GOOD-GOVERNMENT ADVOCATES ACROSS THE IDEOLOGICAL SPECTRUM ARE HOPING A NEW ACCOUNTING RULE WILL SHED LIGHT on the costs of property tax incentives for business, following years of public skepticism about the purported economic benefits of these tax breaks. Known as “GASB 77,” the Government Accounting Standards Board Statement No. 77 requires an estimated 50,000 state and local governments to report the total amount of tax revenue foregone each year because of incentives intended to attract or retain businesses within their borders.

Local governments have begun adhering to GASB 77 for the first time in their FY16 comprehensive annual financial reports (CAFRs), released in 2017. The disclosures will offer a vast new collection of data to elected officials, policy makers, researchers, and journalists looking to analyze the costs of business tax incentives and enable more accurate assessment of fiscal health in reporting jurisdictions.

Total business tax incentives have tripled since 1990, according to a report released in February by the W. E. Upjohn Institute for Employment Research (Bartik 2017). Author Timothy Bartik found that state and local governments spent $45 billion on total business tax incentives in 2015, including $12 billion a year on property tax abatements alone.

While many public officials offer business tax incentives for commendable reasons, critics claim these deals can conjure a brief illusion of prosperity but fail to offset the toll taken on fiscal health, both short- and long-term. Attracting new businesses to a jurisdiction can increase income or employment opportunities, expand the tax base, and revitalize distressed urban areas (Kenyon, Langley, and Paquin 2012). But opponents point to a growing body of research suggesting that incentives erode tax bases while spawning additional roads, sewers, and public services that governments must maintain and finance for the foreseeable future (Wassmer 2009, Marohn 2011).

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“Right now, the story about incentives is largely focused on the potential benefits of bringing in business, without much attention to the tradeoffs,” said Adam Langley, senior research analyst for the Department of Valuation and Taxation at the Lincoln Institute of Land Policy. “Disclosure has definitely increased in the past decade, but in a lot of places there’s still so little public information about the tax revenue lost because of incentives.”
The uniform disclosure of governments' financial information enables easy fiscal comparisons among states and public agencies, and it can inspire public confidence that a given government is conducting business with transparency and accountability. This confidence helps build and sustain healthy credit ratings, which allow governments to borrow cheaply.

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LAND LINES

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KANSAS CITY, MISSOURI

Business tax incentives gave rise to such corrosive competition within the Kansas City metropolitan area, which straddles the Missouri-Kansas border. Business executives were pitting local governments within the region against one another by threatening to relocate to the municipality that offered the sweeter deal. A particularly extreme economic development war between political jurisdictions on each side of the border got so bad in recent years that 17 business leaders wrote to the two states’ governors in 2011 and begged them to end the rivalry.

“The states are being pitted against each other and the only real winner is the business that is ‘incentive shopping’ to reduce costs,” the letter read. “The losers are the taxpayers who must provide services to those who are not paying for them.”

Don J. Hall, Jr., president and CEO of Hallmark Cards, has been a particularly vocal advocate for reform, to little avail. The Hall Family Foundation has calculated that, as of this spring, Wyandotte and Johnson counties in Kansas have sacrificed a combined $161 million in taxes to spur business relocations to Jackson County over the state line in Missouri. Meanwhile, Jackson County has spent $114 million to poach over 4,474 jobs from Wyandotte and Johnson counties in Kansas.

None of the combined $275 million was spent creating truly “new” jobs for the larger metropolitan area, notes Angela Smart, vice president of the foundation. “It’s corporate welfare in many respects, at the expense of eroding tax bases,” she adds.

Kansas City also suffers from a lack of transparency related to Tax Increment Financing (TIF). With TIF, growth in property taxes or other revenues in a designated geographic area is earmarked to support economic development in that area, usually to fund infrastructure improvements. Unlike property tax abatements, TIF does not lower taxes on business, but earmarking property tax revenue is an option in all TIF programs (Kenyon, Langley, Paquin, and Tuohey 2014). “We’ve created a fundamental right to real estate tax relief for developers and corporations in Kansas City,” said Kemper.

Michigan researchers Laura Reese and Gary Sands have found that tax incentives can actually perpetuate inequality between high- and low-income areas, because incentives go further in areas with higher income. The suburbs award tax breaks at a higher rate per capita than cities, promoting sprawl and making it harder for lower-income people living downtown to access the “new” jobs (Sands and Reese 2012). In Greater Cleveland, 80 percent of deals that followed the creation of community reinvestment programs involved businesses moving out of the city into Cuyahoga County suburbs, Good Jobs First found.

“I think GASB 77 will awaken some of the social justice warriors, because the inequality argument definitely has resonance,” said Kemper, who believes the annual dollar value of tax abatements and other government incentives in Kansas City could eventually hit $150 million. “This is money that’s being taken away from social services—from the most socioeconomically deprived folks in the community—to subsidize the most profitable people and corporations in the community. How could that possibly be fair?”
But Lincoln researchers, including Kenyon and Langley, criticized the lack of reliable information about property tax abatements that Franklin County taxpayers have at their disposal. The issue isn't the quantity of combined data released by local governments, the county, and Ohio state agencies; it's the quality, especially when it comes to calculating forgone revenue. For example, seven cities in the county provide basic information on incentive programs, such as eligibility criteria and benefits, but none report the cost of abatement programs. Others participate in Ohio's Online Checkbook, a transparency initiative where governments can report every expenditure and check issued. But it doesn't disclose individual property tax abatements or any other tax expenditures. The State of Ohio publishes a tax expenditure report, but it does not include property tax abatements.

