



# HIGH ROAD POLICY

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## Economic Development on Common Ground:

*Two Bipartisan State Policies for Defunding Low Road Infrastructure*

Americans are living through and participating in an era of historic political division.<sup>1</sup> As one reporter recently put it: “Polarization, building for decades, was already intense before COVID-19. Now it’s on steroids.”<sup>2</sup>

The signs are everywhere – from mass demonstrations and protests in support of Black Lives Matter<sup>3</sup> to the politicization of mask-wearing<sup>4</sup> and other seemingly commonsense measures to curb the coronavirus pandemic.<sup>5</sup> The latter of these divisions is being fueled in part by “divergent cues” from “political elites” in the two major political parties.<sup>6</sup> This lack of a concerted, bipartisan response is seriously undermining efforts to stop the spread of COVID-19, with deadly consequences.<sup>7</sup>

If these observations are not enough to convince readers of just how far apart politically Americans have grown, then consider one of the most widely used numerical indicators of polarization: the partisan gap in Presidential job approval ratings.<sup>8</sup> This long-running measure, which has been tracked since at least 1945,<sup>9</sup> has been on an upward trajectory for decades.<sup>10</sup> Prior to the current Presidential administration, the metric topped out at 77 points for the 2016 calendar year.<sup>11</sup> During that year, 89% of Democrats

approved of President Obama’s job performance compared to 12% of Republicans. Since that time, the gap has widened even further. The overall gap for the 2019 calendar year hit 79 points, with 87% of Republicans approving of President Trump’s job performance compared to just 8% of Democrats.

Early data suggest that 2020 will be another year for the record books. As of this writing, the partisan gap in Presidential approval has been at or above 80 points in seven of the ten two-week periods for which data are available. During the remaining three survey periods, the figure stood at 78 points twice and 79 points once.<sup>12</sup> The spread has been as high as 87 points – during consecutive reporting periods from mid-January to mid-February – and has averaged around 83 points since the start of 2020. Data from the most recent two-week period (ending 4 June 2020) show that 85% of Republicans currently approve of President Trump’s job performance compared to just 5% of Democrats.<sup>13</sup>

On the backdrop of civil unrest and the nation’s politically discordant handling of COVID-19, these alarming figures bode poorly for the prospects of overcoming partisan gridlock to pass progressive, High Road legislation.<sup>14</sup> At face value, members of opposing political parties seem too unwilling to

cede any ground to their rivals to come together to enact meaningful change. To be sure, lawmaking bodies are even unable to agree that a global pandemic, which has thus far killed over 125,000 Americans and left tens of millions jobless, demands additional government intervention.<sup>15</sup>

Nevertheless, there is at least one domain where the two sides of the political divide appear to share common ground. Organizations and authors from right-leaning free market think tanks like the Mercatus Center<sup>16</sup> to the left-leaning Good Jobs First<sup>17</sup> have made the case to end targeted economic development subsidies and tax incentives.<sup>18,19</sup> The next section explores the rationale for this position. From there, the memo highlights two opportunities to reform – and ultimately phase out – economic development incentives in New York State. Both opportunities were introduced to the New York State Assembly in the 2019-20 legislative session. Thus, the legislation already exists and does not need to be drafted anew. The bills are available to be reported out of committee and put to a vote (or, since the session has ended, reintroduced in 2020-21 and then reported out of committee for a full Chamber vote). They accordingly represent near- to medium-term actions that the State legislature can take to wind down and then end a practice that, as detailed below, is roundly derided across the political spectrum. Finally, the memo concludes with an even more immediate policy target: a federal COVID-19 relief package for state and local governments that might help end the “interstate economic development arms race.”<sup>20</sup>

## **Bipartisan Consensus on Economic Development Incentives**

While the ultimate reasons that representatives from the right and the left both want to do away with development incentives might diverge (e.g., market distortion<sup>21</sup> versus subsidized inequality<sup>22</sup>), their proximate justifications are essentially

identical. Both sides have raised the following points:

