

**REQUEST FOR COUNCIL ACTION**

**SUBJECT: California Enterprise Zone Program and the San Bernardino Valley Enterprise Zone**

**MOTION:**

I move to consider participation in the San Bernardino Valley Enterprise Zone (SBVEZ), and direct staff to exercise its due diligence in seeking Enterprise Zone designation.

**STAFF RECOMMENDATION:**

Staff recommends that Council explore membership in the San Bernardino Valley Enterprise Zone, and direct staff to exercise its due diligence in seeking Enterprise Zone designation.

**DISCUSSION:**

**Background**

In order to provide background on this agenda item, and the conversations that have occurred to date, the following is noted:

Objective 19 on page 10 of the Council adopted Economic Development Plan states: "Regional collaboration on economic development / redevelopment." The measures for this objective reflect working with the San Bernardino County Economic Development Agency.

On August 20, 2009, the City was advised of the opportunity to explore a joint Enterprise Zone application. This invitation was sent from the San Bernardino County Economic Development Agency.

On November 18, 2009, a meeting was held at the Redevelopment Agency with Redevelopment Agency staff, County staff, and chaired by then Mayor Harrison. The outcome of the meeting was agreement that this was a good project to look into and that it should be brought forward to the Council.

**California Enterprise Zone Program**

California's State Enterprise Zone Program was established in 1984 to stimulate business investment in depressed areas of the State and create job opportunities for Californians. The California Enterprise Zone Program is administered by the State of California's Department of Housing and Community Development. Current legislation allows for 42 Enterprise Zones. California communities received their designations from the State of California through a competitive process. Each zone designation is in effect for 15 years.

The California Enterprise Zone Program targets economically distressed areas using special state and local incentives to promote business investment and job creation. By encouraging entrepreneurship and employer growth, the program strives to create and sustain economic expansion in California communities.

Businesses within Enterprise Zones are eligible for substantial State tax credits and benefits. The following is a highlight of the Enterprise Zone benefits to businesses:

- Firms can earn \$37,440 or more in state income tax credits for each qualified employee hired after the designation date, over a five-year period.
- Corporations can earn sales tax credits on purchases of \$20 million per year on qualified machinery and machinery parts. Example: If the business spent \$150,000 to purchase machinery and paid sales tax of \$12,000 (based on 8% sales tax), then the business may reduce the amount of income tax by \$12,000.
- Up-front expensing of certain depreciable property up to 40% of the eligible cost of qualified property as a business expense rather than a capital expense. Example: If the business purchased racks that cost \$30,000, the business would normally depreciate the racks over a 10-year period using the straight-line method. However, using the Enterprise Zone Business Expense Deduction method, the business may claim \$12,000 ( $\$30,000 \times 40\%$ ) as a first year business expense. The business' new depreciable base will be \$18,000 ( $\$30,000 - \$12,000$ ), and the business may claim \$2,000 of normal depreciation for each of the next 9 years, ( $\$18,000$  divided by 9 years = \$2,000).
- Lenders to Zone businesses may receive a net interest deduction. For taxpayers (lending institutions, individuals, etc.) investing in an Enterprise Zone business, a deduction from income is allowed for the amount of net interest received from loans made to a trade or business located solely within an Enterprise Zone area. Types of loans that qualify for this deduction include business loans, mortgages, and loans from non-commercial sources. The following requirements must be met to qualify for the deduction:
  1. Use the loan strictly for the borrower's business activities within the Zone.
  2. The lender does not have equity or other ownership interest in the borrower's trade of business.
  3. Borrower must continue business activities in the Zone.
  4. Payment must be received before the life of the Zone expires.
- Unused tax credits can be applied to future tax years, stretching out the benefit of the initial investment.
- Enterprise Zone companies can earn preference points on State contracts.
- Up to 100% Net Operating Loss (NOL) carry-forward. NOL may be carried forward 15 years.

