Eight Concrete Ways to Curtail
the Economic War Among the States

by
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You could get very depressed thinking about how hard it is going to be to solve this crazy “candy store” mess. There are an awful lot of people with huge financial self-interests tied to the status quo: footloose corporations, site location consultants, accounting firms and tax consultants, industrial real estate brokers, mayors, governors, and building contractors.

Given how deeply entrenched this wasteful system has become, only an organizing approach to the problem can undo it. By organizing approach, I mean reforms that bring everyday taxpayers back into the process, that actively enable and encourage grassroots groups like community organizations, environmentalists and labor unions, as well as journalists and government watchdogs, to wade in. With all due respect to some who have proposed lawsuits or legislation that I would call “silver bullets,” I don’t think such ideas have a prayer up against a problem so deeply embedded as this one.

Reforms, of course, involve legislation. We need some new laws, but generally I favor fewer, simpler laws and stronger enforcement. Don’t forget, today’s candy store mess is a dream for lawyers and accountants, since it consists of so many hundreds of convoluted laws and tax gimmicks. We need a simpler body of laws that are based on common sense. Rules that everyone can understand and work with. Laws with clear intentions that courts cannot pervert.

Sunshine: The Best Antiseptic

The first two reforms we need involve disclosure. Taxpayers need to see how much money each company got – especially how much they got in tax breaks – especially corporate income tax breaks that are usually hidden from public view!

I’m adamant about disclosure because it’s the cornerstone of reform. Think about other major reforms the U.S. has enacted in the past 40 years.

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1 Good Jobs First, www.goodjobsfirst.org, is a non-profit, non-partisan research and resource center promoting corporate and government accountability in economic development and smart growth for working families; it is based in Washington, DC.
When community groups alleged that banks were discriminating against neighborhoods with people of color or older housing stock – that the banks were “redlining” their communities and denying loans to worthy borrowers because of their race or their address – they demanded and won the Home Mortgage Disclosure Act. That law requires banks to disclosure the number and dollar value of all of their housing loans every year, by census tract. The outrageous discrimination revealed by the data soon led Congress to pass the Community Reinvestment Act, which has enabled hundreds of community groups to win billions of dollars for neighborhood revitalization from many of the nation’s largest banks.

When community groups and labor unions alleged that chemical factories and other big polluters were endangering their health with toxic emissions, they demanded and won the Toxic Right to Know law, which requires companies to disclose what they emit and how much. Using that data, coalitions have won hundreds of agreements with companies to reduce emissions and otherwise improve local safety.

When the nation grew disgusted with Washington corruption during Watergate, taxpayers demanded to know who was giving money to politicians and how much. The resulting disclosure produces data compiled by the Federal Elections Commission. And while many people call our campaign finance system “legalized corruption,” at least we know who bankrolls whom. Obviously, if we did not have that data, none of the more recent campaign finance laws, like McCain-Feingold, could have taken hold.

Reform #1: State Economic Development Subsidy Disclosure

By disclosure, I mean annual, company-specific, public reporting of costs and benefits. How much did each company get? Which subsidy program did the money come from? What did the company do with the money? How many jobs did it create? How well do the jobs pay? Do they provide healthcare?

Seems pretty simple, doesn’t it? You’d think every state and city would be able to tell you those basic facts. But as we’ve seen in so many horror stories, most governors and mayors aren’t watching the store. Some even pretend to perform cost-benefit analysis by adding up their own press releases.

Already, 10 states have some form of economic development subsidy disclosure. The 10 states vary a lot in terms of the quality and completeness of their disclosure, but we certainly have enough experience now to talk about what works best. The 10 states are Connecticut, Illinois, Louisiana, Maine, Minnesota, Nebraska, North Carolina, Ohio, Texas, and West Virginia. (You can see details about each state’s disclosure law in Chapter 3 of our research manual, No More Secret Candy Store, at www.goodjobsfirst.org/research/ch3.pdf.)
Now, just because your state isn’t on the list doesn’t mean you can’t investigate. You can normally get quite a bit of information about deals in a state, especially if you are willing to wage a paper war under the state’s Open Records Act or Freedom of Information Act. With a lot of time and persistence (and possibly quite a bit of money for processing charges), you might be able to cobble together as much information as you could get quickly for free in a state with disclosure. But taxpayers shouldn’t have to wage a costly paper war with bureaucrats; they should be able to quickly and easily find out where their economic development money is going and whether their taxpayer investments are paying off. That’s what I mean by disclosure. Indeed, the information should be on the Web, just like it already is in some states.