- peer-reviewed research broadly agrees that “while subsidies may benefit the firms, activities, industries, or regions that [those subsidies] privilege, most are not associated with measurable improvements in the broader communities that pay for them”;<sup>23</sup>
- incentives are almost never decisive factors in employers’ location decisions – meaning that most incentives are not needed to lure employers, and are therefore wasteful;<sup>24</sup>
- the very existence of incentives encourages firms to spend resources on lobbying and procuring incentives – these investments could otherwise be reinvested in businesses and workers, as opposed to enriching already wealthy companies and their shareholders;<sup>25</sup>
- because incentives are paid for with public resources, they often lead to higher taxes, reduced public services, or both, in the jurisdictions where they are provided;<sup>26</sup>
- for all of the above reasons, providing targeted economic development incentives is a Low Road practice that leads to and reinforces spatial and economic inequality;<sup>27</sup>
- and, perhaps most notably, scores of elected officials and decision-makers decry the practice and would prefer to eliminate the use of incentives;<sup>28</sup> however, they feel pressured to continue playing the game for fear of putting themselves and their jurisdictions at a strategic disadvantage in the global economic development marketplace.<sup>29</sup>

It is beyond the scope of this memo to unpack the research on which the preceding conclusions are based, nor is it our aim to relitigate specific findings or pieces of evidence from that body of work.<sup>30</sup> Instead, we note only that the

instructive literature points to at least two general problems with status quo economic development incentive policies: (1) incentives subsidize private companies and shareholders with public resources, at a net cost to the public; and (2) there is no mechanism for coordinating economic development policy across jurisdictions to prevent this outcome from happening.

With respect to the latter, even a slight suspicion that a “rival” jurisdiction might offer development incentives causes all other jurisdictions to do the same. This absence of mutual assurance makes all jurisdictions worse off by pushing them deeper into an “economic development arms race” from which they see “unilateral disarmament” as a losing strategy.<sup>31</sup>

Logic suggests that the former of these problems would disappear if the latter were wholly resolved – that is, if jurisdictions mutually agreed to eliminate development incentives. Assuming that such an agreement could be reached – and assuming that jurisdictions would face sanctions that cost them more than the perceived benefits associated with defecting from the agreement – there would be no incentives to speak of, and, hence, no net cost imposed on the public.

Unfortunately, this type of complex, multilateral arrangement is probably not something that can be accomplished in the near- to medium-term, given all the parties and transaction costs involved (though, as expanded on in the final section below, COVID-19 may change that reality). As such, for any given state or locality wishing to withdraw from the arms race, the more expedient path is arguably to solve the first problem first, while laying the groundwork to gradually build a solution to the second one over time. New York State is positioned to provide national leadership on both matters, by (1) passing the Economic Transparency and Accountability Act (NYS Bill A07096) and (2) adopting the Interstate Compact Agreement to Phase Out Corporate Giveaways

(NYS Bill A08675/S3061). The remainder of this memo examines the key provisions included in these two legislative proposals.

## Opportunity 1: Pass the Economic Transparency and Accountability Act

The Economic Transparency and Accountability Act (“ETA”) was introduced to the New York State Legislature in the 2019-20 session by Assembly Member Ron Kim (D-40). The ETA is a far-reaching economic development law that would, among other things:

- substantially reduce the total amount of incentives provided by any granting agency on a per employer basis;
- contractually obligate incentive recipients to create new, full-time, quality jobs;
- contractually obligate incentive recipients to reserve a minimum percentage of new full-time jobs for persons from low-income geographies and vulnerable population groups;
- require incentive recipients to provide periodic, consistently formatted, comprehensive disclosure reports to granting agencies – recipients that fail to provide these reports on time are subject to daily monetary fines that increase in value after 20 days past the deadline;
- require all property-taxing entities to aggregate reports from incentive recipients in their respective jurisdictions into comprehensive, consistently formatted, periodic reports that are published and conspicuously advertised on those entities’ (e.g., cities, towns, villages) websites – state funding can be withheld from jurisdictions that fail to comply with these deadlines and responsibilities;
- recapture incentive monies from recipients that fail to meet the job creation, job quality, and/or job perpetuity standards set forth in the ETA (see especially Sections 456-459 of the bill).<sup>32</sup>

The above provisions speak to at least five major reforms<sup>33</sup> and strategic imperatives<sup>34</sup> for shifting status quo, Low Road economic development incentive policies toward the High Road. Specifically, the ETA:

