SALES AND USE TAX REVIEW COMMISSION

RECOMMENDATION PURSUANT TO P.L. 1999, C. 416

BILL NUMBER: **A-2712**

DATE OF INTRODUCTION: **7/13/00**

SPONSOR: **Assemblyman Cohen**
Assemblyman Impreveduto

DATE OF RECOMMENDATION: **10/13/00**

IDENTICAL BILL:

COMMITTEE: ACT

DESCRIPTION:
The bill authorizes the creation of a new UEZ in Roselle Borough, Union County.

ANALYSIS:
In 1983, the Legislature enacted the New Jersey Urban Enterprise Zone Act to help revitalize the state's economically distressed urban areas. N.J.S.A. 52:27H-60 et seq. The Act was meant to provide a framework for encouraging private capital investment and job creation in these selected urban areas. There were originally 10 designated zones, which was increased to 20 zones in 1993 and 27 in 1996. The main benefits made available to qualified businesses in an urban enterprise zone are twofold: a sales tax exemption on most purchases of goods and services for use at the zone business (intended to attract relocation/expansion of business into the zone) and a reduced sales tax rate of 3% on sales of goods from the zone business (intended to attract shoppers into the zone). This bill would increase the number of enterprise zones to 28.

The validity of granting an ongoing government subsidy that favors particular municipalities at the expense of all other municipalities has to be questioned. The Bill Statement refers to the negative economic impact on Roselle due to the bordering enterprise zone of Elizabeth. However, there is no indication that granting Roselle zone status would reverse its decline or attract new business to the area. Moreover, if zone status did attract substantial business investment, it is probable that part of the new business growth would result in a commensurate loss of economic development in Elizabeth and other surrounding towns. As the Bill Statement mentions, this has already happened, thereby providing the impetus to create a new zone in Roselle. There is no reason to believe that it will not continue in the future, town by town.

A perpetual cycle of economic cannibalization is inevitable when government creates a favorable tax situation in multiple districts scattered throughout a densely populated state such as New Jersey. Assuming a somewhat inelastic level of routine retail purchases, the greater the number of zones, the greater the negative effect of simply shifting economic growth from one municipality to another. The result must be a gradual but steady dilution of the economic benefits that served as the foundation of the 1983 Act. More zones will translate into less real benefit for each authorized zone. Although zones in the aggregate may show an increase in employment and business activity, it is likely that such increases are at the expense of the other municipalities of the state. It is also possible that some of the increases would have occurred regardless of the zone incentives.

There is a strong indication that the reduced sales tax rate benefit is not what drives the Urban Enterprise Zone program. Most people will shop where it is convenient, although the infrequent big-ticket purchases may be a reason to travel to a lower sales tax area. The reduced tax rate incentive creates severe administrative problems for zone vendors as well as marketplace competitive disadvantages for non-zone vendors. It also exposes the State to commerce clause challenges because the use tax rate in the zones must be equal to the 3% sales tax rate, while the general use tax rate in the state is 6%. Once the use tax rate is established at 3%, the state will eventually face a huge revenue loss from the purchase of goods from vendors outside of New Jersey (e.g. mail order, Internet sellers, wholesalers and distributors) and delivered to the purchaser within a reduced rate zone. In effect, the state will have created a de facto "enterprise zone" reduced tax rate for all businesses located everywhere, except those located in non-zone areas of New Jersey, where the use tax rate remains 6%. The negative implications for in-state non-zone businesses could be devastating.

Although the tax exemption on business purchases for use or consumption within a zone is a valuable incentive, not unlike others that currently exist in the sales tax law, for many of the large businesses moving into the zones, it is merely the "icing on the cake", the cake being the myriad of benefits that are completely unrelated to the zone program; for example, New Jersey's transportation and communication infrastructure, lower rents and operating costs, proximity to major markets, availability of labor pool, property tax incentives, low rate financing, etc.

As a matter of public policy, the expansion of the Urban Enterprise Zone program as it currently exists should not be encouraged. The Fiscal Impact Study conducted in 1998 for the Urban Enterprise Zone Authority by Response Analysis Corporation and Urbanomics supports the position that additional zones should not be designated until performance standards and minimum cost/benefit ratios are put into place for the entire program (Final Report, Section 1.5.4). To date, this has not been accomplished. Until this is done, there should be no consideration of further expansion of enterprise zones in New Jersey. In addition, consideration should be given to amending the provisions regarding the reduced rate benefit in order to diminish or eliminate its potentially adverse impact on in-state business activity and sales tax revenue.

RECOMMENDATION:

The Commission does not recommend enactment of this bill.

COMMISSION MEMBERS FOR PROPOSAL: 0

COMMISSION MEMBERS AGAINST PROPOSAL: 5

COMMISSION MEMBERS ABSTAINING: