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The Honorable Julia Lynn, Chair
The Honorable Mary Pilcher-Cook, Vice Chair
and Members of the Senate Commerce Committee

RE: Testimony for the Proposed Amendment for HB2006

Dear Sirs and Mesdames:

I am writing to you as a private citizen regarding the state economic development programs and oversight thereof, pursuant to the proposed amendments to HB2006.

I. My Background

While I testify solely in my private citizen capacity, I have substantial experience in capital markets which forms my understanding of financial reporting and portfolio management. For your reference, my credentials are summarized in **Exhibit A**.

II. My View of Economic Development Incentive Programs, in general

Before getting into the specifics of HB2006, I want to give you my overall thoughts about state economic development incentive programs. I am generally opposed to state tax policies which favor a particular industry, business, or developer. My views are based on both a **pragmatic outlook** (i.e. I don't believe incentive programs are generally *effective,* net of unintended consequences) and a **moral outlook** (i.e. I don't believe it is *morally* proper for the government – acting as a steward of taxpayers' money and with coercive authority – to provide economic incentives to a particular party that are not available to all taxpayers…and indeed, are sometimes funded by the beneficiary's taxpaying competitors).

Having a critical view of state economic development incentives is not a partisan issue; notions of "corporate welfare" should be troublesome to elected officials (stewards of taxpayer funds) regardless of political party or faction. At the state level, three high-level principles should be kept in mind with such programs:

a. **Moral fairness of tax policy:** Tax policy (or worse, outright cash grants) that benefit a particular party rather than all Kansas taxpayers is not morally fair.

Government should seek to minimize the bestowing of particular blessing or treasure on one party over another, in a free market economy.

b. **Cannibalization:** Cannibalization happens – often invisibly at a "macro level" – when state policies or programs enable a favored industry or business to put its in-state competitors out of business, or at least to impair its competitors as a result of receiving "favored status" through cash grants or tax preferences. Consider a tourist destination that received STAR Bond funding that draws families away other existing Kansas tourist/entertainment enterprises, or an insurance agency that receives PEAK grants which it uses to expand its workforce, which competes with non-PEAK competitors that are paying "full sticker price" on their Kansas taxes. It is very difficult to measure cannibalization, but it is an inevitable consequence of economic development incentives. This is related to the moral fairness principle, insofar as it is *morally* unfortunate for the state to cause cannibalization of taxpaying Kansas businesses.

c. **Subsidiarity:** This principle refers to the traditional American limited government concept that generally speaking, government should operate closest to home (government "pushed down" to subsidiary levels). For example, we have local dogcatchers rather than state dogcatchers; a state cosmetology board rather than a Federal cosmetology board, etc. The relevance to economic development policy is that the state should always consider, "why is this a state program rather than local?" Or said differently, "How do the taxpayers of Garden City benefit from such-and-such program that subsidizes a business or real estate developer in Olathe? If Olathe wants [such-and-such] so badly, let them pay for it!" (I'll pick on my hometown of Olathe.) In many cases with state economic development programs, the "subsidiarity principle" is often violated, with adverse consequence.

I hope that you consider these principles when evaluating Kansas state economic development programs, pursuant to HB2006 and in general. I believe that HB2006 will provide helpful tools to you as you evaluate the state's eco-devo programs.

III. Readily Available Critical Analyses of Tax Incentive Programs

Across the country, economic development incentive programs have grown tremendously in the past 20 years. Prior to the past 20 years, such programs scarcely existed at all, including in the state of Kansas (for example, the two Kansas programs that I am most familiar with are PEAK and STAR Bonds. These programs date to 2009 and 1998, respectively).

With the proliferation of such eco-devo programs, a growing body of analysis is already available to evaluate and critique such programs nationally. Please refer to my **Exhibit B** for a sample summary of such critiques, readily available for you to read.

IV. HB2006 summary

I am happy to see light shone upon the state economic development / tax incentive programs, pursuant to HB2006 and your committee's other activities. I hope that such light will provide you with information that you need as you consider these programs' efficacy in the future, and as you consider the proper role of state government and tax policy.

HB2006 generally prescribes an evaluation framework for the legislative post auditor to review the state's various economic development/incentive programs, and to submit its evaluation to the legislative post audit committee.

