St. Louis
Global Issues Testimony
9-21-10

Christine Harbin Global Issues Testimony

Grove East and Fox Park, and it's expanding out towards the city with buying and rehabing historic homes for low-income housing, and I'm proud to be a part of that.

I'm just here to say that I'm in support of Historic Tax Credit, what it's done for South Grand and the city of St. Louis and what it can do for our state. Thank you.

CO-CHAIR GROSS: Thank you very much, Rachel. Appreciate you being here.

MS. WITT: Thank you.

CO-CHAIR GROSS: Next is Christine Harbin. Welcome, Christine. Go ahead and spell your name for the record.

MS. HARBIN: Christine, C-H-R-I-S-T-I-N-E. Harbin, H-A-R-B-I-N.

My name is Christine Harbin, and I work with the Show-Me Institute. We're a free market think tank in St. Louis. We're dedicated to a free market solution for Missouri's public policy. And I'm one of the -- probably one of the only people here speaking against tax credit programs.

SENATOR WRIGHT-JONES: Can't hear you.

CO-CHAIR GROSS: A little louder. Speak up a little bit.

SENATOR WRIGHT-JONES: Thank you.

Harbin (cont)

MS. HARBIN: Okay. Thank you for allowing me address you here today. I commend your efforts to evaluate the appropriateness and the effectiveness of the tax credit program in Missouri. As I've just said, unlike many people who spoke before me, I am here to help explain why tax credit programs are a poor strategy for economic development in Missouri.

These programs defeat the purposes that supporters usually cite in their favor, which are encouraging employment and helping Missouri compete. In short, tax credits are a form of wealth redistribution. We all bear the cost, but only special interests and favored industries benefit.

Tax credit programs are not as effective as advertised. According to a recent audit by the state auditor, tax credits have less of an impact than predicted and cost more than anticipated. The state auditor's office reviewed 15 major tax credit programs in Missouri, and found that the fiscal notes underestimated the total cost of the programs by 1.1 billion over a five-year period.

Tax credit programs have also failed to delivery on their promises in other states. The Mackinac Center for Public Policy in Michigan released a study in which it compared job promises made in press releases issued by Michigan's economic development agency that were

Harbin (cont.)

accompanying tax credit awards to the actual outcomes of these programs. Mackinac found that only 7.9 percent of the projects were completed on time and produced the number of jobs promised. And this is a failure rate that Missouri can't afford.

Additionally, a particular program may provide social benefits, we've heard from many today. However, the state has to weigh this against the cost of the particular project.

As Governor Nixon said in his opening remarks to this Committee, the State has already made cuts in education and public safety. Whenever the State of Missouri awards a tax credit, that credit comes at the expense of other activities. This is because the State had a budge, and a dollar spent on tax credits, is a dollar the State must cut from other programs.

This Commission must consider whether the social benefits of, say, increased wine production or vacant land assemblage or Hollywood Film Production is worth cutting the budget of another state program. Are dollars spent on tax credits being used better than dollars spent on education, for example?

Furthermore, tax credit programs are an attempt by the government to pick winners and losers. The government has no special ability to predict which

Harbin (cont.)

businesses and industries will succeed. Yet, tax credits are an attempt to identify and subsidize future successes.

Unfortunately, in the game of picking winners and losers, the government also expect losers. This is because tax credits an attempt to protect companies and industries that the market has already rejected to some degree. If they were successful and viable on their own, these companies and industries wouldn't need to seek the favor of the government.

In addition, another recent state audit found that the Department of Economic Development had a 43 percent error rate just when recording estimated jobs and investment figures from the businesses receiving enterprise zone tax credits. In one instance, the DED inflated a business' investment estimate by 333 percent.

Given this amount of misinformation, how can the state possibly have a chance at encouraging the right businesses and industries? Government officials should not have a role in deciding who wins and who loses in the marketplace. They should allow businesses to fail under their own efforts and the preferences of consumers.

In addition, tax credits often don't make economic activity -- or they don't create economic activity, but instead they merely shift it to another location.