**Imposes strict subsidy caps.** Subsidy caps are limits, or maximum dollar figures, placed on the incentives that any one granting agency may offer to a private entity for any one development project. Caps can be tied to a project's total cost or to the number of qualifying jobs the project is expected to create.<sup>35</sup> The ETA employs the latter mechanism, specifying that no granting agency shall provide more than \$6,000 in incentives per qualifying job. In practice, subsidy caps commonly range from \$5,000 to \$35,000 per qualifying job.<sup>36</sup> The ETA would therefore place New York State at the low end of the spectrum – and thus a step closer to phasing out giveaways altogether. The strict cap would be a major shift from existing policy. Consider that, prior to breaking down, the deal to bring Amazon's HQ2 to New York City amounted to more than \$112,000 in incentives per job.<sup>37</sup>

**Requires disclosure of incentives and recipient compliance.** Disclosure refers to the regular “reporting of public costs (subsidies received) and public benefits (jobs created, wages, etc.) relating to economic development deals.”<sup>38</sup> For disclosure to be effective, it must (i) be transparent and accessible, (ii) cover all granting agencies, (iii) apply to all development incentives and be deal- and company-specific, and (iv) be continuous. The ETA satisfies these provisions. It mandates that all incentive recipients provide annual, detailed reports on job creation, job quality, worker benefits, and other public benefits. And it requires that all property-taxing jurisdictions (e.g., cities, towns, villages) compile and publish detailed annual reports on incentive activity and corporate compliance with ETA standards. The Act further makes progressive *process reforms*<sup>39</sup> to increase

public awareness about prospective incentive packages and provide opportunities for public participation in decision-making.

**Creates clawbacks.** A clawback “is a clause of a subsidy law or contract that...says...a company must uphold its end of the bargain or else taxpayers have some money-back protection.”<sup>40</sup> In other words, if the incentive recipient does not deliver on the conditions set forth by the ETA, then the granting agency is entitled to reclaim, or recapture, a monetary sum up to the dollar value of the incentives.

**Contractually obligates incentive recipients to create quality jobs.** As the text that introduced the ETA to the New York State Assembly reads: “Any job is a good job’ is no longer a sufficient rationale for corporate subsidies.”<sup>41</sup> *Job quality standards* are “requirements that subsidized companies create jobs that meet certain criteria, including wage levels, availability of health insurance, and full-time hours.”<sup>42</sup> Among the job quality standards imposed by the ETA are: (i) full-time employees must be paid statewide, industry-standard wages, verified against Bureau of Labor Statistics and Bureau of Economic Analysis data; (ii) full-time employees must provide health benefits that cover at least half the cost of employees’ insurance premiums; (iii) full-time employees must be guaranteed an average of 35 hours of work per week per calendar year; (iv) all full-time employees must receive at least twelve days paid leave per year; (v) at least 30% of full-time workers must live in a relatively low income geography; and (vi) at least 10% of full-time workers must come from certain marginalized populations (see Section 457.7 for a full enumeration of qualifying subpopulations). Stated more plainly, the ETA requires subsidy recipients to create full-time jobs that pay decent wages and offer essential benefits – and it specifies that a meaningful fraction of those jobs must be filled by workers from geographies and population subgroups that have

been disproportionately harmed by the Low Road economy.<sup>43</sup>

**Creates a State “carrot” for local governments to judiciously monitor compliance.** That is, under the ETA, property-taxing entities that do not follow reporting and disclosure requirements could potentially lose State funding. The ETA therefore provides a strong incentive for localities to “race to the top” by carefully monitoring and enforcing the terms and conditions of local incentive agreement with recipients.<sup>44</sup>

In combining these five elements, the ETA would fundamentally overhaul a system of economic development incentives that is condemned on both sides of the political aisle. The resulting system would be fairer, transparent, and more participatory; would create net public benefits or else recapture funds; and would motivate close monitoring and enforcement of its provisions by local property-taxing jurisdictions. It is therefore a commonsense bill that advances the public good. Still, there are at least two minor amendments that might make it even stronger.