V. Positive Aspects of HB2006

a. As passed by the House
    a. Operates with the existing LPAC as the oversight body, thereby ensuring that a reasonable quorum of legislators are looking critically at the state eco-devo programs
    b. Provides for return on investment calculations, with visibility to the methodology used
    c. Would require a catalog of incentives to be maintained and publicly available in a centralized and visible place

b. Improvements as Amended
    a. The amended version of HB2006 that I received Thursday, March 7, includes a number of helpful improvements. Some of these are simply helpful clarifications (e.g. ensuring that records include businesses that are no longer solvent, ensuring that the Commerce webpage as discussed in the bill is permanently accessible, and ensuring that the data required by the bill is permanently preserved, not just preserved for three years).
    b. Several of the other amendments to HB2006 are more substantive and are very helpful, including:
        i. Eliminating the Commerce Secretary's ability to utilize his/her personal discretion regarding required reporting that may pertain to STAR Bond applications.

This is a critically important modification to the bill. The whole point of setting forth required standards for reporting is that you – the legislators, acting as fiduciaries for the taxpayers' treasury – define what you expect to see in the way of reporting from Commerce. I cannot think of data required by existing STAR Bond statutes or by the proposed bill that would be inappropriate to disclose to you and to the public at any time. I certainly can think of data that the developer or political subdivisions may not want to disclose (e.g. data that may demonstrate a lack of success with past projects), but that does not mean that it should be withheld. These programs are voluntary programs. No one has a right to the taxpayers' treasury, so if a STAR Bond applicant doesn't like the reporting requirements, they are free to not pursue funding from the program.

ii. Adding the requirement for the Commerce Secretary to personally appear before the appropriate legislative committees to present a report on the eco-devo programs.

In the capital markets world (banking and asset management), in-person presentations to oversight bodies is standard procedure. Such a practice adds a higher level of personal accountability for the person who ultimately "signs the deals" and who is charged with ensuring program compliance. This also gives the committee members the opportunity to ask questions to the Commerce Secretary. Overall, this rather simple requirement should add a high "return on investment" to the legislature, acting on behalf of Kansas taxpayers.

iii. Adding "teeth" in required reporting

The proposed amendments include "teeth" to enforce the reporting requirements under the various eco-devo programs. The "teeth" is a pause on new eco devo commitments while any reporting is delinquent. This structure is set fort beginning at the top with the Commerce Secretary and implemented on down the line at each level of operation. This is a very good addition to the eco-devo reporting.

VI. My Concerns with HB2006

With the version of the amendments that I have seen as of this writing (March 11 writing; March 7 bill amendment), I am concerned with the following provisions:

a. Insert A:
    i. Section d(2): I am not sure what a "literature review" is, and I am concerned that the inventory of similar programs in other states is too expansive of a mandate

ii. Sections 3(a),(b), and (c): I don't believe these are reasonable roles for an audit function, and are too broad in scope.
iii. Sections 5, 6, and 7: not an audit role; too broad in scope.

b. Insert B, New Sec. 4: developing policy guidelines for sales tax exemptions does not strike me as an appropriate role for the legislative post auditor.

c. Insert B, New Sec. 6: subsection (a) addresses incentives being used for intra-state relocation, and subsection (b) installs protections against cannibalization of retail within a 25 mile radius. Both of these provisions are addressing real problems with the various state eco-devo programs, but it should be noted that these provisions are well outside of the scope of HB2006, which deals with auditing and reporting, rather than with amending program requirements. While I applaud the spirit of these provisions, I would encourage your committee to pursue future legislation that specifically addresses program requirements on a program-by-program level, rather than attempting to address aspects of program requirements in a bill that otherwise deals with auditing and reporting.

VII. Conclusion

Thank you for the opportunity to present to you. I hope that you will consider my suggestions and get an amended version of HB2006 to the Governor's desk. Further, I hope that you will critically consider the macro considerations involved with using tax policy and subsidies as a tool for "economic development". As many of the studies cited in my Exhibit X conclude, the most effective tax policy is one that is simple, low, and uniformly applied to all appropriate taxpayers, rather than an approach that puts the government in the role of favoring certain parties at the expense of others.

Sincerely,

Clinton E. Anderson