Harbin (cont.)

When states compete over companies by offering increasingly generous incentive packages, taxpayers lose because they have to foot the bill. We experience this in Missouri earlier this year with Ford. While the company lobbied for $150 million in tax incentives from the state of Missouri, Ford also courted Kentucky, Michigan, Ohio and Illinois for financial assistance, communicating the message that it would locate within the boarders of the highest bidder.

This is a very expensive game, and taxpayers everywhere would be better off if their state government stopped playing it.

Cutting the targeted tax credit programs does not imply not imply that economic development will halt in Missouri. On the contrary, there are many examples of it in Wisconsin and other states. Wisconsin, for example, has scaled back its film tax credit programs and is still able to attract blockbuster film productions all the same. American Express decided to build a $600 million data center in North Carolina without receiving a cent of subsidy.

Even if other nations, states or localities offer tax incentives to lure businesses, Missouri would be better off if we didn't do -- if we don't do the same, because we benefit from the lower prices that those

Harbin (cont)

subsidies create without it costing Missouri taxpayers a dime. It would be better for everyone if all states stopped providing these subsidies, but Missouri will still experience better economic growth if it unilaterally removed itself from the tax incentive bidding wars.

In summary, Missourians would be better off if the state government took a hands-off approach to economic development instead of providing subsidies to private companies.

Consumers would benefit because they'd be able to purchase goods at a lower cost instead of subsidizing private firms with their tax dollars. Producers in other industries would also benefit because they would not be forced to compete at an artificial competitive disadvantage. Missouri residents would be better off if state government widened the tax base by eliminating targeted tax credits instead of continuing to subsidize specific industries in the market. The region would be better off if its resources, human and otherwise, were employed in activities that do not require subsidies. As a direct consequence, the region would have the capacity to produce more and individuals in the market would be able to keep a greater percentage of their income.

Missouri's tax credit programs have not fulfilled their stated purposes and spending more on them

Harbin (cont.)

will not likely result in better outcomes. Missouri's tax dollars would be much better spent in the hands of individual Missourians than on enticements for companies like IBM and Ford.

If Missouri's state officials are serious about promoting economic development, they will stop attempt to pick and choose the economic activities that occur within its borders. The strategy didn't work for the Soviet Union, and it won't work for Missouri.

Thank you for the opportunity to speak to you today, and I'm happy to answer any questions that you have.

CO-CHAIR GROSS: I have two to start off with. One, there is a study that was talked about yesterday from the Wash U or St. Louis U.

MR. WOOD: St. Louis U.

CO-CHAIR GROSS: St. Louis U?

MR. WOOD: Yeah.

CO-CHAIR GROSS: Mike, do you recall who authored that study? Zach, do you recall?

MR. WOOD: It was e-mailed to us today. I don't know if you got it.

CO-CHAIR STOGEL: Yeah.

CO-CHAIR GROSS: Could you make sure I get your e-mail address or is it in the testimony?

Harbin (cont)

MS. HARBIN: It is. It's also on that, but I'd love to look at it.

CO-CHAIR GROSS: Yeah, I'd like to talk with you later about that.

MS. HARBIN: Sure.

CO-CHAIR GROSS: The second question is do you generalize tax credits, and are you more specifically referring to economic development tax credits, or all tax credits, including the social or --

MS. HARBIN: I --

CO-CHAIR GROSS: -- contribution tax credits?

MS. HARBIN: My emphasis -- my emphasis is on the financial tax credits; however, I also say in my testimony that there is a cost associated with everything. And I think we need to be mindful of the expenditure and how it's being used for all tax credit programs. So I am speaking generally.

CO-CHAIR GROSS: Because in fairness to -- I'll just now address the social credit side of things for a second. In fairness, you know, when we were visiting before this meeting and talking about the role that the agencies play in everything from senior citizens, to disabled, and young, you name it. The social services industry in Missouri fills a large gap.

Harbin (cont.)