### **San Bernardino Valley Enterprise Zone**

San Bernardino Valley Enterprise Zone (SBVEZ) is a multi-jurisdictional State Enterprise Zone formed in 2006. SBVEZ is presently comprised of the County of San Bernardino (the "County"), the Inland Valley Development Agency (IVDA) and the cities of San Bernardino and Colton. SBVEZ is the result of a successful joint application for an Enterprise Zone designation submitted in competition with other jurisdictions to the State Department of Housing and Community Development (HCD). Portions of the SBVEZ are located within each of the jurisdictions. Attachment No.1 shows the current boundaries of the SBVEZ.

### **Multi-jurisdictional Memorandum of Understanding**

Each of the jurisdictions, comprising SBVEZ, entered into a Memorandum of Understanding (MOU) to demonstrate a high level of commitment, consistency in programs, and cooperation as required by HCD. The MOU sets forth the duties and responsibilities for each jurisdiction. Each jurisdiction has the duties to provide business assistance to their respective businesses within the SBVEZ, cooperate in a joint marketing strategy, and approve an annual budget.

San Bernardino County has the responsibility as Zone Manager. The Zone Manager administers and coordinates joint efforts of the SBVEZ. Zone Coordinators are appointed by each participating jurisdiction to oversee its respective portion of the SBVEZ. Zone Coordinators are usually city, or redevelopment/economic development agency staff members.

The IVDA Board of Directors presides as the SBVEZ Oversight Committee. The Oversight Committee oversees the administration, budget and operations of the SBVEZ. San Bernardino County and the cities of San Bernardino and Colton are members of IVDA. The City of Redlands is currently exploring membership in IVDA.

### **California Enterprise Zone Program Memorandum of Understanding**

The State of California's Department of Housing and Community Development entered into a Memorandum of Understanding (HCD-MOU) with multi-jurisdictions upon official designation of SBVEZ. The HCD-MOU is the official notification of the designation of the San Bernardino Valley Enterprise Zone under the California Enterprise Zone Program. The purpose of the HCD-MOU is to ensure SBVEZ's compliance with the California Enterprise Zone Program (a) statutes; (b) regulations; (c) the representations contained in the SBVEZ application/MOU; and the terms and conditions of the HCD-MOU. The HCD-MOU is effective from October 15, 2006 through October 14, 2021; which coincides with the 15 year life for Enterprise Zone designation.

### **SBVEZ Expansion**

The State Department of Housing and Community Development is drafting revised expansion rules and the process for submitting an application to expand (1) within the existing enterprise zone jurisdiction(s), (2) to expand into an adjacent (neighboring) jurisdiction, and the contiguity rules for each. The revised rules would allow for zones to expand by 15% of original designation acreage. SBVEZ's current acreage is

approximately 25,065 acres. SBVEZ anticipates submitting an expansion application for up to 1,568 acres. San Bernardino County as Zone Manager is approaching neighboring jurisdictions interest in submitting a joint application for the expansion of the SBVEZ. Among other jurisdictions, SBVEZ has approached the City of Redlands.

Guidelines for expansion applications are as follows:

- The land in the proposed expansion must be zoned for industrial or commercial use.
- The expansion areas must have definitive boundaries and be contiguous to an existing zone.
- Each of the jurisdiction's governing bodies must approve the expansion by adoption of an ordinance or resolution.
- Basic infrastructure including but not limited to gas, water, electrical service and sewer systems are available to the area included in the expansion.

#### **Redlands Enterprise Zone Expansion Opportunity**

SBVEZ anticipates applying to the State for expanding the Enterprise Zone into the unincorporated area of the County, commonly known as the "Donut Hole". (The Donut Hole is also designated as Sub-Area 4 of IVDA's redevelopment project area, bound by Lugonia/Palmetto and the California/210 Freeway.) If SBVEZ expands into the Donut Hole, this would allow Redlands to meet the application criteria for being contiguous to an existing zone for land east of the 210 Freeway, north of Lugonia Avenue (See Attachment No. 2). Attachment No. 2 identifies one option of approximately 397 acres within Redlands which meets the eligibility criteria listed above for Enterprise Zone expansion.

Under this option, the question is whether the State would allow for enterprise zone expansion into adjacent lands (Redlands) concurrently with expansion into existing jurisdictional boundaries (County Donut Hole). The alternative would be a two step process; whereby, (1) SBVEZ initially applies for expansion into the Donut Hole; and, then (2) a second application to expand into Redlands.