Mingo would like to see tax incentives evaluated every few years. He hopes Franklin County can partner with surrounding counties in central Ohio to create a regional version of the Congressional Budget Office.

“Municipalities would do well to hire an independent authority to provide a cost-benefit analysis before awarding an abatement,” he said. “That is a worthy spend on behalf of taxpayers.”

The City of Columbus, Franklin's county seat, has offered a preview of the GASB 77 debates to come. In April 2017, Columbus became the second large municipality after New York City to release its annual financial report with disclosures required by GASB 77. The report revealed that 2016 tax abatements cost Columbus $1.3 million in forgone tax revenue (City of Columbus, 2017). But this figure did not include the nearly $31 million that was redirected last year to the city’s TIF districts.

City Auditor Hugh Dorrian said, “Governments, ours included, should disclose these various incentives. The more open governments are, the better they function. That’s why I’m very supportive of the principle behind GASB 77, even if there is disagreement over how to interpret it.”

Good Jobs First Executive Director Greg LeRoy noted that Dorrian, Columbus's auditor since 1969, had a stellar reputation for disclosing costs of tax subsidies long before GASB ever intervened. But in a written statement released last April, Good Jobs First chided the city for not counting the TIF payments and tax rebates as abatements in its 2016 CAFR.

“Columbus is the state capital and Ohio's largest city,” LeRoy wrote. “If it sets a flawed example, other jurisdictions might avoid disclosure of tax abatements and undermine this landmark transparency reform” (GJF 2017).

Regional Cooperation and Transparency in Denver, Colorado

Economic development officials in Denver have been devoted to transparency since the 1980s, and their experience suggests that GASB 77 may help public officials regain control over counterproductive business tax incentives by institutionalizing respect and trust on a regional level.

The guiding principle of Metro Denver’s Economic Development Corporation (MDEDC) is “more information is better than less.” Members are kept in the loop about economic development activity without compromising the confidentiality of business clients. The tradition dates to the oil collapse of 1986, which triggered an economic development fracas that had businesses essentially moving back and forth across the street, said Laura Brandt, economic development director for the MDEDC.

That experience drove a small group of local officials to decide that communities would work together under a common entity—what would eventually become the MDEDC—to promote the entire region first and individual communities second.

Members sign a Code of Ethics that has hardly been revised since the late 1980s. It’s a legally nonbinding document that acknowledges its own limitations. The preamble includes this sentence: “We fully realize that no Code of Ethics is of value without an inherent level of trust in the integrity of one another and a commitment from each of us to conduct ourselves at the highest levels of professional conduct” (MDEDC 2004).

Metro Denver’s Economic Development Corporation includes more than 70 governments, economic development organizations, and industry groups committed to a Code of Ethics that encourages regional cooperation regarding property tax incentives for business.

Credit: iStock.com/nick1803

Believe it or not, the Code of Ethics has worked. The MDEDC today includes more than 70 governments, economic development organizations, and industry groups. “People call all the time and ask, ‘How did you do this?’” Brandt said. “It wasn’t easy at first. But now it’s become a habit.”

Members who sign the code promise to notify another member community if a company located in the latter expresses an interest in relocating. Per the code, “Violation of this commitment shall be viewed as the single most serious breach of our membership pledge.” Breaking the code warrants a sit-down intervention of sorts with an MDEDC committee.

Companies interested in the Denver area are directed straight to the MDEDC, which then provides all member communities information about the type of property the company is looking for. The MDEDC introduces business decision makers to local officials only after it has narrowed potential sites to less than a handful.

“The model relies upon trust,” Leigh McIlvaine wrote in a 2014 Good Jobs First report. “Its members believe that the system will serve their communities fairly and feel confident that investments in neighboring communities will benefit their own as well” (McIlvaine and LeRoy 2014).
Improving Tax Incentive Programs

Besides promoting greater transparency and more regional cooperation, communities can improve tax incentive programs by taking a few clear steps, experts say. Limit the length of the tax abatement. Property tax deals tend to span more than 15 years, according to Bartik—considerably longer than other types of government-sponsored incentives. The longer the abatement deal, the less likely the government involved will ever collect full taxes on the property at hand. Plus, business executives are generally focused on a relatively short time frame—think stock options, fees that exceed the cost of providing new public services, once the tax deal is in place, so that government funds aren’t depleted?

If not, is the fiscal stress generated by the tax deal worth the benefits of jobs generation, potential neighborhood revitalization, and shot at additional businesses as a result of the multiplier effect?

GASB isn’t the first effort to improve transparency around tax incentives, nor does it offer a new-era subsidies transparency, or destroy value in places. But it does help the public with community tax abatement programs answer these questions with more than just instincts or wishful thinking.

Will additional exposure sway public opinion enough to spur meaningful reform? Or are local leaders and taxpayers hooked on the promise of incentives? Time will tell. André Wagaman is a business reporter for The Morning Call newspaper in Allentown, Pennsylvania. He can be reached by email at wagamanandrew@gmail.com.

REFERENCES