Let’s look at an example. Minnesota is one of my favorite disclosure states. Although the Gopher State’s law does not cover corporate income tax breaks, it does cover lots of other subsidies – and the data is on the Web! Since its original law was passed in 1995 and improved twice later, thousands of Minnesota deals have been disclosed every year. Here is an example of one deal, in Caledonia, Minnesota.
<table>
<thead>
<tr>
<th>1. Funding government agency name</th>
<th>2. Contact name</th>
</tr>
</thead>
<tbody>
<tr>
<td>EDA</td>
<td>Troy Bankowski</td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th>3. Agency main address</th>
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</tr>
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<tr>
<td>231 E. Main St</td>
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<table>
<thead>
<tr>
<th>5. Zip code</th>
<th>6. Phone number (area code)</th>
<th>7. Fax number (area code)</th>
<th>8. Type of government agency</th>
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<tr>
<td>55921</td>
<td>507-724-3632</td>
<td>507-724-5258</td>
<td>Other (Please Indicate)</td>
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<table>
<thead>
<tr>
<th>9. Name of borrowing organization</th>
<th>10. Inquiry of preference (CIC page)</th>
<th>11. Type of assistance (e.g. loan, TIF, grant, infrastructure, etc.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Also Discount Stores</td>
<td>Dairy Queen</td>
<td>TIF</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>12. Source of TIF decision (if applicable)</th>
<th>13. Date project (if applicable)</th>
<th>14. Dan assistance firm (if applicable)</th>
<th>15. Dan assistance firm</th>
<th>16. Date project (if applicable)</th>
<th>17. Dan assistance firm (if applicable)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dairy Queen</td>
<td>11/20/98</td>
<td>pending</td>
<td>Dairy Queen</td>
<td>12/20/98</td>
<td>pending</td>
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<table>
<thead>
<tr>
<th>18. Average hourly wage (if applicable)</th>
<th>19. Average hourly wage (if applicable)</th>
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<tbody>
<tr>
<td>$4.50/hr</td>
<td>$5.15/hr</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>20. Actual average hourly wage paid to employees in each wage level and indicate the corresponding benefit level.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dairy Queen</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>21. Date Creation</th>
<th>22. Number of employees in each wage level and indicate the corresponding benefit level.</th>
</tr>
</thead>
<tbody>
<tr>
<td>9/19/97</td>
<td>Dairy Queen</td>
</tr>
</tbody>
</table>

<table>
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<th></th>
<th></th>
<th></th>
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<tbody>
<tr>
<td>Dairy Queen</td>
<td>Dairy Queen</td>
<td>Dairy Queen</td>
</tr>
</tbody>
</table>

An actual disclosure form from Minnesota: a company got a TIF (box 11) worth $275,515 (16) to create 1 new job (17) at Dairy Queen (12) paying $4.50 an hour (18).
So here we have a tax increment financing deal (box 11) worth $275,515 (box 16) to create one new job (box 17) at Dairy Queen (box 12) paying $4.50 an hour (box 18). Now, I don’t know how many ice cream cones they sell in Caledonia in February, I mean, I really hope that’s a full-year job. Healthcare? I doubt it. I suppose we should be grateful that the company is reporting an actual wage of $5.15 an hour, but then, that may be due to the federal minimum wage getting raised in the interim. But isn’t that an awfully big subsidy for a poverty-wage job? Until the state enacted disclosure, Minnesotans didn’t know there were deals like this happening.

