

Oversight Division

Committee On Legislative Research

PROGRAM EVALUATION

Review of the
DEPARTMENT OF ECONOMIC
DEVELOPMENT
POLICY FOR ECONOMIC GROWTH

Program Evaluation
DEPARTMENT OF ECONOMIC DEVELOPMENT
POLICY FOR ECONOMIC GROWTH

*Prepared for the Committee on Legislative Research
by the Oversight Division*

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COMMITTEE ON LEGISLATIVE RESEARCH
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Members of the General Assembly:

The Joint Committee on Legislative Research adopted a resolution on June 20, 2011 directing the Oversight Division to perform a program evaluation of the Department of Economic Development, Policy for Economic Growth to determine and evaluate program performance in accordance with program objectives, responsibilities, and duties as set forth by statute or regulation.

The report includes Oversight's comments on internal controls, compliance with legal requirements, management practices, program performance, and related areas. We hope this information is helpful and can be used in a constructive manner for the betterment of the state program to which it relates. You may obtain a copy of the report on the Oversight Division's website at <http://www.moga.mo.gov/oversight/audits.htm>.

Respectfully,

A handwritten signature in cursive script that reads "Tom Flanigan".

Representative Tom Flanigan
Chairman

EXECUTIVE SUMMARY

The State of Missouri offers a wide range of tax credits as a part of its economic development program, and also offers tax credit incentives to participants in specific business and social activities. Applicants are generally required to make qualifying investments or conduct specific business or social activities in exchange for the credits.

Tax credits result in a direct reduction of a government entity's tax revenues. They are not an expenditure subject to normal budget and appropriation controls. Tax credits can provide direct financial assistance to a business or to an individual if the recipient of the tax credits has a tax liability. If the business or individual does not have a tax liability, the financial assistance may still be available by selling the tax credits but the financial assistance may be reduced due to broker fees or other transaction costs. However, some tax credits can not be sold or otherwise transferred and the benefit may be delayed or lost if the tax credits expire.

The Department of Economic Development (DED) and the Department of Revenue (DOR) are the primary Missouri state agencies involved in economic development tax credit programs, but additional state agencies are involved with other business or social tax credit programs.

Oversight reviewed the statutes, regulations, DED procedures, and other activities related to the economic development tax credit programs. We also reviewed a sample of recently active projects for which DED provided financial assistance. Our observations resulted in several comments and recommendations.

In our review of project files, we noted the files did not appear to be adequately organized and we could not determine if they were complete. We could not verify that DED staff had verified compliance with program requirements in some of the files. We recommend DED managers develop a standard format for project files, and ensure an annual file and compliance review is done by an appropriate manager. We also recommend DED managers develop a process to ensure more oversight over projects including more frequent project site visits.

We have significant concerns regarding compliance issues in three projects including the value of a contribution to a community development corporation, the shipment destination for computer equipment, and the wages paid to new employees on a project. We recommend DED managers reconsider the tax credits and other financial assistance provided to these projects and work with the Department of Revenue to recover any overpayments. Finally, we recommend consideration of a future program evaluation of the Missouri Development Finance Board, a component of the Department of Economic Development involved in large economic development project financing.

Chapter 1

Purpose/Objectives

The General Assembly has provided by law that the Committee on Legislative Research may have access to and obtain information concerning the needs, organization, functioning, efficiency and financial status of any department of state government or of any institution that is supported in whole or in part by revenues from the state of Missouri. The General Assembly has further provided by law for the organization of an Oversight Division of the Committee on Legislative Research and, upon adoption of a resolution by the General Assembly or by the Committee on Legislative Research, for the Oversight Division to make investigations into legislative and governmental institutions of this state to aid the General Assembly.

The Joint Committee on Legislative Research directed the Oversight Division to conduct a program evaluation of Missouri Tax Credit programs in 2009, and a report on that review was issued in January of 2010. Oversight was requested to update our review of these programs in 2010, to consider whether the technical and management requirements for these programs had been met, whether those requirements were adequate, and to review the potential for cost controls over these programs. On June 20, 2011 the Joint Committee on Legislative Research directed the Oversight Division to perform a program evaluation of the Department of Economic Development, Policy for Economic Growth, to determine and evaluate program performance in accordance with program objectives, responsibilities, and duties as set forth by statute or regulation.

Oversight's review addressed, but was not limited to, the following:

- * Determining the Department of Economic Development's policy for long-term economic development.
- * Comparing the nature and scope of Missouri tax credit programs with other states' programs.
- * Considering whether other states have overarching policies regarding tax credits.
- * Comparing the amount of tax credits issued and redeemed by Missouri and other states.
- * Considering the economic impact of tax credit programs to the state.
- * Reviewing the criteria used by the Department of Economic Development in selecting projects for discretionary tax credits.
- * Documenting the stated purpose for each tax credit program.

Scope

The Oversight Division reviewed information regarding tax credit programs active from 2005 through 2011.

