A Model for SME Economic Development:
The South Carolina Enterprise Zone Act

J. Michael Alford, Ph.D.
Dept. of Business Admin.
The Citadel
171 Moultrie Street
Charleston, SC 29409 USA
Office Phone: 803-953-5170   Home Phone: 803-723-0243   FAX: 803-953-6764
e-mail: alfordm@citadel.edu

Abstract

This paper comments on some worldwide Enterprise Zone activities which have occurred over the past thirty-five years and then reports on the recently enacted South Carolina Enterprise Zone Act and the Rural Development Act by providing information on those portions which are most relevant to the Small and Medium Enterprises. The important aspects of involvement of all levels of government are reported. This act sed the experiences gained by developers of earlier Enterprise Zone developers. Hence, it is recommended as a model for adoption by governments at all levels.

Introduction

As competitive pressures increase and the demand for support of economic development at local and state or provincial levels increase as well, it is important that all players be aware of current programs for economic development available. This is especially true for SMEs. This group has a history of difficulty in obtaining funds for start up and expansion. Thus, it has been typical for governments worldwide and at various levels from community governments to national governments to offer incentives for business start-up and expansion. These incentives are for the purposes of attracting new industry to both developed and undeveloped areas as well as increasing job creation in the particular areas of concern. EZ programs typically use tax incentives of various types to attract industry.

Whether Enterprise Zones have achieved their purpose is a subject of continuing debate. Some feel that the programs are fragmented and do not include the appropriate agencies at various levels of government [1]. One of the primary difficulties in the United States has been achieving agreement on the roles of various government agencies. At the heart of this is the concept of "home rule" or local governments' ability to have a significant voice in how programs would be implemented and the resultant monetary impact on services and infrastructure of local governments.

Although most Enterprize Zone(EZ) programs have been enacted in recent years, the concept has been with us for over thirty-five years. For Example, Scotland reacted to the decline of its heavy industry in the 1960s by shifting its emphasis to high technology industries[2]. Electronics industries have been particularly prized additions to the economy of Scotland. A company, 'Locate in Scotland', was formed in 1981 to solicit business through the offering of attractive monetary packages. Additionally, Scotland has developed research consortiums among companies and universities.

One of Prime Minister Margaret Thatcher's earliest action in as Prime Minister in 1979 was to set up urban development corporations with the goal of reviving the declining city centers[3]. The areas were declared as EZs. The result in the London docklands area is that about 24 million square feet of commercial and industrial space has been made available for buildings, about 55 miles of new and improved roads have been built, and employment in the area is now 68,000 as compared to 27,000 before the project.

EZs have been established in St. Petersburg, Russia[4]; the Peoples Republic of China[5]; the Philippines[6]; and many other countries including seemingly unlikely countries such as Laos. Many of these efforts have been reported by Lorincze (Eastern Europe)[7], Lee(Korea)[8], Doh(Singapore)[9], Vianen(the European Community)[10] Alford(Japan, Korea, and U.S.)[11], and many others. Newton[12] reported on the genesis of Enterprise Zone efforts in 1993 and provided information on Enterprise Zone activities involving New Jersey (state), Newark, New Jersey(city), Louisville, Kentucky(city), and Louisiana(state) programs.

Enterprize Zone Modelling

One of the difficulties involved in developing EZs has been developing models which could accurately reflect the various impacts of EZ actions. As one local government official stated, "We need to know at what point the incentives we offer will outweigh the benefit to our community. While there have been a number of efforts to properly model the EZ, two models look especially promising. One was provided by Ge[13]. Ge analyzes the direct and indirect impacts of urban EZ on regional development. The direct and indirect impacts of urban EZs on regional economies such as job creation, urban development, agricultural wage and changes in the intermediate goods sector. A more complex model is used for the empowerment zone of Louisville, Kentucky. Louisville uses the computer mapping and data analysis resources of the Louisville and Jefferson County Information Consortium. This group has built one of the most comprehensive metropolitan geographic databases in the United States[14].

The South Carolina Enterprise Zone Act[15]

The State of South Carolina studied the programs in place, such as those mentioned above, plus programs in Alabama, Mississippi, and other county and municipal government programs in developing the Enterprise Zone Act of 1995. The original act covered about 70 percent of the state. The act was later amended by the Rural Development Act which became law on June 27, 1996.

It is felt that the South Carolina acts provide an especially good model for agencies at all levels seeking to provide programs aimed at increasing economic development in their respective areas. This is because of the clarity of the language and the fact that the different levels of government are participants in the program. That is, the acts have recognized both the impact upon and role to be played by local governments. A unique feature of the South Carolina Enterprise Act is that it provides for SMEs as well as for larger firms. This reduces duplication of programs. Another very important feature of the act is that specific activities on the part of county and municipal governments in regard to taxes and fees are covered. This protects these governments from revenue loss and provides them an opportunity to actively participate in the programs covered in the act.