Notice how unbureaucratic this disclosure system is. A city staff person fills in the top half of the form (based on its files from the original deal), then she calls the company and asks about jobs created and wages paid. Then she stuffs the sheet of paper in an envelope and mails it to the state Department of Trade and Economic Development in St. Paul, and DTED compiles the data into a spreadsheet. Or at least DTED used to compile the data on a spreadsheet that you could get under Freedom of Information, but since the forms have gotten a little longer, it just scans the forms into pdf and posts them on its website. You can see the last two years’ worth at www.dted.state.mn.us/02x05f.asp.

Of course, I prefer a state’s disclosure system to include corporate income tax breaks, and some already do. West Virginia has been reporting on every company that claims any major kind of corporate income tax credit for more than a dozen years. Maine has been disclosing three since it enacted disclosure in 1998. North Carolina enacted disclosure in 2002; you can see oodles of company-specific data at www.dor.state.nc.us/publications/williamslee.html.

I can hear the business lobbyists howling already. “This is invasion of taxpayer privacy. This will threaten small businesses. This will poison the business climate,” they’re crying. Well, to them, I say three things:

First, there is no evidence that any of the 10 states I have cited here have harmed their business climates by having disclosure. (Nor, for that matter, is there any evidence that any state has hurt its business climate with any other kind of reform I cite below, such as wage rules or money-back guarantee clawbacks.) As the person who has been out there publicizing these safeguards for 10 years, I think I would have been presented with such evidence if there was any, and I haven’t.

Second, no one said anything about invading anyone’s privacy or harming any small businesses. By disclosure, I am not talking about public release of any companies’ state income tax returns. I am not talking about seeing a company’s profits or losses, nor am I talking about disclosure of how much most companies paid in state income tax. But I do think that as a taxpayer, I ought to have the right to see how much a company claimed on a tax credit. Because when a company claims a credit and pays less income tax, it is the same thing as if the government wrote a check to the company for some other economic development purpose like a training grant. When a company claims an income tax credit, it means the company is paying less for public services, and I have to pay more, and I want to know how much more.
Third, lots of other kinds of tax breaks and subsidies are already public information. If a company gets a property tax abatement, I can usually go to the county tax assessor’s office and get the details pretty easily. If a company got a training grant, I can get that file at the Workforce Investment Board. If a company got a low-interest industrial revenue bond, I can go the county industrial development authority and get that information. Why should income tax credits be treated any differently? They were sold to us as “jobs, jobs, jobs,” so we should be able to see how much those jobs are costing, period.

Oh, yes, we need a little more info on the disclosure form. Will these jobs be accessible by public transportation? Does this deal involve a relocation? If so, from where and to where? Were the jobs accessible by public transportation before? Will they be accessible after the relocation? Otherwise, how do we know if the jobs are even available to low-income workers who cannot afford a car?

Reform #2: Disclosure to Corporate Shareholders of State Taxes Paid

Publicly traded companies (those that are listed on stock exchanges) already disclose how much they pay in federal income tax each year, in their annual reports and Forms 10-K. They also already disclose how much they pay in all state and local taxes, but they are only required to disclose the total from all 50 states in one aggregate number. So, for instance, it is not possible to determine, looking at General Motors’ Form 10-K, how much its taxes have gone up or down in Michigan the past dozen years.

The solution would be simple: require publicly traded companies to include a 50-state matrix in their Form 10-K showing how much tax they paid in each state. Breaking it down into three categories in each state would be best: income tax, property tax, and sales, utility and excise taxes.

This would surely produce data that would grab people’s attention. We already know from accountability campaigns in states such as Connecticut and New Jersey that many big companies there pay tiny amounts of income tax – as little as $200 a year, far less than low-income families – thanks to gimmicks like the Delaware royalty loophole.

If taxpayers learned that large companies in their state were paying almost no income tax, they would demand to know why, and that would inevitably lead them to question all of the tax gimmicks in the candy store. Indeed, a 1986 revelation by Citizens for Tax Justice that many huge corporations were paying zero federal income tax was memorialized in the famous bumper-sticker “I paid more income tax than General Motors, General Electric and General Dynamics combined.”
The ensuing outrage prompted a major progressive reform, closing some corporate loopholes; the 1986 law is considered the best thing to happen to the federal tax code in decades. But there has never been equivalent data about specific companies and their state income taxes. Lots of people suspect that corporations are paying less, but they don’t realize how little some really big companies are actually paying. Combined reporting would solve that.

