

Report on the Effectiveness of Local Economic Development Planning in Lawrence and Douglas County, Kansas

Lawrence-Douglas County League of Women Voters
Local Economic Development Study Group

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Draft of February 11, 2015

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Abstract

The League of Women Voters Local Economic Development Planning Study Group examined the effectiveness of local economic development planning in Lawrence and Douglas County, Kansas. It finds that the City and the County have been led into ineffective programs and poor investments due to poor organization and leadership in the field of economic development. The current process relies on the Chamber of Commerce to guide the City and County in its economic development projects and programs. The guidance from the Chamber has been flawed and poorly informed. Local economic development can be effective if it is guided by professionals in the field who possess a strong, research based knowledge of how to assess conditions, design strategies and implement projects and programs. These professional need to serve the community as a whole, rather than just the business interests. The Chamber is not staffed with such professionals. It is recommended that the City and County end its contract with the Chamber of Commerce and expand the professional economic development expertise of its own staff.

Introduction

Practical Realities of Economic Development

Thousands of communities across the nation are engaged in economic development, yet only a few hundred firms will build significant new facilities in any single year. This means that the job growth rate in Lawrence will largely be driven by the natural expansion and contraction of existing firms and only rarely will a new firm be added to the mix.

Manufacturing is declining in Lawrence as it is for the nation as a whole. While manufacturing jobs pay well, Lawrence is going to lose its share of these jobs, and the return of these jobs is not likely in the foreseeable future.

Lawrence should avoid repeating the mistakes that it and

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other communities have made in the past in the false belief that economic development efforts improve the competitive position of the city in attracting tourists, new residents, and new businesses. At best, economic development efforts can make the advantages Lawrence has to offer more widely known. Lawrence should continue to improve the quality of its work force, seek to raise the wage levels of the work force, and seek to make Lawrence a community where everyone wants to live.

Definition of Economic Development

It is important to understand the definition of economic development. Economic development is the expansion of the total income of a community by importing more dollars for locally produced goods and services. Expanding the total income means attracting more dollars into the community from outside the community. This can be through attracting tourists or new retirees, attracting new customers who live outside of the community to businesses already in the community, attracting new businesses to the community that sell their products or services outside of the community, or any action that raises the wages of the labor force by bringing dollars into the community.

The most essential ingredient for successful economic development is the maintenance and development of a high quality of living in the community. This means making the community a place where people want to live, where workers are well educated and well paid, and where firms want to do business.

Necessary ingredients for successful economic development

Labor

A community must have a good balance between the demand for labor and the skills of the labor force.

Warehousing requires little or no training. Manufacturing usually requires a well-trained labor force. Professional services can require a highly educated labor force. Lawrence generally enjoys a highly educated labor force. In the U.S. 16% of adults did not complete high school; in Lawrence only 4% did not complete high school. In the U.S., 25% of adults have a college degree; in Lawrence it is 35%. We need to seek employment opportunities that match the composition of the labor force.

Economic development is the expansion of the total income of a community by importing more dollars for locally produced goods and services.

A community has to have the right quantity and quality of labor available. If the labor force is too small or not available, then the community will not be attractive. This is usually not a big problem as most new firms are looking for only a small number of employees. Douglas County contains 47,000 workers; most new firms will add fewer than 100 employees. A workforce of this size can easily absorb this type of growth.

The labor in a community has to be competitively priced. Unfortunately, Lawrence excels in this dimension. Wages in Lawrence are low in virtually all occupations. Thus, wages are not held down by student labor; wages are low across all sectors including those that admit only skilled workers beyond student age. This makes Lawrence attractive to firms, but sadly it is making Lawrence unattractive to workers.

Land

A community needs to have an adequate supply of appropriately serviced land available. Adequate means the right amount, not too much and not too little. Too often communities are led into preparing large quantities of land that only sits idle. It is unwise to develop more land than can be reasonably absorbed within a decade or two.

No self-contained community like Lawrence is going to attract an extremely large employer needing a very large site. A firm employing thousand or more workers will not locate in Lawrence because the workforce cannot deliver this many workers and Lawrence does not have adjacent communities to provide additional workers on this scale. Virtually all of the firms moving into Lawrence over the last two decades developed on parcels of 25 acres, more or less. While new land for future employment centers may be needed, it is doubtful that the number of acres needed cannot be accommodated by existing sites and by the Venture Park site. Remember that the University of Kansas remains the largest employer, and it has provided for its own growth. The community only needs to provide for the non-University growth.

Loans

A community is often called upon to provide financing for business expansion and development. As long as this is done in a way that minimizes or eliminates the risk to the taxpayers, this can be a successful tool to facilitate economic development.

