tax derived from investing in or operating a business in a zone, motor vehicle sales taxes and sales tax.

Another, perhaps more significant difference, however, is that the current tax abatement program functions on a much smaller scale: county and municipal governments and school districts can all participate, but the program is not designed to operate across county lines or even across municipal boundaries. Geographically, these zones look more like tax-increment financing districts.

The proposed JOBZ program, on the other hand, can be applied on a regional basis, involving several counties. A program encouraging large-scale thinking may give local economic developers new options to consider. Some local officials are already discussing how to assemble their counties into tax-free zones while the program is still working its way through the Legislature.

Ethnic Diversity Conference this Summer

The date and time has been set for the Center for Rural Policy and Development's conference on ethnic diversity. The conference will take place Aug. 7 in St. Cloud at the Holiday Inn. The Center has partnered with the League of Minnesota Cities to examine communities and school districts around the state that have experienced a large change in the ethnic makeup of their populations and see what they are doing to address the changes in their communities. The results of that research will be a "tool kit" of best practices for rural communities. It will be an opportunity for community leaders to learn and discuss how to meet the changing needs of their cities and regions.

Please watch for further information on the conference and how to register.

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Rural Perspectives...

recent years, our average size loan, as well as our overall loan volume, has increased dramatically. We've been relied upon by our long-term partners, such as IRRRB and Minnesota Power, to play a far more significant role, particularly in larger deals, than in the previous decade. Two million in loans used to be a huge year for us. By contrast, we will most likely do \$6 million in loans this year.

We have also created some innovative financing techniques to accommodate the changing needs of business. Most notable is our Royalty Fund, which provides greater flexibility than typical business finance programs. This benefits start-ups and other businesses that are highly leveraged, or have cash flow issues, which cannot be addressed through traditional sources. It's clear that even more creativity in business finance is going to be necessary if this region, and all of rural Minnesota, is going to compete in the information age through growth of technology-related companies.

I would be remiss if I didn't mention the recently announced Early Childhood Initiative, in which the six Initiative Foundations are partnering with The McKnight Foundation and the Ready 4K organization. I know we're talking about economic development here, but that's exactly how investing in our youngest children is viewed by many people, including myself. The Federal Reserve Bank of Minneapolis recently released a study concluding that early childhood programs offer a significant economic return on investment. The investment we make in our youngest citizens affects the future vitality of our communities, as much as anything else we've talked about.

Q What are one or two things the state could do immediately that would have a positive impact on the Northeast Minnesota economy?

A The first thing I would ask is that the Governor make a very thoughtful appointment for Commissioner of the Iron Range Resources and Rehabilitation Board (IRRRB). Amidst all the rumors of dismantling, merging, or otherwise gutting the agency, I would hope that a Commissioner be chosen that can really lead the efforts of this unique resource. Despite its decreased revenues, the IRRRB as an economic development entity has a significant role to play, if those resources are focused and strategically invested. Although the Taconite Tax Relief Area is only a portion of the region, an IRRRB Commissioner with vision,

strategic thinking, and diplomacy will be viewed as a leader throughout Northeast Minnesota.

Secondly, I hope the administration takes note of the efforts currently under way to develop a comprehensive rural economic development strategy, led primarily by the Blandin and McKnight Foundations. This is an attempt to identify development opportunities that can effectively leverage current assets in greater Minnesota. A statewide strategy will be the compilation of six regional analyses, plus an industry sector analysis that cuts across geographic boundaries. Engagement of the administration and the legislature in this process would dramatically increase the potential of this effort to produce real impact. Economic development should amount to more than legislating a few unrelated programs. Although politically difficult to do, the administration should take a broad-based statewide approach, making targeted investments in regionally based strategies that capitalize on the strengths of the distinct sub-economies of rural Minnesota.

Q Where do you see northeast Minnesota in three to five years, economically and socially?

A I'd like to see the barriers broken down between traditional adversaries, particularly the Range and Duluth. Northeast Minnesota has lost a lot of political power in recent years, but that can be compensated for if we work together. Current efforts to engage the private sector in economic development, in leadership roles where appropriate, could be the key here.

I would hope that the current efforts in IT development would have begun to pay real benefits with a variety of businesses and sustainable jobs. This can only be accomplished if we continue adequate investment in higher education for workforce development. I would also hope that the industries I mentioned before, such as health care and aviation, not only continue to flourish, but give rise to many ancillary and support businesses.