The Act

The essential sections of the act will be presented to establish the framework of the model and then the amendments provided via the Rural Development Act will be presented, followed by a summary of important features.

The South Carolina Enterprise Zone Act of 1995(the act) is composed of three different components: (1) The Enterprise Zone Act of 1995, (2) the Economic Impact Zone Community Development Act of 1995, and (3) provisions relating to apportionment of income. A significant amendment to the act occurred in 1996 with the enactment of the Rural Development Act(RDA) its impact on the act will be described following the description of the act.

Enterprise zones

Section 1, the act, provides state income and property tax, as well as financial incentives for "qualifying businesses" which locate in an "enterprise zone." These terms are:
Enterprise Zone - any one of the following:

- A census tract in which either the median household income is 80 percent or less of the state average or at least 20 percent of the households are below the poverty level.

- A county classified as "less developed" pursuant to the Jobs Tax Credit Act. (The Department of Revenue annually ranks the counties for purposes of the Jobs Tax Credit Act; the counties qualifying as "Less Developed" in 1995 are ...)

- A federal military base or installation in which employment was reduced by 3,000 or more jobs since December 31, 1990 (this includes the Air Force Base in Myrtle Beach, the Charleston Naval Shipyard, and the Savannah River Plant in Aiken. Note that only the base itself qualifies as a zone under this provision).

- A census tract in which at least 50 percent of the employment is in textile or apparel jobs.

-A census tract in which certain catastrophic job losses have occurred, including where a manufacturing facility has closed resulting in job losses of at lest 25 percent of the work force (this includes Ware Shoals and Great Falls).

- A census tract any part of which is within 20 miles of a federal facility which has reduced its civilian workforce by 3,000 or more jobs after December 31, 1990; which includes both the Charleston Naval Shipyard and the Savannah River Plant; the net effect includes all of Aiken and Charleston counties and most of Berkeley and Dorchester counties.

- A census tract in which a penal institution operated by the South Carolina Department of Corrections has closed, including CCI in Richland County.

Qualified Business - A business which locates in an enterprise zone and meets the following criteria:

The business must qualify for the Jobs Tax Credit Act; qualifying businesses include corporations operating manufacturing, tourism, processing, warehousing, distribution, research and development and corporate office facilities.

The business must provide health care benefits to full time employees.(The act does not specify any minimum benefit levels.)

In addition, the business must enter into a revitalization agreement with the Advisory coordinating Council for Economic Development if it wishes to collect Job Development Fees and the Council must certify in such cases that the incentives are appropriate for the project and that the total benefits of the project exceed the costs to the public.

Income tax incentives

- First, with reference to state income tax incentives, if at least 51 percent of the full time employees hired for the project either reside in an enterprise zone at the time of employment, have a household income that is 80 percent or less of the median household income for the county prior to employment or have been a recipient of AFDC(Aid For Dependent Children) payments within the past 12 months, the business is entitled to the maximum Corporate Income Jobs

- Tax Credit($1,000 annually per employee): in addition the business is entitled to an additional $500 per year tax credit in the third, fourth, and fifth year of any AFDC recipient's continued employment with the business.

These credits are in addition to any other credits for which the business is entitled, for example the credits available for locating in a multi-county industrial park.

Property Tax Incentives

-Second, with reference to property tax incentives, the business is eligible to negotiate for fee-in-lieu of property tax advantages if it meets one-half the requirements of the current Fee-in-Lieu statute.

The Fee-in-Lieu of Property Taxes Act provides a mechanism by which companies which make the requisite investment within a five year period might enter into an agreement with a county under which the company pays the county a reduced fee instead of the usual county property taxes.

The Fee-in-Lieu Act can save a company substantial property taxes by allowing the company to negotiate an assessment ratio as low as 6 percent(instead of the normal 10.5 percent) as well as "freezing" the applicable millage rate and the value of the property for up to 20 years.

The Fee-in-Lieu Act now applies on a tiered basis.

Qualifying businesses locating in an Enterprise Zone may negotiate with the respective county government for a Fee-in-Lieu contract if they:

-create 100 new full time jobs and invest a minimum of $30 million

-create 150 jobs and invest $20 million

-create 200 new jobs and invest $10 million; or

-invest $42.5 million. Businesses are also eligible to use special source revenue bonds under the Fee-in-Lieu Act.

Financial Incentives - Qualifying businesses may also collect and expend Job Development fees by retaining certain employe withholdings which would otherwise be going to the State of South Carolina. in order to collect the fee, the business must enter into a revitalization agreement which allows such withholdings, and the funds must be held in an escrow account with an FDIC insured bank.

