Rep. Mark Larson 11/12/09

Page 1

The Council disagrees that the program cap was implemented as a safeguard to protect the State's resources, and feels that it serves to limit the potential for new economic growth. The Council also recognizes that they are not 100% infallible and states that, in addition to the 80% incentive ratio, the cost-benefit model is a safeguard. SAO recognizes that the cost-benefit model can be an effective tool for assuring that the public's dollars yield the greatest possible return. However, the cost-benefit model assumes the growth would not occur but for the incentive. In other words, the assumption is that the "but-for" decision is 100% correct all of the time. The safeguards are, in part, to mitigate the effects of incorrect decisions by the Council that are assumed to be 100% accurate by the cost-benefit model. That the funds paid out to applicants are outside of the budget review process is also relevant here.

Historical Growth vs Industry Average

We recommended that a company's historical rate of growth, if higher than industry average, be used in the cost-benefit model when it is available.

The Council disagrees with this recommendation stating that the use of different rates would be inconsistent and, therefore, violate statute; would put certain companies at a disadvantage; and would impose unnecessary inefficiency and additional cost to the program.

The discussion provided in the findings in regards to the use of the Historical growth rate versus the Industry Average rate is an opportunity to visit a recommendation for improved fiscal management of the program. As we indicated and VEPC reiterated in their comments to this finding, this has been the subject of much discussion when the original program was first implemented. If there has been recent debate of the alternatives this information was not in the memos provided to the SAO by a member of the Technical Working Group. However, SAO feels that this area should be revisited.

An argument that VEPC brings against using the background growth rate is that it would violate the statutory requirement that the cost-benefit model be applied in a uniform manner. Currently, there are different growth rates applied to applicants in the various industries which could be considered inconsistent when using the same logic as VEPC is suggesting. SAO is suggesting using the the industry rate when it is higher than the historical rate or where the historical rate is unavailable.

Another argument against its consideration given by VEPC is that this could favor certain companies over others. Using the industry approach does this as well. The two companies that were used for the examples we discussed in our finding which have significantly greater historical background growth rates than industry rates are large, well-established companies. The examples show how they are being awarded incentives for growth that would be occurring normally in those particular companies.

Using the historical background growth rate would better serve the intent of the General Assembly to not incent a company's normal growth. This message is given clearly in statute and even in the program information written by VEPC. In fact, even in the Council's response to this (page 74) they state that legislative intent is to not provide incentives for the first dollar of desired activity. VEPC indicates that the use of a 15-year rate fulfills this legislative intent but we have shown in our examples how this line of thinking is flawed. The incented activity using industry rates is based on the growth of all applicable companies, rather than solely a company's own growth rate.

Further, there need be no additional burden on the applicant. As stated in the report, SAO used information readily available in the Tax Department's records. There would, however, be some additional work for VEPC in calculating the historical rate. Again, as we have indicated, it is not difficult to do. This, however, should not be a deterrent for the use of a rate that will result in a more conservative use of public funds while still fulfilling the intent of the program.

Comparative Assessment of VEGI with EATI

In this section of the report, we considered the objectives of the new program and assessed whether the objectives have been met. We believe that the objectives have been met in regards to emphasizing job growth and more directly linking company performance to award payouts. We also believe it is premature to opine on the objective to minimize subjective award revisions. We feel that it is unclear whether the objective for the program to have equal or less fiscal expense to the State has been met due to the potential payout in the VEGI program as compared to the EATI program payouts.

The Council disagrees with our opinion that the VEGI program is potentially more expensive than the EATI program, saying that if the economic activity of a company within the VEGI program occurs then the result is that the State earns money. Here again, VEPC is disallowing the risk that the Council can be incorrect in its "but for" assessment by stating that if the activity occurs