If they weren't there -- I mean, I've always looked at it we could either hire a bunch of state employees to do that, or we can kind of privatize it and encourage them to do it as a group somewhat in the private sector in the social services area to do it. But either way, it's going to happen, and I don't know which is the most efficient. I think probably the way we're doing it is a little more efficient. They get some of those private dollars to come into those agencies which you wouldn't get except for through taxes if -- if we were going to direct that as a state.

But either way, you know, there's XI, but the rest I didn't know if you were, like I said, lumping it in the social credits along with the economic credits, because when you say financial, I don't know exactly what you mean when you say financial.

MS. HARBIN: Well, the social and financial tax credits, I think you're categorizing them similar distort behaviors of individuals in a private economy.

CO-CHAIR GROSS: Say that again. Sorry. Go ahead.

MS. HARBIN: The -- the social and financial tax credit programs that you're lumping them have similarly distortionary effects on consumers and their

Harbin (cont.)

behavior in the private market.

CO-CHAIR GROSS: How do the social credits -- how do they have a distortion?

MS. HARBIN: Well, the social credits, for example, have to be made somehow, and so they're diverting money from alternative uses within the state government from the state budget.

CO-CHAIR GROSS: Okay.

MS. HARBIN: And I planned to ruminate on this with Mike would be better as well.

CO-CHAIR STOGEL: I was just going to ask for something similar. There's a list of 61 programs at -- well, I'll give you the 61 programs, and maybe you can target your comments to the social programs. That would be Bill Hall's committee, or the economic development ones or the low-income one the historic one.

I'm not trying to put you on the spot, but to the extent you've covered in your testimony the whole spectrum, it would be helpful for the Commission to digest how you view this market approach is working better as to which programs.

MS. HARBIN: Sure.

CO-CHAIR STOGEL: And maybe your conclusion is there's 10 or 15 or 20 to which this should apply and the recommendation would be to end those

Harbin (cont.)

programs. That would be legitimate testimony, but reacting to something as broad-based -- this is just helpful to us. It's nothing specific, so I'll give you --

MS. HARBIN: Why don't I --

CO-CHAIR STOGEL: I'll give you -- I'll actually give you a disk with all the programs on it, and you can get back to us where you think this applies and give us some more jobs. That would be helpful.

CO-CHAIR GROSS: Anyone else? Did you have anything else, Christine? Is that all?

MS. HARBIN: Yeah, that's fine at this time.

CO-CHAIR GROSS: Okay. Thanks for being here. Next on the list is Peter George. Welcome, Mr. George. Go ahead and spell your name and proceed.

MR. GEORGE: My name is Peter George. And it's G-E-O-R-G-E.

Commission members, thank you for your time today. I am here to speak to you as a fourth generation St. Louisian and as a developer.

During previous conversations with the Commission, there were four goals that were outlined by Governor Nixon for the Commission to consider when reviewing the benefits of the State's tax credit programs for Missouri. And they were preserve Missouri's triple A

TESTIMONY

SEPTEMBER 21, 2010

SHOW-ME INSTITUTE

ADVANCING LIBERTY WITH RESPONSIBILITY BY PROMOTING MARKET SOLUTIONS FOR MISSOURI PUBLIC POLICY

TAX CREDITS:

A POOR STRATEGY FOR ECONOMIC DEVELOPMENT

by Christine Harbin

To the members of the Tax Credit Review Commission:

Thank you for the opportunity to address you today. I commend your efforts to evaluate the appropriateness and the effectiveness of tax credit programs in Missouri. I want to use my time today to explain why targeted tax credit programs are a poor strategy for promoting economic development in Missouri.

These programs defeat the purposes that supporters usually cite in their favor: encouraging employment and helping Missouri compete. In short, tax credits are a form of wealth redistribution — we all bear the cost, but only special interests and favored industries benefit.

Tax credit programs are not as effective as advertised.

According a recent audit by the state auditor's office, tax credits have less of an impact than predicted and cost more than anticipated. Montee reviewed 15 major tax credit programs in Missouri, and found that the fiscal notes underestimated the total cost of the programs by $1.1 billion over a five-year period.