Reform #3: Clawbacks, or Money-Back Guarantees

A clawback rule or contract simply says that a company must hold up its end of the bargain or else taxpayers have some money-back protection. Eighteen states and dozens of cities already use clawbacks, which basically say: after a certain period of time after a company gets a subsidy (say two years), it must create so many jobs at such and such a wage and benefit level. The clawback may also require other public benefits such as a certain number of dollars invested to modernize a facility. Then, if the company does not meet the targets, taxpayers get paid back. The rule can be prorated so that, for example, if the company falls 10 percent short, it has to pay back 10 percent of the subsidy; it can also be set for a steeper penalty, if the company falls far short.

I can hear the business lobbyists wailing again about poisoning the “business climate.” But I think just the opposite is true. From the mid-1980s to the mid-1990s, there was a string of lawsuits in which cities tried to get subsidy money back from companies that were shutting plants (Chicago vs. Hasbro/Playskool, Norwood, Ohio vs. General Motors, Duluth vs. Triangle, Yonkers vs. Otis Elevator, Ypsilanti Township vs. General Motors). The latter was best known: Ypsilanti Township alleged that statements made by GM in public hearings amounted to an oral contract obligating the company to stay in exchange for huge property tax breaks.

Now, given the prevailing business climate dogma, these lawsuits were huge events, with mayors risking their cities’ reputations for being friendly to business. The lawsuits speak to incredible frustration and anger, even desperation. If the cities had negotiated clawbacks with the companies, it’s unlikely there would have been any lawsuits, or angry statements or court pleadings. The companies’ obligations would have been spelled out in black and white – just like any private-sector contract – and there would likely never have been a dispute. Clear obligations on both sides of the table and no litigation: isn’t that a good business climate?

Reform #4: Job Quality Standards

Why give a company a subsidy and then allow it to pay a poverty wage? Lord knows the economy has been producing lots of lousy jobs all by itself. Subsidizing more only means
taxpayers get stuck with even higher, hidden costs – in the form of food stamps, Medicaid, Earned Income Tax Credit, and housing assistance. Thanks to the living wage movement – and to good old common sense – this reform is already taking root. As of our last updated survey, at least 43 states, 41 cities and 5 counties now attach wage and/or healthcare requirements to economic development incentives.¹

I hasten to add that while these numbers have risen sharply since I first started surveying for them in 1989, we still have a long way to go. Most jurisdictions still only apply these rules to one program – we found a total of 165 – but if the 50 states have an average of 30 or more subsidies each, or a total of at least 1,500, that means 89 percent of the programs still allow companies to pay, well, as little as that Dairy Queen in Caledonia, Minnesota.

Reform #5: Unified Development Budgets

About 35 states publish what is called a tax expenditure budget. That is, they provide the legislature with a report that says the state lost X dollars in revenue to A, B and C tax credits. But most of these reports are incomplete or unreliable. Incredibly, there is no standardized national set of accounting rules or guidelines for the states to track these expenses. (A group called the Government Finance Officers Association, which is the largest professional association of state and local treasurers and comptrollers, formed a committee to study the issue of subsidies in the late 1980s, but its work never went anywhere. The Government Accounting Standards Board, which sets guidelines for how governments should keep their books, has no firm rules telling states how to account for tax expenditures.)

It’s a big issue because tax expenditures for economic development (i.e., companies claiming corporate income tax credits or sales or utility tax exemptions that remain undisclosed) often dwarf other forms of spending such as grants that do show up clearly in budgets because they require appropriations. It’s no exaggeration to call appropriations the top of the iceberg and tax expenditures the bottom. So most state legislatures really are flying in the dark when it comes to the big picture. They don’t really know how big the bottom of the iceberg is, much less what they are getting for it.