Public sector loans can subsidize a development, but they cannot create demand for the product or service to be produced. It is important to remember that subsidized financing can help a good investment succeed, but it will not turn a risky investment into a safe one. Cautious underwriting is required.

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Many things do not work

Tax abatements

Property taxes comprise such a small portion of the operating expenses of manufacturing or research and development facilities that abatements cannot influence a successful firm's location decision. Property tax abatements are an ineffective waste of scarce resources. They have failed in Lawrence (under Chamber of Commerce leadership), and they have failed elsewhere.

Speculative development

Building structures on a speculative basis is highly risky. Too often they sit empty and lose money. This has been the case in Lawrence (again, under Chamber of Commerce leadership).

Equally, a community must avoid speculative provision of expensive infrastructure in the hope of attracting new development. Lawrence has often failed in this area as well.

Free land

The price of land in the Midwest is sufficiently inexpensive that it does not influence the location decision of firms. Note that Abilene provides free land but has a job growth rate below that of Lawrence, while Johnson County charges high land prices and has a much higher job growth rate higher than that of Lawrence.

Hasty planning

The amount of time it takes to plan and develop a project in Lawrence is comparable to the time it takes in other communities. It is not true that Lawrence takes longer; this is a myth pushed by those who oppose careful planning. Good planning takes a reasonable amount of time in Lawrence, just like it does everywhere else.

Current Practice in Lawrence for Economic Development

The Chamber of Commerce receives over \$400,000 in taxpayer dollars each year from the City and the County. The Chamber provides some outreach services to firms seeking sites for their own expansion. The Chamber has supported numerous applications for subsidy packages from the City to private firms, without analyzing the need for the subsidy packages. The Chamber

conducts little to no planning research to assess conditions, design strategies and implement projects and programs that are driven to serve the community as a whole.

The record of accomplishments for Chamber of Commerce is poor.

*Surplus retail
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History of Economic Development Planning in Lawrence

Tax Abatements

The City and County use the Public Incentives Review Committee (PIRC) to monitor the performance of the various subsidy packages given to firms as part of economic development efforts. Primarily, the PIRC monitors the performance of the various tax abatements given to firms. The Chamber packaged and supported each of these tax abatements.

Review of the annual reports from the PIRC finds a disappointing performance of these tax abatements. Each tax abatement promised to produce a specified number of jobs, to pay wages that are at or above community standards, and to make a specified amount of investment in property adding to the tax base. Here are the facts:

The Chamber has actively led the City into a large list of tax abatements. Of the 17 firms granted abatements:

- Only 6 produced the promised jobs and wages.
- The remaining 11 are either out of compliance, out of business, or not reporting.

Compliance is defined as producing at least 90 percent of the jobs promised, paying at least 90 percent of workers' wages that are at least 90 percent of the mean wage reported for the occupation in Lawrence, and making at least 90 percent of the promised property investment.

This record of success is unimpressive. The abatements are:

- Successful only 35% of the time,
- Non-compliant 40% of the time, and
- Complete failures 25% of the time. (See Annual Reports of the Public Incentives Review Committee.)

The tax abatement program, supported and implemented by the Chamber, is a needless expense for the taxpayers. All of the published research on tax abatements finds this to be true. (See Luke Middleton. Literature Review: Tax Abatements and Economic Development Incentives. The University of Kansas, Center for Economic and Business Analysis, Policy Research Institute, 2001.) The firms would have produced the jobs without the tax abatement.

Some of the firms have made public statements to this effect. Property taxes are too small a percentage of a firm's total operating expenses to be crucial to the decision to build or expand. However, lower taxes are always helpful to enhance profits; thus, firms ask for the tax abatements even when they are not important to the decision to build or expand. The firms misleadingly state their position to the City, saying that without the tax abatement the firm cannot build or expand.

What the reports from the PIRC show is that Lawrence has an ongoing problem with its tax abatement program. In a normal economic development program, non-compliance should be minimal. The PIRC should be discussing what to do with no more than one firm that is out of compliance. Instead, the PIRC has, over time, had to deal with the fact that non-compliance is normal in Lawrence. Six of the eight firms have been substantially out of compliance in at least one of the important areas or investment, wages, or jobs. This is not a new or temporary condition; it has been going on for years. Nevertheless, under Chamber leadership Lawrence continues to honor tax abatements that are producing no benefit for the city.

The City has been misled. It has been told by the Chamber of Commerce and other business advocacy organizations that tax abatements are needed to attract firms even though the experience both locally and nationally says the opposite. The City has been led into a position of offering abatements, almost automatically, to firms just for the asking. Yet, these firms fail to make the promised investments, fail to pay wages comparable to other firms in the community, and fail to produce the promised jobs. In many cases, the firms go out of business before the City can hope to realize any benefits.