Tax credit programs have failed to deliver on their promises in other states, too. The Mackinac Center for Public Policy in Michigan released a study in which it compared job promises made in press releases issued by Michigan's economic development agency accompanying tax credit awards to the actual outcomes of those programs. Mackinac found that only 7.9 percent of projects were completed on time and produced the number of jobs promised. Missouri cannot afford that failure rate.

A particular program may provide some social benefits, but the state has to weigh this against the cost of a particular project.

As Gov. Jay Nixon said in his opening remarks to this committee, the state has already to made cuts in education and public safety. Whenever the state of Missouri awards a tax credit, that credit comes at the expense of other activities. This is because the state has a budget. A dollar spent

Christine Harbin is a research analyst for the Show-Me Institute.

Government officials should not have the role of deciding who wins and who loses in the marketplace. They should allow businesses to succeed or to fail as a result of their own efforts, and the preferences of consumers.

on tax credits is a dollar that the state must cut from another program. This commission should consider whether the social benefits of, say, increased wine production or vacant land assemblage are worth cutting the budget of another state program. Are dollars spent on tax credits being used better than dollars spent on education?

Tax credit programs are an attempt by the government to pick winners and losers.

The government has no special ability to predict which businesses and industries will succeed. Yet tax credits are an attempt to identify and subsidize future successes.

Unfortunately, in the game of picking winners and losers, the government almost always picks losers. This is because tax credits are an attempt to protect companies and industries that the market has already rejected to some degree. If they were successful and viable on their own, these companies and industries wouldn't need to seek the favor of the government.

In addition, another recent state audit found that the Department of Economic Development (DED) had a 43-percent error rate just when *recording* estimated jobs and investment figures from businesses receiving enterprise zone tax credits. In one instance, the DED inflated a business' investment estimate by 333 percent.

Given this amount of misinformation, how can the state possibly have a chance at encouraging the right businesses and industries? Government officials should not have the role of deciding who wins and who loses in the marketplace. They should allow businesses to succeed or to fail as a result of their own efforts, and the preferences of consumers.

Tax credits often don't create economic activity, but instead merely shift it to another location.

When states compete over companies by offering increasingly generous incentive packages, taxpayers lose because they have to foot the bill. We experienced this in Missouri earlier this year with Ford. While the company lobbied for $150 million in tax incentives from Missouri, Ford also courted Kentucky, Michigan, Ohio, and Illinois for financial assistance, communicating the message that it would locate within the borders of the highest bidder. This is a very expensive game, and taxpayers everywhere would be better off if their state governments stopped playing.

Cutting the targeted tax credit programs does not imply that economic development will halt in Missouri. Wisconsin, for example, has scaled back its film tax credit program and it is able to attract blockbuster film productions all the same. American Express decided to build a $600 million data center in North Carolina without receiving a cent of subsidy.

Even if other nations, states, or localities offer tax incentives to lure businesses, Missouri would be better off if we don't do the same — because we benefit from the lower prices that those subsidies create, without it costing Missouri's taxpayers a dime. It would be better for everyone if all states stopped providing these subsidies, but Missouri will still experience better economic growth if it unilaterally removes itself from the tax incentive bidding wars.

Tax credits represent a future financial liability for the state.

This is because many credits do not have to be redeemed in the year that they were issued. This negatively affects Missouri's ability to recover from difficult economic times, because officials will have to dole out money at unexpected intervals in the future. When these tax credits are redeemed in the future, it could cause the state to run a deficit, or exacerbate an existing deficit. Even if Missouri were to scale back or eliminate its incentive programs, it could still end up paying out credits in the future as they are redeemed. The uncertainty of when these tax credits will be redeemed makes it difficult for policymakers to forecast and plan future budgets. The tax credits will be redeemed at some point — just not necessarily during the same year that they were issued.

Missourians would be better off if the state government took a hands-off approach to economic development instead of providing subsidies to private companies.