First, legislators can strengthen the bill’s subsidy cap language to foreclose on a potential loophole. The bill presently states that “no *granting body* shall provide a development subsidy to a recipient corporation in excess of six thousand dollars for each new full-time job created by the recipient corporation” (Sec. 452; emphasis added). The Act defines a *granting body* as “any agency, board, office, public-private partnership, public benefit corporation or authority of the state or a local government unit that provides a development subsidy” (Sec. 451.5). Taken together, these two provisions might allow for *multiple granting bodies* to legally provide the maximum allowable subsidy (\$6,000 per qualifying job) to the same private entity for the same development project, thereby circumventing the cap. Language to exclude these possibilities can be introduced to guarantee that

the maximum subsidy for a single project *from all granting bodies, combined*, is set to \$6,000 per qualifying job.

Second, legislators should consider amending the bill to add African Americans to its list of population subgroups for whom a fraction of quality, full-time jobs must be reserved. In its current form, the Act undeniably puts a stop to Low Road economic development subsidy practices and creates mechanisms to promote economic equality; but it does not explicitly engage with the ongoing fight for racial justice. Requiring that incentive recipients create quality jobs for African American residents could be an incremental step in that direction.

With or without these recommendations, reporting the ETA out of committee and getting it to the floor of both State houses seems like a reasonable priority for the upcoming legislative session. There is political consensus that targeted economic development incentives are wasteful and inequitable in their current form. The ETA offers strong remedies for these problems.

## Opportunity 2: Adopt the Interstate Compact Agreement to Phase Out Corporate Giveaways

Recall that the research on targeted economic development incentives points to at least two big problems with the status quo: (1) incentives rarely net public benefits and typically only enrich wealthy corporations and shareholders;<sup>45</sup> and (2) even though many public officials recognize this problem and disapprove of incentives,<sup>46</sup> they fear that unilateral withdrawal from the subsidy game would put their jurisdictions at a strategic disadvantage relative to other regions.<sup>47</sup>

The Economic Transparency and Accountability Act (ETA) arguably offers solutions to the first problem for New York State – but what about the

second one? How can subsidies be phased out when no granting agency is willing to be the first back down?

Authors in the economic development literature frequently frame this coordination failure as a *prisoners' dilemma* (PD).<sup>48</sup> The PD is a conceptual device for describing situations in which one or more parties face a choice between cooperating or acting selfishly. If all parties cooperate, then they are all better off. However, each individual party has an incentive to be selfish. In the classic formulation, two partners suspected of carrying out a crime face questioning in separate rooms. If both refuse to talk to investigators, then both receive a light punishment given a lack of more damning evidence against them. If both confess, then both receive a moderate sentence that is more severe than the punishment from when both remain silent, but less severe than the maximum sentence. If one suspect "talks" while the other remains silent, then the confessor goes free while the partner receives the maximum sentence. In such circumstances, *regardless of what the other suspect does, each individual is better off confessing*. More precisely, if one's "rival" confesses, then remaining silent renders the maximum possible sentence. If one's "rival" remains silent, then confessing renders no punishment at all, compared to a light sentence from also remaining silent. In short, both suspects reason that they should confess. And, in the end, both get a harsher sentence than they would receive if they *cooperated* or *coordinated* with one another to remain silent.<sup>49</sup>

Comparisons between the PD and the economic development incentive game are appealing, which is why some State legislators explicitly refer to economic subsidies as a "prisoners' dilemma."<sup>50</sup> However, if the research is right that public officials generally prefer *not* to offer development incentives,<sup>51</sup> then the game is not really a PD. In a PD, participants always have an incentive to act selfishly, even when their "rivals" act cooperatively.

In the economic development incentive game, public officials prefer to do what [they expect] their rivals to do. If they expect their counterparts to use subsidies, then they feel obliged to do the same, thus joining the "arms race."<sup>52</sup> But, if they expect their colleagues to *cooperate*, and forswear development incentives, then they prefer to do the same. Like the PD, this cooperative scenario yields the best outcome for all parties. Unlike the PD, though, parties are not competitors trying to win victories at each other's expense. They are merely interactants hoping to coordinate their decisions. Consequently, the economic development policy game is not a PD, but something called a *game of assurance*.<sup>53</sup>

The distinction here is more than theoretical. Generally speaking, mechanisms to build trust and promote cooperation are costlier, riskier, and often less effective in a PD setting since each party has a unilateral incentive to act selfishly (and "win" a "victory"<sup>54</sup>). By contrast, trust-building mechanisms are quite effective at promoting stable cooperation (meaning that parties face stronger incentives to cooperate than to defect) among participants in games of assurance.<sup>55</sup> After all, participants in such games "win" when their decisions are coordinated.