Finally, I would hope that Northeast Minnesota will have played a significant role in the Early Childhood Initiative that I mentioned earlier, and that in three to five years the issue has landed dead center in the consciousness of the public, the business community, and policy makers. We cannot continue to believe that we can accomplish great things in Minnesota unless and until we make the investments in our youngest citizens that will produce healthy, educated, and contributing adults, who give back to our communities and our state many times over.

Notes

Day at the Capitol

As it does every year, the Center for Rural Policy and Development held its February board meeting at the State Capitol in St. Paul. Besides conducting regular business, the Center's board members joined the board of Minnesota Rural Partners to discuss shared interests and goals for rural Minnesota.

During the day, the Center and Rural Partners boards met with a number of senators and representatives from around the state to talk about issues, voice concerns and hear their positions on important topics. Legislators included Senate Majority Leader John Hottinger, Senate Minority Leader Dick Day, Sens. Cal Larson, LeRoy Stumpf, and Jim Vickerman, and Reps. Elaine Harder, Bernie Lieder, Al Juhnke, and Tony Cornish.

2003 Small Grants Recipients Named

The Center for Rural Policy and Development is pleased to announce the recipients of its 2003 Small Grants Program:

- Monica Manning, The Nova Group, St. Paul, "Policy Initiatives Strengthening Rural Colleges and Communities"
- Mark Muller, Institute for Agriculture and Trade Policy, Minneapolis, "Fostering Economic Development Through Diversified Agriculture"
- Greg Schrock, Minnesota Technology, Inc., "How Do Twin Cities Firms View Greater Minnesota?"

The Center's Small Grants program is an important means of generating objective, original research on rural issues. Each year the Center solicits proposals from researchers around the state to develop projects on rural policy issues.

The smaller grant size (under \$10,000) allows the Center to fund a number of projects, leading to greater variety. This year, for the first time, the Center chose to offer applicants special topics in an effort to focus research in particular areas.

For several years now, the Center for Rural Policy and Development has been an advocate of small rural schools. And why not? Rural schools work, and they work well. In fact, on most measures of success such as graduation rates, parental involvement and achievement test scores, small rural schools consistently confirm their value.

However, others argue that due to their small enrollments, many rural school districts simply cannot achieve the necessary critical mass and subsequent economies of scale to reach fiscal efficiency; that the most rational solution to this dilemma is for small school districts to consolidate with neighboring districts, thereby increasing their critical mass and helping to achieve greater economies of scale. Some proposals even suggest that school districts should be countywide, reducing their numbers from well over 300 to 87.

In fact, data from the Minnesota Department of Children, Families and Learning (CFL) at first glance appear to support this argument. Using CLF district-level revenue data for 2001, I compared Minnesota's 50 largest school districts with its 50 smallest. Essentially, I totaled all state and local revenues received by these districts and divided by their student enrollment to produce a "per student" cost of education. What I found was that revenues (and presumably costs) for the 50 largest districts averaged \$6,869 per student, while the average for the 50 smallest districts was \$7,146, suggesting that small schools cost 4 percent more per student on average than the large schools. Conclusion: large districts spend less per student and are in fact more fiscally efficient than small districts.

However, while I was at the CFL website, I decided to more closely examine what is known as the "Completion Studies." This is a tracking of students in each school district who entered the ninth grade in the 1997-98 school year and would have been expected to graduate as part of the Class of 2001. And it was here that I found information that helped me rethink the definition of the term "efficiency."

As we all know, every student who entered the ninth grade in 1997 did not necessarily graduate as part of the Class of 2001. Of those students tracked, it was found that while the majority did graduate, some were still in school attempting to complete their high school education, and of course, some others dropped out. Of those students

Examining Efficiency in our Public Schools

by Jack M. Geller
President
Center for Rural Policy and Development

tracked among the 50 largest school districts, 80.5 percent graduated as part of the Class of 2001. While no district among the largest 50 graduated 100 percent of their students, Edina (98.9%), Wayzata (98.7%) and Cambridge-Isanti (96.4%) came the closest. However, of the students tracked from the 50 smallest districts, 95.8 percent graduated as part of the Class of 2001. Furthermore, an outstanding 44 percent (22 out of 50) of the 50 smallest districts graduated 100 percent of their students.