Employers might use the withheld amounts for any of the following purposes:
-training cost and facilities
-acquiring and improving real estate
improvements to both public and private utility systems, including water, sewer, electricity, and telecommunications
-fixed transportation facilities including highway, rail, water and air; and construction and improvements for the purpose of complying with environmental laws.

Economic Impact Zone Community Development Act

Section 2 of the act provides a state income deduction for persons who purchase stock in a small business which locates in an "Economic Impact Zone," which includes areas within 50 miles of certain federal military installations which have closed.

The definition currently appears to cover only areas within 50 miles of the Charleston Naval Shipyard, although there is legislation pending to include the Savannah River plant.

These Zones must also be certified by the Budget and Control Board. As April 18, 1995, the Board had not yet issued this certification.

Section 2 provides that an individual may receive a state income tax deduction for 20 percent of the purchase price of certain stock up to $10,000 a year($100,000 lifetime). The stock must be issued by a small corporation which uses the proceeds to purchase property in an economic impact zone.

The bill also provides for all businesses located in a zone(and not just small businesses) an investment tax credit of up to 5 percent of the cost of obtaining certain manufacturing and other tangible property which is constructed or acquired for use in a zone. Eligible property includes tangible property(including certain computer software) which is used as an integral part of manufacturing, production, or extraction of or furnishing transportation, communications, electrical, energy, gas, water or sewage disposal services in the Economic Impact Zone.

Apportionment of Income

Section 3 modernizes the South Carolina law for apportionment of income for taxpayers who do business in multiple states. The first part of this section applies to existing taxpayers. The second part of the section allows a taxpayer to negotiate an allocation or apportionment of income agreement with the Department of Revenue if the company is planning a new facility or an expansion of an existing facility and the Coordinating Council certifies that the benefits to the public exceed the costs.

The Rural Development Act

The major provisions of the Rural Development Act are:

1. The entire state is made an Enterprise Zone;
2. Job Tax Credits are increased for almost every county, and are greatly increased for the poorest counties;
3. County Council may approve 4% assessment ratios(down from 6%) for fee-in-lieu agreements for the very largest investments($400 million and 200 new jobs, with certain exceptions);
4. A Rural Infrastructure Fund is established to provide infrastructure for projects which locate primarily in the two poorest tiers of counties; while the initialfunding will be in the range of $4 million, the fund is expected to rapidly grow; and
5. The Fee-in-Lieu program is made much simpler and more flexible.

Provisions of the Rural Development Act

Some provisions of the Rural Development Act are outlined below. Those which deal with legislative issues and matters not impacting content are omitted.

Rural Infrastructure Fund

Grants from the Fund will primarily be available to benefit counties designated as "least developed" or "under developed" as defined by the job;bs tax credit statute. The Fund shall be administered by the Coordinating Council for the purpose of providing "financial assistance to local governments." The funds may be used for (1) training costs and facilities; (2) improvements to regionally planned public and private water and sewer systems; (3) improvements to both public and private electricity, natural gas, and telecommunications systems; and transportation facilities, including highway, rail, water, and air.

Job Development Fees(Withholdings)

A new code section is created for purposes of allowing development authorities for closed or realigned military installations to keep job development fees from their federal tenants.

Utility Territorial Assignment Plan

Insures that the bill does not alter or amend the Territorial Assignment Plan or other regulation of electrical utilities in the state. NOTE: In South Carolina, electric power is provided by two public owner (stock traded on the market) companies and several electric co-operatives which were established to provide power to rural areas under state sponsorship. The latter generate electricity and also buy electricity from other suppliers in order to provide service to their companies. The geographic areas they serve are regulated by the Public Utilities Commission.

Fee-in-Lieu(Property Taxes)

Deletes the requirement that the Board of Economic Advisors solely determines the benefits of a fee project. This section now requires that the county council of the affected county, with the assistance and advice of the Department of Revenue or the Board of Economic Advisors, determine the benefit of the fee project.

Allows certain qualified investors to receive the availability of a 30 year fee agreement. Also, the same qualifying businesses will be granted an eight(8) year period to meet the minimum investment requirements. The investor also must report annually to the county the amount of each year's investment during the period allowed for investments.

Allows for a minimum assessment ratio of four percent(4%) for qualifying businesses(1) investing $200 million and having invested $200 million previously, and creating 200 new full-time jobs; (2) investing at least $400 million and creating 200 new full-time jobs; (3) a Limited Liability Company investing $400 million and crating 100 full-time jobs with an average salary of at least $40,000 in a county classified as either least developed or under developed; or(4) a business which meets the minimum investment totals which pays at least 50% of the taxes in the county for more than 25 previous years is not required to meet the job creation levels.