An ongoing problem of non-compliance hurts the City. Not only does the City not get the jobs and wages and taxes promised, but it cannot negotiate effectively with future firms. A firm can promise much, produce little, and still keep its tax break.

Subsidy to Retail

The Chamber supported subsidizing retail chains seeking to enter the Lawrence market. These new vendors would add to an already overpopulated supply of retail stores that we have in Lawrence. Moreover, by bringing in outside managers they further dilute the employment options for Lawrence's labor force.

Inflation adjusted growth in retail spending after 2000 is growing at 0.2 percent per year, enough to support about only 25,000 to 30,000 additional square feet.

From 2000 through 2007, the stock of retail square feet grew at 3.1 percent or about 150,000 square feet per year. The developers added about 1.3 million square feet beyond what the growth in retail spending could support. This is approximately the size of the retail space in the entire downtown or about one-fourth of the total stock of space. This is much more retail space

than growth in retail spending can support.

The situation is rapidly becoming worse as an additional 750,000 square feet of space have been approved for West 6th Street from Folks Road to the South Lawrence Trafficway. If all of this space is built, it will swell the stock of surplus space to over two million square feet.

Surplus retail space does not generate additional retail demand. The amount of spending only grows with the income growth of the local population, which has been close to stagnant for some time. The surplus development only spreads the available demand over more space, reducing the spending at each location, hurting the performance of those existing stores. The surplus new development has stalled several redevelopment plans downtown and has pushed the vacancy rates so high that disinvestment and blight now threaten several older shopping centers.

Despite this condition, the Chamber of Commerce supported subsidizing new chain stores, such as Olive Garden.

Led the City into Questionable Investments

The Chamber supported a City investment in a building in West Lawrence that probably cannot generate enough occupancy to support the price paid by the City.

The Chamber supported the investment of \$2.9 million of taxpayer funds into 4050 Research Parkway. The City purchased the property from the firm CritiTech with the property to be managed by the Lawrence Douglas County Bioscience Authority. Firms, including CritiTech, would lease the property to pay the debt the taxpayers incurred on the property. The financial projections for the property anticipate that it would not generate sufficient income to cover the costs of operation and that the taxpayers of Lawrence and Douglas County would subsidize the property to cover the losses.

The purchase price becomes immediately suspect because one of the previous owners of the property is a principal in the CritiTech firm which is to be a subsidized occupant of the property. The sellers have an interest in obtaining as high a price as possible for the property, even a price higher than it can command in the private market. CritiTech, as an occupant, has an interest in leasing the space at a low lease rate, even a rate that is below the market rate. With no arm's length separation between the seller and the tenant, the taxpayer cannot trust either the purchase price or the lease rate.

The purchase was financed with general obligation bonds. It is more common for projects of this type to be financed with revenue bonds. With revenue bonds, the city promises only the revenues from the project for payment of the debt. Revenue bonds insulate the taxpayers from

a heavy financial burden if the project fails.

This is a highly risky project for the taxpayers. Not only is the investment risky, the Chamber and the LDCBA do not make public reports on the performance of this investment or others like it. Transparency and accountability to the taxpayer are missing.

Illegal Meetings

The Chamber actively sponsored meetings to arrange for packages of taxpayer-funded subsidies to private firms under the mistaken belief that confidentiality was paramount. The parties at these meetings included the City Commission, the buyers of the property, and the sellers of the property. The only people excluded were the taxpayers. The Attorney General found these meetings to be in violation of the Kansas Open Meetings Act. (See "AG: City leaders broke law: Morrison proposes open meetings training for settlement" Lawrence Journal World December 1, 2007.) Following the decision of the Attorney General, the members of the City Commission were censured and had to take instruction on the limits of their authority to meet in secret, executive sessions.

The Chamber of Commerce initiated this type of meeting to further its economic development activities. Effective local economic development should not be kept secret from the taxpayers who fund the programs. Transparency and accountability are essential to the process.

Professional Best Practices

Enforcement

Chamber staff have actively resisted all efforts by the Public Incentives Review Committee to investigate the level of compliance by firms with the terms of their tax abatements. (See Minutes of the Public Incentives Review Committee.)

Lack of Planning

The Chamber conducts virtually no planning in its economic development exercises. It has supported proposals for such grandiose projects as the development of 1,000 acres of industrial park space, yet it has failed to produce any planning analysis that would justify such a large facility. (Lawrence Journal World, Group recommends 1,000 acres to assist in creation of jobs,

December 5, 2001.) It has led the community into a \$5 million investment in a vocational training center without any study on whether or not this facility is the best way to serve any shortcomings in the workforce. Such a center may or may not be needed, but the Chamber forged ahead on the center without any detailed study of the need for such a center, how best to design such a center, or how to assess the costs and benefits of such a center.