The solution is a unified development budget, as advocated for by groups in Texas, California, North Carolina and Illinois. A unified development budget provides legislators with a comprehensive inventory of all forms of spending for economic development, including all the tax breaks as well as all the appropriations.

Although there is not yet much experience with this safeguard, the idea is sound. Give taxpayers and lawmakers a document that puts the whole iceberg on the table every year or two. A document that treats tax breaks no differently than appropriations, that portrays them both correctly as simply different forms of the same thing: state spending. And then let people decide
if they have the right balance. Chances are, with an accurate mapping of the whole iceberg, more people will turn their attention to the previously hidden bottom part, the secretive tax breaks, where most of the money is. Especially in times of budget deficits and fiscal strain, there is a better chance that legislators will look at both the top and the bottom as they seek to balance their budgets.

Reform #5: School Board Say on Abatements and TIF

As Good Jobs First documented in 2003, only two states effectively shield school funding from revenue losses caused by property tax abatements and revenue diversions caused by tax increment financing (TIF). A few states give school boards limited input or say, but the great majority give school boards no say in the process. It’s a big issue for school finance; although local revenue sources for schools are less important than they used to be, as states play a greater role, property taxes remain the largest single source of funding for K-12, and in some states, they still account for more than half. But with 43 states allowing abatements and 48 using TIF, the threat to school funding is present in every state.

It’s crazy public policy when you think about it. Voters elect members of the school board and expect them to meet their obligation to educate the kids. But then along comes a city council or a county board doling out abatements or TIF, eating the school board’s lunch. Call it an inter-governmental free lunch. What would the Department of Defense say if school boards had the unilateral power to grab some of its budget?

Protecting education funding matters doubly for economic development. Good schools are a key amenity that help cities attract and retain good employers, especially those that require highly skilled (read well-paid) workers. And with the Baby Boom generation approaching retirement, the growth rate of the U.S. labor force is plummeting, suggesting that we face chronic skilled labor shortages. For both these reasons, those states and regions with good schools will be the economic development winners of the 21st century.

School boards should have a full voting seat on any board that abates or diverts property tax revenue away from schools. And school boards should have veto power over that portion of property tax that would be lost to the schools in each specific abatement or TIF deal.

Reform #6: A Federal “Carrot” Against Job Piracy

The federal government often uses the power of its purse as a “carrot” to entice the states to reform their programs. A fraction of federal highway funding was held back from states until they lowered their blood-alcohol threshold to 0.8 percent for the definition of drunk driving. The
federal No Child Left Behind Act uses federal funds to encourage school reform (though many doubt its effectiveness).

There is no reason the same idea could not apply to economic development. Ten percent of a state’s money from the U.S. Departments of Commerce and Labor could be held back until a state adopted certain reforms. Just a few strategic ones would suffice: a certification by the governor that the state will not use taxpayer dollars to pirate jobs from another state, and adoption of disclosure and a unified development budget.

Reform #7: Properly Define Site Location Consultants as Lobbyists

Miriam Webster’s Collegiate Dictionary defines lobbying as “to attempt or influence or sway (as a public official) towards a desired action.” That sure sounds like the work of a site location consultant to me, since the deals they orchestrate routinely involve the passage of local ordinances for property tax abatements, industrial revenue bonds and/or zoning, and bigger deals sometimes involve state legislation as well.

Site location consultants work both sides of the street; that is, they work for companies looking for places and places looking for companies. It’s an apparent conflict of interest that allows them to profit by controlling the key information about a deal. It’s like a trial lawyer who represents children who got cancer from a nearby chemical plant also working for the chemical company. Or better yet, like a Black Jack dealer who knows what your down card is.

 Somehow, site location consultants have come to occupy a space where they defy norms about professional ethics and the proper representation of opposing parties. Let’s be clear: there are opposing interests at play here: companies want to pick the public pocket for every dime they can get, and public officials (or at least most of them) are trying to land the deal while spending as little as possible. But the bargaining table is sloped sharply because the site location consultant controls all of the information between the company and the sites competing for the deal. And in some cases, the site location consultant has a monetary self-interest in upping the ante of subsidies because he is working on commission of up to 30 percent of the value of those subsidies.

