ITEP
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Policy Brief

Informing the debate over tax policy nationwide

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Fighting Back: Accountable Economic Development Strategies

Even though there is little evidence that cutting taxes and reducing public investments actually spurs economic development, lawmakers across the country have been persuaded to give tax breaks to companies in hopes of encouraging a thriving economic climate in their state. Some lawmakers are wising up to the idea that subsidies don't work. But for policymakers who insist on offering incentives, there are some important, simple, and concrete steps that can be taken to ensure that subsidies aren't allowed to go unchecked. This policy brief offers guidance on best practices for alternatives to providing blanket tax breaks.

Best Practices for Accountable Economic Development

The national nonprofit watchdog group **Good Jobs First** focuses on issues of economic development accountability and recommends a variety of best practices for lawmakers enacting tax breaks including:

- **Online disclosure of how much tax breaks cost state and local governments and what public benefits resulted from the tax breaks.** For example, lawmakers and the public should be able to determine how many jobs were created as a result of the tax breaks and whether the jobs created are "good jobs" in terms of the wages and benefits provided. This information should be made publicly available online and frequently updated. Illinois has a corporate accountability online portal designed to show the "development and employment commitments" of any entity that receives economic development money. Companies must submit documents describing how much money they received, how those funds were utilized to increase the number of people employed, whether the funds actually reduced jobs in another part of Illinois, and even the salary of employees. The Illinois website ensures that lawmakers, media, and the public are aware of how tax dollars are being spent.

- **Strict job quality standards should be applied to any tax break designed to increase in-state employment.** Requiring newly created jobs to provide a basic "living wage" along with health care benefits helps to avoid imposing hidden taxpayer costs on state and local governments. If a tax break results in a company hiring employees who are paid so little that they qualify for food stamps, Medicaid, or other taxpayer-funded safety nets, the cost of the tax break may actually exceed its benefits to the state. For example, in Montana companies receiving federal Workforce Investment Act training monies must pay wages and benefits of at least 110 percent of the state's median wage. On the other hand, the Democracy Resource Center in Kentucky found that in a two year period the state awarded tax breaks to 31 companies that actually paid workers an average salary that was below the federal poverty level for a family of four- taxpayer dollars were used to subsidize low quality jobs. Policymakers should place important standards on the types of jobs that can be created with public money.

- **Money-back guarantees that companies receiving tax breaks to create new jobs will create jobs that will remain in the state for some specified period of time and if they don't those tax breaks will be returned to the state.** These guarantees, known as "*clawbacks*," are now used in almost twenty states to ensure that lawmakers get enough "bang for the buck" for the tax breaks they offer. For example, Minnesota has strong clawback statutes, if a company receiving benefits doesn't fulfill the subsidy's requirements the company is banned from getting more aid for five years or until they have repaid the subsidy amount. According to Good Jobs First, clawback provisions can be written so that "different penalties apply depending on how badly a company fails to meet its targets." If for example, a company only creates 80 percent of the new jobs they promised to create when the subsidy was awarded, they could be required to return 20 percent of the state or local money they initially received. Clawback provisions are essential to ensuring that taxpayers actually receive a return on their investment.

- **Location-efficient incentives.** Tax incentives should encourage economic development in areas that are accessible to public transportation and shouldn't shift development from one part of the state to another. This creates more opportunity for low-income families who cannot afford cars and reduces traffic congestion. Good Jobs First suggests that, "Governments encourage sprawl when they allow subsidies to go anywhere (even when the result is a loss of farmland), and they pay companies to do what they would have done anyway (move outwards)." Ideally, protections would be put in place so that tax dollars couldn't be used to encourage sprawl.

- **Automatic review of giveaways.** Corporate tax breaks are often given without regard for how long the tax break will remain on the books. Automatically reviewing tax breaks and allowing them to expire, or sunset, is essential to ensuring that subsidies that aren't working are removed from state law. In 2006, legislation in Washington State was signed which ensures that tax preferences are automatically reviewed for their effectiveness and recommendations about those tax preferences are then given to the Legislature.

- **Encourage taxpayer involvement in the subsidy process.** Often times the process of offering subsidies is conducted behind closed doors with only corporate lobbyists and select state or local policymakers present. This typical process doesn't include taxpayers, media, or advocates. Allowing more public involvement in the subsidy process would ensure adequate oversight and offer taxpayers the ability to critique and examine how their tax dollars are being used. Good Job First correctly suggests that, "Residents have a right to know what projects are being considered, and are often better judges than public or company officials as to what constitutes "good" economic development in their area." The approval process should be as transparent as possible offering elected officials the opportunity to publically vote up or down on each individual proposed subsidy.

Accountable Economic Development Good for Everyone

Despite the flawed assumptions that economic incentives work, it appears that subsidies are here to stay. Policymakers and advocates should work to ensure that "strings are attached" to subsidies in the form of disclosure, job quality standards, clawbacks, automatic review, and transparency in the approval process. These reforms are essential to ensure that businesses don't take advantage of taxpayers.