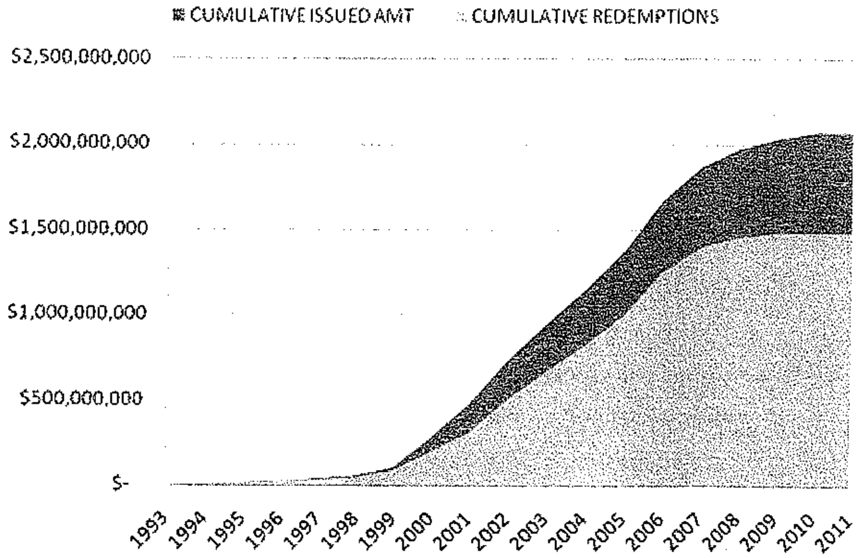
Consumers would benefit because they would be able to purchase goods at a lower cost instead of subsidizing private firms with their tax dollars. Producers in other industries would also benefit, because they would not be forced to compete at an artificial competitive disadvantage. Missouri residents would be better off if the state government widened the tax base by reducing rates and eliminating targeted tax credits instead of continuing to subsidize specific industries in the market. The region would be better off if its resources — human and otherwise — were employed in activities that do not require subsidies. As a direct consequence, the region would have the capacity to produce more, and individuals in the market would be able to keep a greater percentage of their income.

Missouri's tax credit programs have not fulfilled their stated purposes, and spending more on them will not likely result in better outcomes. Missouri's tax dollars would be much better spent in the hands of individual Missourians than on enticements for companies like IBM and Ford.

If Missouri's state government officials are serious about promoting economic development, they will stop attempting to pick and choose the economic activities that occur within its borders. This strategy didn't work for the Soviet Union, and it won't work for Missouri, either.

For more of the Show-Me Institute's research about tax issues, visit www.showmeinstitute.org.

Cumulative Total Issued & Redeemed



Even if other nations, states, or localities offer tax incentives to lure businesses, Missouri would be better off if we don't do the same — because we benefit from the lower prices that those subsidies create, without it costing Missouri's taxpayers a dime.

SHOW-ME INSTITUTE POLICY AREAS

TAXES

Our economy works better when the tax system is simple, fair, and lets workers keep more of the money they earn. Show-Me Institute scholars study the impact of tax and spending policies, and develop reforms that will give us more for our tax dollars and spur faster economic growth.

EDUCATION

The latest education research confirms what common sense has always told us: Kids learn better when their parents have more choices. The Show-Me Institute studies how to empower parents by expanding educational options and providing them with better information, so that every child can attend a school that best meets his or her unique needs.

CORPORATE WELFARE

From eminent domain abuse to subsidies and tax breaks for the powerful and well-connected, government officials often try to pick winners and losers in the market. The Show-Me Institute develops policy recommendations to protect property rights and promote economic growth without caving in to demands for corporate welfare. Secure property rights encourage investment and entrepreneurship. Trying to create economic success through government intervention is a formula for failure.

HEALTH CARE

The standard employer-based model for health insurance leaves a remarkable number of people out. The Show-Me Institute highlights the ways that a consumer-driven, market-based model for coverage can help more people get the care they need while taking ownership for their own health and lifestyle decisions.