Lack of Analytical Skills:

The Chamber is staffed with people who design and implement the economic development programs of the City and County. None of these staff members have professional degrees in economic development planning. To be successful at local economic development requires the skills and guidance of planners with advanced education in the field. Many cities are active in these efforts; the successful ones hire skilled professionals to guide them. This expertise is necessary so that the community's actions are driven by research-based knowledge in the field so that the taxpayers can be assured of transparency and accountability in all of the actions taken.

Research on Who Should Run Local Economic Development

It is not unusual for a city to contract with a Chamber of Commerce to operate its economic development activities. Because of this, the process has been studied widely. These studies find that Chambers of Commerce are not an effective means to implement effective economic development. Good business practitioners are not necessarily good economists.

Wolman and Spitzley find that local economic development decisions are made through a political process masquerading as a rational process. A political "growth machine" exists in many communities that is a coalition of interests who benefit from real estate development, rather than real economic growth. Led by business interests such as real estate developers and the Chamber of Commerce, this growth machine maneuvers to take control of the economic development process (Harold Wolman and David Spitzley. 1996. The Politics of Local Economic Development, *Economic Development Quarterly* 10(3):115-150.)

Rubin finds that when economic development is directed by a Chamber of Commerce, the deals are structured to benefit the businesses, often at the expense of the taxpayers. When economic development is directed by a local government, the deals are structured to benefit the community as a whole. When local government turns over the administration of local economic development to a special interest group, such as the Chamber, that special interest

group generates a systematic bias in favor of the Chamber's constituents (Herbert J. Rubin, 1988, *Shoot Anything That Flies; Claim Anything that Falls: Conversations with Economic Development Practitioners*, *Economic Development Quarterly* 2(3):236-251)

McGuire finds that economic development is a collaborative process, but the form of the collaboration is important. When the Chamber is in the lead role, it will direct the process to the benefit of its constituents, its member businesses (Michael McGuire. 2000. Collaborative Policy Making and Administration: The Operational Demands of Local Economic Development. *Economic Development Quarterly* 14(3): 278-291.)

Opening up the process can be beneficial. KU's own Elaine Sharp finds that "Public officials in tax-stressed communities who are wary of the potential consequences of popular mobilization may be relieved to find that heightened citizen involvement can actually enhance the climate for economic development policies . . ." (Elaine B. Sharp and David B. Elkins. 1991. The Politics of Economic Development Policy. *Economic Development Quarterly*, 5, 126-139.)

No one can serve two masters, and the Chamber of Commerce is no exception. It works for its membership as a special interest group advocating for businesses. It does not work for the community as a whole.

Economic development is an exercise that has been studied widely and effective implementation of economic development strategies requires in-depth knowledge of this research. The staff of the Chamber of Commerce lacks this knowledge. If the City of Lawrence wants to pursue economic development policies that are beneficial to the community as a whole, it needs to both professionalize the local economic development staff and make the process open and transparent. This means taking the Chamber of Commerce out of its sole leadership role in economic development and placing these duties in the hands of well trained professionals who report to the City Commission, rather than a special interest group.

Recommendation

Each year, the City and the County pay over \$400,000 to the Chamber of Commerce to guide and implement its economic development initiatives. The City and County Commission should redirect this money towards professional planners who report to the elected officials. These planners would bring professional skills and knowledge to their work and would serve the community as a whole. The Chamber should be at the table

The Chamber should be at the table when economic development policy is designed and implemented, but it should not be the sole leader in the city's economic development efforts.

when economic development policy is designed and implemented, but it should not be the leader in the city's economic development efforts.

The Chamber of Commerce is a business advocacy organization. Economic development strategies need to be good for business, but, more importantly, they need to be good for the community as a whole.

Lawrence needs staff economic development planners that can guide the City through detailed negotiations with firms to ensure that a subsidy package, if any, is in the City's best long-run interests. Lawrence needs unbiased economic development planners who can accurately project the City's future needs.

Lawrence needs economic development planners that will be transparent in the development and analysis of subsidy packages and will work within the confines of the law prohibiting secret meetings.

Lawrence needs economic development planners who will determine criteria and evaluate the effectiveness of incentive agreements

It is recommended that the City of Lawrence and Douglas County, Kansas:

- End its contractual relationship with the Chamber of Commerce for purposes of local economic development planning, and
- Improve its local economic development programs and procedures through expansion of its own planning staff.
- Adopt reporting and disclosure practices to ensure transparency and accountability in its local economic development activities.