A second option (See Attachment No. 3) identifies approximately 300 to 400 acres within Redlands' corporate boundaries which is adjacent and contiguous to the existing enterprise zone along Mountain View Avenue at West San Bernardino Avenue. The benefit of this option is that the State could consider the enterprise zone expansion without the concurrent expansion of the County Donut Hole.

A third option is a combination of both alternatives up to 300 to 400 acres maximum.

#### **Redlands Membership**

Redlands could become a party to SBVEZ through an amendment of the multi-jurisdiction Memorandum of Understanding agreement; and approval of SBVEZ's application for expansion. The amended MOU must receive 100% approval by the governing bodies of the current jurisdictions. The amended MOU, allowing Redlands to

become a party to SBVEZ, would be conditioned upon the State of California's Department of Housing and Community Development approving the SBVEZ expansion.

SBVEZ estimates several months to process an amended MOU due to the lead times required by each City Council and the Board of Supervisors. SBVEZ would then submit a joint application for zone expansion. The State will notify the applicant of its decision to approve or deny the expansion request within thirty (30) days of receipt of the expansion request.

Possible benefits for the City joining as a party to SBVEZ:

- The City could market the benefits of an Enterprise Zone to attract businesses.
- California's Enterprise Zone Program is one of state's largest and most successful economic development tools.
- Enterprise Zones provide incentives to create jobs, attract private investment, and improve economic conditions.
- The SBVEZ program will help stimulate business and industrial growth in depressed areas of the City.
- An Enterprise Zone in Redlands would have an effective life from the date the State approves the expansion through October 14, 2021 (the end date for the current SBVEZ designation); potentially an eleven year period.
- An Enterprise Zone would be an added tool for economic development in Redlands.
- The City would receive additional economic benefits which would be offered to businesses through the County's Department of Economic Development, such as:
  1. Free business advertising
  2. Free site selection assistance
  3. Free business market analysis
  4. Workshops for little or no cost
- Coordinated efforts with other members of SBVEZ for collaborative marketing, economic development and business outreach.
- Representation at the California Association of Enterprise Zone's annual conference, training events and seminars.
- Increased networking with the State's Department of Housing and Community Development Department.
- Receive the latest updates from the State Franchise Tax Board.
- Network with other Enterprise Zone managers throughout the State.

Possible reasons for not joining as a member of SBVEZ:

- Regional collaboration is not a priority at this time.
- SBVEZ requires 100% approval by each of the jurisdiction's governing bodies
- State may not approve SBVEZ expansion.

- Supervisorial districts may want enterprise zone expansion elsewhere.
- Zone expansion may not include Donut Hole; hence, proposed expansion is non-contiguous.
- Future legal and financial liabilities of the SBVEZ and its affect on Redlands.
- Limited staffing to oversee SBVEZ activities.

**FISCAL IMPACT:**

- There is an associated annual fee for joining SBVEZ.
- The annual fee is based on the total budget for five years divided by the number of acres within the entire zone. (As reported by the SBVEZ members, the estimated cost to Redlands would be \$13,498 for the remaining 2 years of SBVEZ's 5 year budget). This is all contingent upon the budget staying in the same ratio as the land. As SBVEZ adds additional land or revises the budget, the numbers may change.
- Through new businesses locating within a proposed Enterprise Zone, there could be increased property tax and/or sales tax revenues to the City; and, increased tax increment revenues to the Agency.

As part of the City's consideration, prior to joining SBVEZ, staff will consult with legal counsel to determine the extent of any potential legal or other financial liabilities.

**ALTERNATIVES:**

The City Council may:

1. Direct staff to pursue possible membership and exercise due diligence; or,
2. Direct staff not to pursue; or,
3. Receive and file this report; or,
4. Provide alternative direction to staff.

**ATTACHMENTS:**

1. SBVEZ Current Boundary Map
2. Alternative 1 - Redlands Enterprise Zone boundaries adjacent to Donut Hole
3. Alternative 2 - Redlands Enterprise Zone boundaries adjacent to existing SBVEZ

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