To help remedy this, states ought to legally classify site location consultants as lobbyists. In many states, that would require them to disclose at least a little about their activities. More importantly, it would block them from receiving success fees – read commissions – and thereby remove their most outrageous incentive to fuel the candy-store arms race.

The long-term objective here is to split the profession into two. Site location consulting ought to consist of fish and fowl, i.e., consultants who work for companies and others who work for
cities, counties and states. There should be a robust, adversarial process in which the taxpayers benefit from a side of the profession that specializes in aggressive bargaining, professional cost-benefit analysis, and cold market judgments about corporate behavior.

Reform #8: Promote Smart Growth and Curtail the “Economic War Among the Suburbs”

In some respects, the “war among the states” alarm bell is misleading. Far more common than state-vs.-state competitions for deals like the Boeing 7E7 are deals in which two or three jurisdictions within the same metro area compete for a deal. Indeed, in a study we did looking at 29 subsidized corporate relocations in the Twin Cities metro area, contemporary evidence indicates that only one company even considered locating just across the state line in Wisconsin. Most relocating companies cannot afford to move to another state; they want to retain their workforce, and stay close to their customers and suppliers. They simply need more space or a better location within the same metro area.

But because a small number of competitions that occur between states get a lot of media attention – since they are the more unusual event and since they include high-profile events such as new auto assembly plants – the public is unaware that intra-regional competition is far more common. Only four states – Connecticut, Ohio, Minnesota and Maine – collect information about subsidized relocations as part of their disclosure systems, and none has ever analyzed the data. To their credit, local development officials in some regions, by informal arrangements, seek to deter the use of subsidies to pay for relocations within their areas.

States should deny subsidies altogether to retail deals (except in truly depressed inner-city markets that are demonstrably under served, that lack basic retail amenities such as groceries, drugs and clothes). Retail is not economic development; it’s what happens if people have disposable income. (It has lousy upstream ripple effects – all those goods from China – and paltry downstream ripple effects, since retail jobs are overwhelmingly part-time, poverty wage without healthcare.) And big-box retail, which has become so expert at mongering subsidies, undermines existing retailers and a is primary cause of abandonment of urban core areas and the loss of open space at the suburban fringe.

States should also repeal point-of-sale sales tax collection rules. That is, they should not allow the city where a retail sale occurs to collect any share of the tax. Allowing one suburb to build a mall that sucks up sales tax revenue from the core city and dozens of surrounding suburbs simply undermines the tax base of older areas. And it creates a perverse incentive for another suburb to build yet another mall further out, and so the leap-frog sprawl continues. For the same reason, those states that allow sales tax to be “TIFed” should repeal it; that just puts the perverse incentive on steroids. In today’s spread-out metro areas, people live in one jurisdiction, work in another and shop in a few others. Sales tax revenues ought to be shared statewide and regionally, reflecting that reality.
In metro areas, states should explicitly link economic development to public transportation, requiring that to get a subsidy, the project must be accessible by transit (i.e., within a quarter of a mile of a regularly served transit stop). That would reduce companies’ ability to whipsaw suburbs against each other (by taking exclusionary suburbs out of the race), steer more jobs onto the transit system, help low-income families gain access to more jobs, give more commuters a choice about how to get to work, and improve air quality. In a 50-state survey, we found that not one state effectively coordinates any of its subsidy programs with public transit, even though the average state now has more than 30 subsidies. It’s a huge wasted opportunity for transportation dollars to leverage smart growth, since states spend five times more on economic development than on public transportation.3

Finally, states should deny development subsidies (as Maryland does under its Smart Growth Act) to any kind of deal that is not located in an area that already has infrastructure. Making developers bear the full infrastructure cost of sprawling fringe development helps tip the scales in favor of urban reinvestment. If land use policies bring jobs and tax base back to older areas, there will be less need for subsidies to revitalize them as well.
Endnotes