PRIVATIZATION

Many government services can be provided more effectively, and at a lower cost, by the private sector. When public services are provided by private industry, economic incentives and accountability provide a critical feedback loop that is largely absent in government bureaucracy. Show-Me Institute scholars analyze public programs to determine how taxpayers can benefit from market-based alternatives.

RED TAPE

One thing that government officials do well is establish barriers to market innovation and erect hurdles for entrepreneurs to clear. The Show-Me Institute is committed to showing how burdensome regulations stand in the way of economic growth and individual prosperity. Market solutions lose their strength when bound by red tape.

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Commentary
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Missouri's Development Tax Credits Cost Too Much, Deliver Too Little

By Christine Harbin

SHOW-ME INSTITUTE
MARKET SOLUTIONS FOR MISSOURI

Summary

In difficult economic times, it's more important than ever to scale back tax credit programs that single out companies or industries for favored treatment. Legislators don't have a special ability to predict which company or industry will maximize revenue or economic growth, so the cost of such credits to taxpayers will almost certainly exceed the benefits.

Main text word count: 568

By reducing the tax burden of a single targeted industry or company, the marginal tax rate for everybody else necessarily increases if overall government spending is not also reduced.

In a recent *Post-Dispatch* op-ed ("Tax credits work for Missouri," June 17), Donald Rosemann argues that tax credits create jobs and promote economic development, and also suggests that historic preservation tax credits in particular have been very successful. Unfortunately, he overlooks everything that Missourians lose when the state hands out billions to favored industries.

Rosemann claims that tax credit programs are "too important for St. Louis and Missouri to scale back — especially in difficult economic times." To the contrary, difficult economic times are exactly when the state can least afford to give tax credits to select firms and businesses. Tax credit programs place an additional burden on taxpayers who are already hurting. A particular tax credit may provide some benefits, but the state has to weigh these against the costs of the program, which are much more difficult to anticipate fully.

Additionally, because many credits do not have to be redeemed in the year that they were issued, tax credits represent a future liability for the state. This negatively affects Missouri's ability to recover from difficult economic times, because officials will have to dole out money at unexpected intervals in the future.

Targeted tax credits discourage economic development in the state by hurting businesses in non-favored industries. Legislators don't have a special ability to predict which company or industry will maximize revenue or economic growth, so the cost of such credits for taxpayers will almost certainly exceed the benefits. By shifting the tax burden from one favored party to others, targeted tax credits force everyone else in the market to compete at a disadvantage, and an uneven playing field is not an optimal economic climate for fostering development. By reducing the tax burden of a single targeted industry or company, the marginal tax rate for everybody else necessarily increases if overall government spending is not also reduced.

A recent report from Missouri's state auditor found that tax credits have less of an impact than predicted and cost more than anticipated. The report reviewed 15 major tax credit programs in

continued on back

Missouri, and found that the total cost of the programs had been underestimated by $1.1 billion over a five-year period. Furthermore, many of these tax credit projects include property tax abatements, so those developments won't bring additional tax revenue for state and local governments to fund schools and other essential services.

Proponents of tax credits fail to consider the many other types of economic activity that could have come into existence had the taxpayers of Missouri been allowed to keep and invest their billions. A factory and a renovated historical building are easily seen effects of tax credits; however, the unseen negative effects include those products and services that were never purchased or consumed in the private sector, because public officials spent the money that would have paid for them.

When the state carves out sections of its tax base in order to reduce the burdens for a select few, everybody else has to pick up the difference. Broad tax cuts are preferable to tax credits because they bring growth to the entire economy, rather than only to those lucky or connected enough to be singled out for special treatment. A lower-tax environment for everybody would attract new businesses and individuals to Missouri more efficiently and effectively. Missouri's tax credit programs have not fulfilled their stated purposes, and spending more on them will not likely result in better outcomes.

Christine Harbin is a research analyst at the Show-Me Institute, a Missouri-based think tank.

Broad tax cuts are preferable to tax credits because they bring growth to the entire economy, rather than only to those lucky or connected enough to be singled out for special treatment.

Attention Editors and Publishers

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