In the case of interstate economic development policy, one trust-building mechanism to promote coordination among subsidy granting bodies – and hence solve the coordination failure in the assurance game – is an *interstate compact*. An interstate compact is a contract "between two or more states creating an agreement on... specific policy challenges [or] regulatory matters." Compacts have been used in the U.S. since 1789 and "let states develop a dynamic, self-regulatory system that remains flexible enough to address changing needs."<sup>56</sup>

Interstate compacts are voluntary, but legally binding for all member states that enter into them. For that reason, a "compact allows states

to credibly commit to a given course of action and to be sure that their compact partners will be held to their own promises.”<sup>57</sup> That is, compacts create *mutual assurance* that members will act cooperatively in a given domain. As such, writers from the left<sup>58</sup> and right<sup>59</sup> have argued that states should adopt a multilateral compact to phase out targeted economic development subsidies.

This proposal has taken off in recent years. Legislators from both parties, representing around one-third of states, have introduced bills to their respective chambers that call for an interstate compact “to phase out corporate tax giveaways.”<sup>60</sup> So far, the bill has passed the lower chamber in the Utah State Legislature, where it was introduced by a Republican Assembly Member; and it is gaining momentum in states across the country.<sup>61</sup>

During the 2019-20 legislative session in New York, the interstate compact proposal was introduced to the lower chamber by Assembly Member Ron Kim (D-40) and to the upper chamber by State Senator Julia Salazar (D-18). To date, the bill has attracted six cosponsors in the Assembly and one in the Senate. Consistent with parallel proposals in other states, this “Act to... [establish] an interstate compact agreement to phase out corporate giveaways” contains five core provisions:

**A conceptually and geographically inclusive definition of corporate giveaway.** The Act defines a giveaway as “any company-specific or industry-specific disbursement of funds via property, cash or deferred or reduced tax liability by a state or local government to a particular company or industry.”<sup>62</sup> This sweeping definition suggests that the agreement applies to all direct and indirect handouts in all jurisdictions that lie in participating states.

**Voluntary membership that is open to all states.** Multilateral agreements characterized by open and voluntary participation are conducive to

consensus-building and cooperative governance.<sup>63</sup> Put another way, voluntary associations connect members that have at least some shared sense of a problem and some shared vision for a solution. As such, members are generally motivated to work cooperatively. More coercive arrangements can crowd out these positive motivations. Nevertheless, as expanded on in the final section below, coercive mechanisms may be useful when cooperation fails to emerge organically.

**Explicit recognition of the Low Road nature of targeted economic development incentives.** The bill states plainly that: (i) “Corporate giveaways are among the least effective uses of taxpayer dollars to create and maintain jobs”; and (ii) “Corporate giveaways fuel business inequality as only the largest businesses receive the vast majority of these funds.”<sup>64</sup>

**Prohibitions against job poaching.** *Job poaching* is the “use of subsidies to lure existing business facilities from one jurisdiction to another.”<sup>65</sup> The Act to establish an anti-corporate giveaway compact expressly prohibits this practice for all member states. This anti-poaching provision is the actionable piece of the compact. The compact does not declare that member states will end the use of corporate giveaways – only that they will not provide giveaways that have the effect of luring a company from one member state to another. As the Act proclaims, anti-poaching is simply a “first step” toward phasing out giveaways altogether.

**Democratic enforcement powers.** While the Act states that the “chief law enforcement officer of each member state shall enforce [the] compact,” it gives every “taxpaying resident of any member state” explicit standing to use their state’s legal apparatus to compel “chief law enforcement officers” to enforce the compact.<sup>66</sup> This subtle provision empowers residents and communities to challenge corporations and public subservience to corporations in a way that is scarcely possible under existing laws.<sup>67</sup>

High Road policies advance society toward participatory democracy via mechanisms that, among other things, build and promote cooperation and solidarity.<sup>68</sup> The Interstate Compact to Phase Out Corporate Giveaways is a tool to facilitate interstate cooperation on, and to provide democratic enforcement powers to residents who want to participate in the process of eliminating, economic development subsidies. The Compact is being championed in multiple states by lawmakers from both major parties. New York has an opportunity to be the first state – or among the first states – to enter into the bipartisan compact by passing Legislative Bill A08675/S3061 in both State houses.

