"The right to criticize government is also an obligation to know what you're talking about."

Lent Upson, First Director of the Citizens Research Council

March 12, 2024

The Research Council's Report on Tax Incentives and How the Future of Health Project Is Connected

In a Nutshell

- Detroit City Council awarded $296.6 million in tax incentives to the Future of Health project, the $22.9 million in tax abatements will add to the $264.5 million in city taxes abated between FY2017 and FY2023.
- Socioeconomic problems such as crime, poverty, and low educational attainment make development more tenuous and costs, some within the city's control and some beyond, make investment less profitable.
- To address these burdens to business, the city commonly awards tax incentives, and those rewards will remain common until the city implements different policies to ameliorate its socioeconomic problems

On February 27th the Detroit City Council approved tax incentives valued at $296.6 million for the Future of Health project. The project and the City Council's decision to award these tax incentives offers an opportunity to expand on research from the Research Council's January report, "An Assessment of Detroit's Economic Condition and a Critique of its Economic Development Efforts." This research note summarizes our report and examines how the Council's actions add to the amount of taxes already abated by the City of Detroit.

The Research Council's report on tax incentives

For as much opportunity as Detroit presents, from the perspective of current and prospective businesses, it presents several challenges. The Research Council's report examined five elements of the city's socioeconomic condition: population, education, income, poverty, and unemployment. Each factors into business location decisions within the city and the potential return on investment.

Detroit's population loss is storied. Since 1950, the population has fallen by 1.2 million or 65.4 percent. The population that remains is Black (77.8 percent of the population), poor, and poorly educated relative to other jurisdictions in the Detroit-Livonia-Warren metropolitan statistical area (Detroit MSA). The Detroit MSA includes Lapeer, Livingston, Macomb, Oakland, St. Clair, and Wayne County.

Only an estimated 16.9 percent of Detroit residents have a bachelor's degree or higher. Detroit ranked 161st among the other 207 jurisdictions within the Detroit MSA. Less education makes for diminished employment prospects. The local unemployment rate is consistently higher relative to countywide or statewide comparisons, and fewer job opportunities make for lower incomes and higher poverty rates.

In 2022, Detroit's per capita income was $22,861. Between 2013 and 2022, inflation-adjusted per capita income grew by 22.4 percent. Still, despite per capita income growth that outpaced that of the Detroit MSA, Wayne County, the state, and the U.S. overall, Detroit is ranked 202nd relative to the other jurisdictions within the Detroit MSA. Again, lower incomes make for higher poverty. Detroit's poverty rate exceeds that of its peers. In 2022, an estimated 31.5 percent of Detroit residents were living in poverty, the sixth highest in the Detroit MSA.

These socioeconomic ills are compounded by other costs particular to Detroit, some of which can be controlled by its elected officials and some which cannot. The city mandates community benefits agreements (CBAs) between private developers and residents who live within the vicinity of planned projects. CBAs are required for projects that either have a value of $75 million and receive tax incentives valued at $1 million or more or receive land transfers from the city of equivalent value. Whatever the merits of CBAs, which have allowed residents to secure affordable housing commitments from private companies and repairs for recreational facilities, these agreements add to the cost of doing business in the city.

Additionally, local hiring requirements mandate that private developments source 51 percent of labor from the Detroit labor pool. The requirement, which has existed since the Kilpatrick administration, requires projects out of compliance to pay fees to the city.

These informal paperwork taxes are levied on top of real property taxes, which are levied at a higher rate than almost any other jurisdiction in the Detroit MSA. Out of the 208 jurisdictions within the Detroit MSA, businesses in only six other cities pay higher tax bills when combining state, county, city, school, and special district taxes.

The city's elected officials set the city's tax rate, but they have no control over tax rates levied by other entities with taxing power. Nor do Detroit's elected officials set car or homeowner's insurance rates, which are relatively higher in the city relative to other jurisdictions, owing in part, to the higher crime rate within the city.

City officials, aware of these challenges, attempt to address them through certain policy levers they can control. Among the city's efforts to offer current and prospective businesses a more hospitable stay, and improve the potential return on investment for select developments, it frequently subsidizes private developments with public dollars. As will be shown with the proposed Future of Health project, it employs tax incentives more so than most other jurisdictions.

The Future of Health project and tax incentives

The Future of Health is the name for a New Center area development project undertaken by a consortium of Henry Ford Health System, the Detroit Pistons, and Michigan State University. Notable components of the project include an expansion of Henry Ford Hospital, a new medical research center, an estimated 662 mixed-income residential units, and an added 326,362 square feet in office space and 31,348 square feet in retail space. Total investment equals an estimated $773 million. To support that investment, the City Council awarded $296.6 million in tax incentives over 35 years.