Allows for replacement property to qualify for the fee available under Chapter 12, of Title 4.

Allows for the amending of Fee-in-Lieu agreements at any time, provided that the assessment ratio or length of the agreement cannot be changed.

Clarifies the distribution of fee payments to local governments. Also, allows a county to use a portion of the fee payment for infrastructure improvements as provided in Section 4-29-68, without the requirement of issuing special source revenue bonds.

Liberalizes the taxpayer's ability to transfer or assign an interest in an inducement agreement, millage rate agreement, lease agreement, or property to which such agreement relates. Also, requires county approval before the transfer can take place.

Jobs Tax Credit(Income Taxes)

As outlined below, this section increases from three to four the tiered classification system for purposes of the jobs tax credit. With the exception of counties with certain closed military for federal facilities and certain other counties, counties are ranked using unemployment and per capita income rates. For example, the 12 counties with a combination of the highest unemployment rate and lowest per capita income are designated least developed(Tier I) counties. The minimum job creation requirement in urban counties is reduced to ten (10) jobs statewide. The Tiers and Jobs Tax Credits are as follows:

ALLOCATION OF JOBS TAX CREDIT

County Classification	Tax Credit Per New Job
Tier I Least Developed	$4,500
Tier II Under Developed	$3,500
Tier III Moderately Developed	$2,500
Tier IVDeveloped	$1,500

An additional $1,000 credit is available for jobs created in a multi-county industrial park.

Retail establishments and service related industries in least developed counties(Tier I) now qualify for the Jobs Tax Credit. In addition, a service related industry which creates at least 250 jobs in any county now qualifies.

A cap of $5,500 tax credit per job is also imposed.

Job Development Fees

Allows a corporation to collect job development fees for new jobs created and for existing purposes for training. Creates the State Rural Infrastructure Fund and provides funding by means of allowing certain businesses to retain only a percentage of the job development fees allowed. The State Rural Infrastructure Fund is funded from a portion of the Job Development Fees collected from qualifying businesses. The amount collected depends upon the county in which the jobs are created, as follows:

Retraining must be approved by and performed by a Technical College under the jurisdiction of the State Board for Technical Training. The Coordinating Council may waive 95% of the limits as listed below to the Rural Infrastructure Fund share in the case of certain very large "core" investments. The allocation of job development fees is below.

Allocation of Job Development Fees

County Class	Rural Infrastructure Fund	Business
Tier I	0%	100%
Tier II	15%	85%
Tier III	30%	70%
Tier IV	45%	55%

Special Source Revenue Bonds(Property Taxes)

Special Source Revenue Bonds may be used for acquiring or constructing improved or unimproved real estate used in the operation of a manufacturing or commercial enterprise.

Comments

The information presented about the Enterprise Zone Act as amended by the Rural Development Act for the State of South Carolina provides a model for use by both government agencies attempting to increase job creation and for entrepreneurs seeking assistance in establishing and/or expanding business operations. Although total credit for economic investment in South Carolina in 1996 may not can be given to the Enterprise Zone Act, there was a record business investment in the state during 1996. One investment by a large firm if $400 million could be tied directly to the RDA [16]. It is well accepted that investments by larger firms spawn business for SMEs. SMEs will be specifically interested in the critical factors below.

Critical factors for SME development are:

-the low job creation level: 10 jobs

-allowing of making investments over a period of time instead of an initial lump sum investment

-allowing the SME firm to negotiate and interface directly with local authorities instead of central government

-tax credits enhance opportunity to hire skilled workers displaced by closing of federal government operations

-rural infrastructure development fund allows SMEs the opportunity to locate in rural areas where real property costs are significantly less than in highly developed areas

-tax credits may be carried forward.

Conclusion

Since the act described herein is one of the most recent anc comprehensive in regards to the relationships between various government agencies and industry, it is recommended as a model of other cities, states, and nations.

The State of South Carolina faces a significant task in educating local government agencies in the application of the Enterprise Zone Act and the Rural Development Act. There have already been prosposal to county governments from businesses wishing to take advantage of the EZ act. Additionally, a major effort at ensuring both existing firms and entrepreneurs are aware of the existence of the new acts and how they can be utilized. Toward this end, assistance should be elicited from business promotion groups such as county and local economic development agencies, chambers of commerce, Small Business Institutes, Small Business Development Centers, and educational institutions which teach courses and conduct programs in small business and entrepreneurship. Members of the above organizations can also assist in this effort by speaking on the topic at meetings of various civic organizations.

Information on the acts described here can be obtained directly from:

Mr. Burnet R. Maybank, III, Director
Department of Revenue and Taxation
P.O. Box 125, Columbia, SC 29214.

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