HOW LOCAL GOVERNMENTS ARE (OR AREN'T) EXAMINING ECONOMIC DEVELOPMENT DOLLARS

by Mike Maciag

A new survey provides a detailed portrait of how local governments use business incentives, finding many lack basic accountability measures.

Just how effective tax breaks and other incentives are at boosting economic development is a crucial question states and localities should answer when they look to expand or renew programs.

Yet the extent to which local governments actually scrutinize economic development programs varies greatly, and many remain without basic accountability measures.

Most published research focuses on tax incentives at the state level, where the largest packages are typically awarded. A new nationwide survey [1] by the International City/County Management Association (ICMA), though, provides a detailed portrait of how local governments use business incentives and employ accountability measures.

For the most part, the survey of about 1,200 local governments and agencies suggests they are taking measures that, if done correctly, will help to ensure better returns on investment. Three-quarters of survey respondents reported measuring the effectiveness of business incentives, while 73 percent conducted cost-benefit analyses.

A smaller share (56 percent) reported always requiring performance agreements, while 27 percent had agreements in place for some incentives and 17 percent did not use them at all. Only 36 percent linked economic development priorities to budget processes.

It's more difficult to gauge how effective and reliable localities' practices truly are, though. Cost-benefit analysis is a particularly controversial area of economic development, for example, and such reports are often characterized by unrealistic assumptions or questionable methodologies.

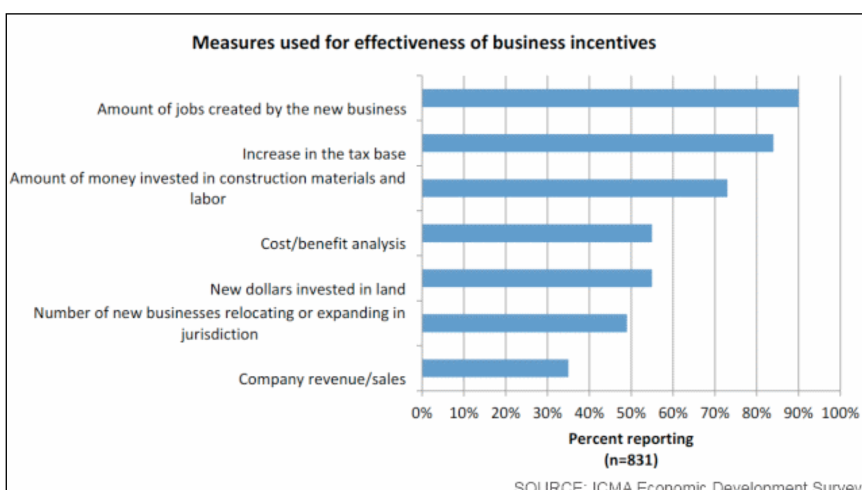
Daphne Kenyon, a fellow at the Lincoln Institute of Land Policy, said the survey results for both cost-benefit analysis and incentive measurement were better than she expected. One potential concern she cited was that some evaluations may be conducted by the economic development agencies rather than more objective outside groups.

Measuring the effectiveness of incentives is no simple task. Take, for example, job creation -- the most common measure used according to the survey. Tallying employment counts before and after an incentive is a far different matter than determining about how many jobs would actually be gained or lost absent an incentive.

"It all depends on who you ask and whether you're a tough judge of the numbers they give you," Kenyon said.

Still, going through the motions -- even if reviews are limited -- is better than doing nothing. "Just taking the sober view of looking at costs and benefits can be so vastly better than a naïve mentality," Kenyon said.

Kenyon recommends localities within a metro area work together and market themselves as a unit. Property tax incentives are relatively unimportant when companies first select a metro area, according to a Lincoln Institute



of Land Policy report[2], but they weigh more prominently in choosing a site within a region.

Compared to local agencies, states generally possess more resources to study incentive programs. But even so, a 2012 Pew study[3] found half of states lacked basic measures to inform policymakers on whether they provided an effective return on investment.

Evidence does suggest slightly more states and localities are starting to take a closer look at economic development. Compared to five years ago, responses for the ICMA survey ticked up a few percentage points for questions assessing use of cost-benefit analysis and measuring incentives' effectiveness. Several states responded to calls for greater transparency and scrutiny of incentives in recent years as well, passing legislation aimed at better evaluating programs.

"An increasing number of policymakers are recognizing the importance of measuring the results of tax incentives," said Josh Goodman, who researches state economic development incentives for Pew Charitable Trusts.

One reason Goodman said more states don't study tax incentives is that they're not part of the regular budget process. More, though, have moved to evaluate programs more regularly, he said.

Earlier this year, the District of Columbia Council approved a measure requiring its chief financial officer to review tax expenditures. It stipulated multiple considerations for analyses of economic development-related programs, such as taking into account whether outcomes would have been any different absent tax expenditures and how they may have been offset by economic losses elsewhere.

Pew has published a fact sheet[4] outlining how a few states evaluate their incentive programs.

Evaluations of incentives must consider their goals; not all economic development awards are designed primarily to spur job creation. Some target economic development around economically-depressed neighborhoods or in other areas, like transit hubs. Others may exist to raise revenue via property taxes.

One of the more common complaints levied against the subsidies is that only a few companies benefit. Using its subsidy tracker database[5], Good Jobs First estimated that at least three-quarters of total U.S. disclosed economic development dollars are awarded to only 965 larger corporations.

There is no comprehensive national tally of just how much states and localities have doled out. For this reason, it's hard to say the extent to which business incentives possibly increased in recent years. The ICMA survey, though, does suggest local incentive award packages generally are not growing, at least on average. The majority of responding governments (61 percent) reported average business incentive packages of about the same value as five years prior; 23 percent reported increases and 15 percent reported decreases.

Much of the data around economic development incentives tends to be fragmented. That could soon begin to change under new rules[6] proposed by the Governmental Accounting Standards Board (GASB) that require governments to report total resulting revenue loss. Some jurisdictions currently disclose much more than others, so the proposed requirements represent a significant shift that is likely to encounter resistance.❑

Mike Maciag is a Data Editor with *Governing Magazine*. This article is reprinted with permission from *Governing Magazine*, November 2014. Find the article on *Governing's* website at *http://www.governing.com/topics/finance/gov-economic-development-tax-incentive-survey-of-local-governments.html.*

End Notes:

1. *http://icma.org/en/icma/knowledge_network/documents/kn/Document/306723/ICMA_Economic_Development_Survey_Results_2014*

2. *http://www.lincolninst.edu/pubs/2024_Rethinking-Property-Tax-Incentives-for-Business*

3. *http://www.pewtrusts.org/~/media/legacy/uploadedfiles/wwwpewtrustsorg/reports/economic_mobility/PewEvaluatingStateTaxIncentivesReportpdf.pdf*

4. *http://www.pewtrusts.org/en/research-and-analysis/fact-sheets/2014/06/strategies-for-evaluating-tax-incentives*

5. *http://www.goodjobsfirst.org/subsidy-tracker*

6. *http://www.governing.com/topics/finance/The-Biggest-Effort-Yet-to-Make-Government-Tax-Subsidies-More-Transparent.html*