I then began to wonder: since we are now firmly in the age of educational accountability, are there other measures of efficiency besides fiscal efficiency? How about educational efficiency? Is it fair to ask not only how much districts spend per student, but also how much it spends per graduate? After all, isn't graduation the best school accountability measure? To do this, I took the average per-student cost figures previously cited and multiplied them by the number of students who should have graduated in 2001. I then divided that by the number of students who actually graduated in 2001. Using this method, if a given district graduated 100 percent of its students, their cost per graduate would equal their cost per student. Consequently, the lower the graduation rate for a district, the higher its cost

per graduate, as the cost of educating those students who did not graduate are spread across those students that did graduate. By doing this I found that the cost per graduate among the 50 largest districts averaged \$8,531, while the cost per graduate among the 50 smallest districts averaged \$7,462, 14 percent lower!

So the question I ask is, what is an efficient school district? In 2001 the cost of educating a student in the state's largest districts was 4 percent lower per student than it was in the smallest districts. However, due to their lower graduation rates, the costs per graduate was actually 14 percent higher in the largest districts than in the smallest districts. And then I was reminded of a conversation I had with my father many years ago, when upon graduating college it was time for me to buy my first suit. In a nutshell he said there would be many different suits on the rack with many different prices. "Don't just look at the price, but rather look at the value," he said. "It's often preferable to pay a little bit more if the value is there."

It was a good way to evaluate suits, and lots of other things.

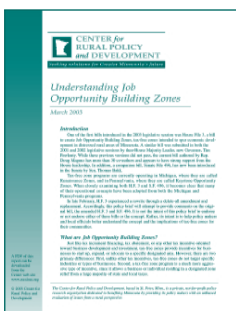


New report on tax-free zones compares, contrasts proposals

One of the most discussed pieces of legislation at the Capitol this year has been the proposal to create a program of tax-free zones around rural Minnesota. The Job Opportunity Building Zones were a principal feature of Gov. Tim Pawlenty's campaign last fall and are now a major tool in the governor's economic development strategy for Greater Minnesota.

To help policy makers and the public understand the JOBZ proposals, the Center for Rural Policy and Development produced a brief that takes an unbiased, non-partisan look at what JOBZ are and how the House and Senate proposals compare. The brief explains how the program would work, who would be able to participate in it, the potential benefits and costs to the state and local governments, and how this proposed program compares to similar existing programs in Michigan and Pennsylvania. The brief does not take a stand for or against the JOBZ proposal, but based on its analysis, it does provide several points for policy makers to consider, including:

- The zones should target real, existing development opportunities and not simply designate vacant, unimproved parcels of land in hopes of development.
- Provide a mechanism to ensure that the tax-free zones do not simply create an unfair competition within local markets. The report states its concerns about potentially providing tax breaks to "big box retailers" and others who will simply compete with local businesses within local and regional markets.
- Provide communities with access to technical support in the application process. It is likely that many of the communities that could most benefit from a zone designation may not possess the expertise to construct a competitive application.
- Ensure a quality, independent evaluation and document the progress and effectiveness of the tax-free zone strategy in a report to both the Governor and Legislature at the end of each biennium.



- Avoid to the extent possible the politicizing of zone designations.

"While the benefits of a tax-free zone seem fairly obvious, the costs to the state and especially to local governments, as well as the likelihood of success, need to be considered," said Jack Geller, president of the Center. "One of the most surprising finds in our research of Michigan and Pennsylvania's programs was how very little information there was on the costs, especially in terms of tax revenue lost to local governments. If and when Minnesota enacts this legislation, that is one factor that should be examined and tracked carefully."

To download a copy of "Understanding Job Opportunity Building Zones," visit our web site at www.ruralmn.org and click on Publications.

Upcoming Vacancies on the Center's Board of Directors

On May 5, the Secretary of State will post four open vacancies on the Center for Rural Policy and Development's board of directors. These four positions will be appointed by Governor Pawlenty in June.

As prescribed by Minnesota Statute 116J.421, three of the open vacancies are to be filled by representatives of private foundations with a demonstrated commitment to rural issues. The fourth vacancy is to be filled by a representative of a rural service industry. Individuals interested in applying for these open appointments should obtain an application for open appointments from the Secretary of State's office or web site.

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Center Welcomed to St. Peter

The Center for Rural Policy and Development was given a warm welcome to its new home in St. Peter with a ribbon cutting Jan. 22. Nearly twenty members of the St. Peter Area Chamber of Commerce came to look around the new offices, present plaques and help hold the giant white ribbon while it was cut by Center President Jack Geller.



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