Two sorts of tax incentives were awarded to the Future of Health project: tax increment financing (TIF) and tax abatement. TIF permits public authorities, such as the Brownfield Redevelopment Authority, to sequester the property tax revenues resulting from a project within an established area that otherwise would have been collected by the state, county, city, and other entities with the power to tax. Captured property tax revenues may then be used to reimburse private developers for some costs or to support debt-financed capital improvements. To be clear, under TIF the tax bill is the same as it would be without TIF. TIF diverts revenue from property taxes paid on the incremental difference between when the TIF district was established and the appreciated value attributed to the development.

On the other hand, tax abatement does lower awardees' tax bills, either via a freeze in taxable property value or a cut to applicable mill rates (i.e., the tax rate—a mill is equal to $1 in tax for every $1000 in taxable property value).

Of the $296.6 million awarded to the Future of Health project, $241.7 million is attributable to TIF, and $54.9 million is attributable to tax abatement.

Understand that the estimated $54.9 million value of tax abatement awarded to the Future of Health project does not represent a direct payment to private developers.

It should also be noted that tax abatement shields awardees from taxes levied by the city, the State of Michigan, Wayne County, and other entities. Detroit businesses pay property tax to the city (27.9520 mills), the school district (31 mills), the county (7.822 mills), the state (6 mills), and miscellaneous entities such as the Detroit Zoo Authority. The $54.9 million in tax abatement value is the total amount of taxes that will be foregone by each of those jurisdictions, not just the city over the term of 35 years.

City Council awarded tax abatement under Public Acts (PA) 147 of 1992 (Neighborhood Enterprise Zone Act), PA 210 of 2005 (Commercial Rehabilitation Act), and PA 255 of 1978 (Commercial Redevelopment Act). Cumulatively across the 35 years of the project plan, $16.1 million in city taxes specifically will be abated under Public Act 147, $6.3 million under Public Act 210, and $498,226 under Public Act 255. The estimated $22.9 million, or calculated annual rate of $654,286, only adds to the approximately $37.8 million abated annually by the City of Detroit.

Detroit's use of tax abatement relative to other jurisdictions

Governments report the amount of abated taxes in their annually issued financial statements pursuant to Governmental Accounting Standards Board guidance under Statement No. 77.

Of the 208 jurisdictions within the Detroit MSA, 200 had Fiscal Year (FY)2022 financial statements in the state database. (FY2022 was the most up-to-date set of financial statements commonly issued by the subject jurisdictions.) The dataset was further whittled down to 73 jurisdictions when those basic financial statements that were without Statement No. 77 disclosures were excluded.

The analysis measures subsidies relative to taxable value. On that basis, Detroit stands out as a heavy user of tax abatement. In FY2022, Detroit abated $41.2 million in taxes, or $6.16 for every $1,000 in taxable value. Out of the 73 jurisdictions within the dataset, Detroit was second only to Wyandotte, which abated $7.9 million or $13.36 for every $1,000 in taxable value. The mean across the 73 jurisdictions was $0.60 in tax abatement for every $1,000 in taxable value.

Most recently in FY2023, Detroit abated $50 million in taxes. Cumulatively, between FY2017, when Statement No. 77 disclosures were first made in the city's financial statements, and FY2023, the most recently issued statements, Detroit has abated $264.5 million in taxes.

Conclusion

Detroit, even as depleted as it is, is a major American city. The city is an epicenter of industry and business, arts, and entertainment. Yet, crime, low levels of educational attainment, low incomes, and poverty, conspire to make an unattractive business proposition. Moreover, public policy, particularly the cumulative property tax rate, further worsens the potential return on investment. To compensate for these socioeconomic problems and its own policies, the city offers tax incentives, more so than almost any other jurisdiction in the metropolitan area.

Detroit should have a different approach to economic development, the subject of phase two of the Research Council's analysis. Without a different approach, private developers, oftentimes multi-millionaires (sometimes multi-billionaires) will continually come to plead before the City Council, and their pleas will be justified by every tax bill, release of FBI crime statistics, and resident who lacks a diploma.

ABOUT THE AUTHOR

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James L. Tatum III is the Researcher for the Detroit Bureau of the Citizens Research Council. Previously, he served as an analyst in the City of Detroit's Office of the Chief Financial Officer (OCFO) where he prepared cost-benefit analyses of City projects, asset sales and labor contracts, forecasted city revenues and expenditures, and conducted scenario analyses for the City's pension plans. In addition to his practical experience, he is an accomplished academic. His research on debt, pensions, insolvency, Chapter 9 bankruptcy, and dissolution has been published in trade, law, and academic journals.

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