Methodology

The methodology used by the Oversight Division included reviewing Missouri statutes, rules and regulations, and legislation and fiscal notes pertaining to tax credit programs. In addition, we interviewed personnel from the Department of Economic Development, reviewed the information available regarding financial and management review of the Missouri tax credit programs, and collected public information from other state tax credit programs.

Background

The state of Missouri has a wide variety of economic development programs designed to leverage our competitive advantages and deliver strong economic growth for Missouri.

The Missouri Department of Economic Development (DED) is the primary state agency devoted to the state's programs for business and community development. Programs managed by DED include small business incubator programs, specialized business loan programs, the Certified Site Program, state programs for the issuance of industrial development, infrastructure, and other bonds, programs allowing sales tax exemptions and employee withholding tax retention programs for new, expanding, or relocating businesses, special tax increment financing programs for infrastructure development, targeted employment training programs, and state tax credit programs.

Staff and responsibility for most of the department's economic development programs have been assigned to the Division of Business and Community Services (BCS). BCS is also the administrative agency for seven of the eight active tax credit programs which were created by the General Assembly to encourage business development in the state. The Film Tax Credit Program is jointly administered by DED and the Missouri Film Commission; the Business Use Incentives for Large-Scale Development (BUILD) program is administered jointly by BCS and the Missouri Development Finance Board.

The business development tax credit programs are as follows.

- * BUILD tax credits authorized by Sections 100.700 to 100.850; RSMo.
- * Business Facility tax credits authorized by Sections 135.100 to 135.150; RSMo.
- * Development tax credits authorized by Sections 32.100 to 32.125; RSMo.
- * Enhanced Enterprise Zone tax credits authorized by Sections 135.950 to 135.973; RSMo.
- * Enterprise Zone tax credits authorized by Sections 135.200 to 135.270; RSMo.
- * Film tax credits authorized by Section 135.750; RSMo.
- * Quality Jobs tax credits authorized by Sections 620.1875 to 620.1890; RSMo.
- * Rebuilding communities tax credits authorized by Section 135.535; RSMo.

Tax credits amounting to approximately \$41 million per year were issued for these tax credit programs over the most recent five years, or approximately 7.4 percent of all Missouri tax credits issued over those years. Total assistance provided by DED to active projects over the most recent five years was approximately \$205 million.

Department of Economic Development

The Department of Economic Development (DED) is composed of divisions, boards, and commissions which execute statutory requirements, develop program regulations, and implement policy in the areas of community, economic and workforce development. The divisions, boards, and commissions work with businesses and communities to help firms create jobs, increase sales, find and train qualified workers, identify sites, and obtain financing support to locate or expand in Missouri, promote capital investment, and increase the self-sufficiency of communities in the state.

The Department of Economic Development, Division of Business and Community Services (BCS) offers programs and incentives for businesses and communities to create a pro-business climate and strong community partnerships where businesses can thrive.

The Missouri Development Finance Board (MDFB) is an instrumentality of the state which reports administratively to the Department of Economic Development. MDFB is authorized by state law to grant tax credits equal to 50% of any moneys contributed by any taxpayer to one of three MDFB funds; the “Industrial Development and Reserve Fund,” the “Infrastructure Development Fund,” or the “Export Finance Fund.” The funds generated can then be used for new or expanding businesses.

The Missouri Film Commission was created in 1983 to attract film, television, video and cable productions to Missouri, and to promote the growth of the film and video production industry within Missouri. The Missouri Film Commission and the Department of Economic Development jointly administer the Film Production Tax Credit which may be up to 35 percent of the amount expended by film production companies in Missouri, for production or production-related activities.

A more detailed description of these tax credit programs is provided on Appendix A and a listing of all Missouri tax credits is provided on Appendix B.

Chapter 2

Application, Vetting, and Review Processes

We discussed with Department of Economic Development (DED) managers the processes the department has implemented to ensure financial assistance provided through these programs is properly used to improve the economic status of Missouri citizens.

A. Project Application and Vetting

We noted DED officials are actively involved in recruiting businesses which could benefit from these programs. The prerequisites for participation in these programs are provided in the statutes which authorize the programs, and although DED has published regulations for these programs, DED has only limited discretion in selecting projects. The DED application and vetting process for new projects in these programs is concerned primarily with examining the documentation for the proposal.

We are concerned these programs may be used to replace or supplement the normal capital requirements for the formation or operation of a businesses. This practice could lead to the state providing financial assistance to projects which could succeed without state assistance, or to projects which are not likely to succeed and to provide long-term jobs. We noted one of the projects we selected for detailed review resulted in jobs which lasted only the two years when state financial assistance was provided. The facility was closed at the end of its eligibility for assistance.

DED managers told us they try to prevent the excessive use of tax credits, and limit the amount of tax credits for each project to the lowest amount which will make the project feasible. They also told us they do not believe they have the ability to reject weak proposals or to shut down failing projects.

We also understand state financial assistance is sometimes provided as a direct response to financial incentive proposals from other states and DED managers are placed in the position of developing a “competitive” proposal for the employer.

We have discussed our compliance concerns with specific projects in another comment.