### **Next Step: Federal Pandemic Relief and Corporate Giveaways**

Because the New York State legislature is out of session until January 2021, the two opportunities outlined above cannot be pursued immediately. What state lawmakers can do immediately is continue pressuring Congress to provide more pandemic relief for state and local governments.

Researchers at the Economic Policy Institute estimate that without additional COVID-19 aid for state and local governments, more than 400,000 New Yorkers will “likely lose their jobs by the end of 2021.”<sup>69</sup> State legislators must therefore use their political capital to increase pressure for aid.

Given the widespread, bipartisan opposition to corporate giveaways, one way that legislators might make the idea of more federal funding palatable to members of Congress is to suggest that aid be contingent on “contractually forswear[ing] future targeted economic development subsidies.”<sup>70</sup> Mercatus Center researchers Michael Farren and John Mozena make a strong case for contingent COVID-19 relief by observing that such a stipulation falls within Congress’ scope of enumerated powers, and that it has several historical precedents.<sup>71</sup> Among

other examples, the promise of federal funding has been used to push states to raise their minimum drinking ages and to “modernize their Unemployment Insurance programs.”<sup>72</sup>

While there are moral reasons to reject a policy of contingent funding during a pandemic that is impacting every state and community in the nation, the reality is that additional state and local government aid has not been otherwise forthcoming.<sup>73</sup> The U.S. Senate Majority Leader suggested on record that “bankruptcy, not more federal money, might be best for state and local governments.”<sup>74</sup> He has, however, signaled that more aid is possible – so long as it comes with strings attached.<sup>75</sup>

If Congress will not provide necessary aid to state and local governments unless the funding serves some dual policy purpose, then it makes sense to target economic development incentives. Both parties want to see the Low Road practice come to an end. While an interstate compact to phase out subsidies is a major step up the High Road, not all states are likely to join. Refusal of some states to participate could undermine any compact that forms organically, due to the perception that economic development policy is an “arms race” from which voluntary withdrawal is a losing strategy.

Federal intervention can diffuse this situation and create conditions for across-the-board disarmament. Rather than intervening in a coercive manner, the promise of funding provides a “carrot” for state and local governments that they can either opt into or decline. Of course, pandemic relief is not a standard carrot. It’s more like the only carrot in an otherwise empty produce section. Attaching strings to such funds is therefore like forcing some state and local governments to sign contracts under duress. Some might enter an interstate compact voluntarily. Others might not ordinarily agree to the terms.

That being said, the bottom line is that Congress would be operating within the scope of its authority if it moves to offer federal COVID-19 aid to state and local governments that agree to end targeted economic development incentives. As we just noted above, this use pandemic relief to advance a separate policy priority would be morally suspect. Nevertheless, if Congress will not provide urgently needed aid without employing it as a carrot for state and local policy change, then, at minimum, that policy change should involve a bipartisan step toward the High Road. State and local officials can use their political capital make this case to their colleagues in Congress.

Eliminating corporate giveaways would critically weaken existing Low Road infrastructure by removing a known source of economic inequality.<sup>76</sup> It would also represent a major bipartisan policy change in an era of intense political polarization. While Congress can take immediate action toward these ends, based on current levels of gridlock, such action seems unlikely. Thus, state and local governments must continue to lead the way. As this memo has argued, the New York State Legislature has two substantive opportunities to do just that.

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## About *High Road Policy*

*High Road Policy* is a quarterly issue memorandum published by the Cornell University School of Industrial Labor Relations (ILR) through its Buffalo Co-Lab. It aims to contribute actionable insights to contemporary policy and political discourses in and beyond the regions and communities of Upstate New York. Content for memoranda comes in part from the Co-Lab's Data for Equitable Economic Development and Sustainability (Good DEEDS) program, which democratizes local and regional data for the purposes of: empowering residents and institutions; informing public policy debates; and providing an empirical basis for ensuring that change and development in Upstate communities follows the High Road to shared prosperity for all residents, from the present to all future generations.

## Notes

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