

Creating Scandals Instead of Jobs: The Failures of Privatized State Economic Development Agencies

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Executive Summary

Three years ago, newly elected governors in several states, most notably Wisconsin and Ohio, decided that the best way to create jobs was to transfer economic development business-recruitment functions to “public-private partnerships.” These experiments in privatization have, by and large, become costly failures. Privatized development corporations have issued grossly exaggerated job-creation claims. They have created “pay to play” appearances of insider dealing and conflicts of interest. They have paid executives larger salaries than governors. They have resisted basic oversight.

State officials cannot say they weren’t warned. In January 2011, Good Jobs First published a report entitled *Public-Private Power Grab* in which we noted that this approach had already been tried in more than half a dozen states and the track record was far from impressive. In the last three years, the story has grown demonstrably worse, with major problems in both new and old privatized development corporations.

We document here again numerous cases in which the public-private partnerships (PPPs) have become embroiled in scandals involving misuse of taxpayer funds, conflicts of interest, excessive executive pay and bonuses, questionable subsidy awards, exaggerated job-creation claims, lack of public disclosure of key records, and other accountability abuses.

We concluded in 2011, as our title suggested, that the real agenda behind these PPPs was not to make economic development efforts more effective but rather to more tightly concentrate the control over—and credit for—job creation events in the hands of governors and their appointees.

Tragically, the history we detailed continues to repeat itself. An examination of the new wave of PPPs shows many of the same problems, especially in Wisconsin and Ohio. We also found new controversies in many of the older PPPs. Specifically:

- Enacted in 2011 at the initiative of Gov. Scott Walker, the Wisconsin Economic

Development Corporation (WEDC) has been racked by scandals and high-level staff instability. It awarded a subsidy to a company that was simultaneously bidding on a \$15 million state contract. It was accused of spending millions of dollars in funds from the U.S. Department of Housing and Urban Development without legal authority. It failed to track past-due loans. It hired an executive who owed the state a large amount of back taxes. Two legislative audits have revealed a loose organizational culture that is failing to perform basic “watching the store” functions on outstanding loans and allowing large amounts of unapproved or unjustified staff credit-card expenses.

- JobsOhio, created in 2011 at the urging of Gov. John Kasich, assembled a board of directors whose members included some of his major campaign contributors and executives from companies that were recipients of large state development subsidies. It received a large transfer of state monies about which the legislature was not informed, intermingled public and private

monies, refused to name its private donors, and then won legal exemption (advocated by Gov. Kasich) from review of its finances by the state auditor.

- The first chief executive of the Arizona Commerce Authority was given a three-year compensation package worth \$1 million, and even though he resigned after a year he received a \$60,000 privately-funded bonus.
- The Indiana Economic Development Corporation, one of the older PPPs, has faced continuing criticism over its job-creation claims. Triggered by tenacious investigative reporting by Indianapolis TV station WTHR, a state audit found that more than 40 percent of the jobs promised by companies described by IEDC as “economic successes” had never materialized. IEDC was also rocked by allegations that its representative to China solicited bribes from companies.
- Enterprise Florida, another older PPP, has faced new questions about shortfalls in the job creation performance of the companies it has

recruited. There have also been controversies over a performance bonus paid to its CEO and subsidies awarded to companies represented on its board.

- Two other older PPPs—the Rhode Island Economic Development Corporation and the Michigan Economic Development Corporation—have also faced new criticisms relating to job creation. The RIEDC is still litigating the biggest economic development scandal in Rhode Island history: its \$75 million loan to the now-bankrupt 38 Studios.

Despite this dismal track record, the allure of economic development PPPs remains alive in certain circles. North Carolina Gov. Pat McCrory, his commerce secretary and their allies in the state legislature are seeking to create such an entity. Their original enabling legislation contained some accountability safeguards, but that bill failed to pass because of a controversial last-minute amendment to allow fracking. To allow McCrory's plan to move on, lawmakers inserted privatization authority into a budget bill—but without any of the safeguards.

Informed by three more years of history, we draw a sharper policy conclusion here than in our 2011 report. We conclude that the privatization of economic development agency functions is an inherently corrupting action that states should avoid or repeal. This is true both because of the recurring and predictable abuses we document here, and because the soft economy is making the site location process—and the already corporate-dominated economic war among the states—even more asymmetrical against taxpayer interests.

In times of lingering high unemployment, painful budget cuts and struggling small business prospects, taxpayers deserve job-creation agencies that are transparent, ethical and effective. Privatization of state development agencies delivers none of these qualities.

Introduction

State efforts to promote economic development have traditionally been carried out by public agencies such as commerce departments, which both market the state to potential corporate investors and administer the subsidies that are frequently used to lure companies.

In late 2010, however, several newly elected governors called for a different approach. Claiming that their state agencies were no longer effective, the governors-elect called for the creation of “public-private partnerships” (PPPs) to take over the functions. At the forefront of this movement were four states:

Wisconsin: During his campaign for governor, Scott Walker made some references to overhauling the state Department of Commerce, but it was only after he was elected that he formally proposed replacing the agency with a PPP. His plan was based on a report produced by the consulting firms Deloitte—a major booster of PPPs of all kinds—and Newmark Knight Frank.¹

Ohio: In August 2010 gubernatorial candidate John Kasich proposed that the state Department of Development be dismantled and replaced with a private corporation called JobsOhio that would be headed by “a successful, experienced business leader.”

Iowa: On the same day Kasich’s plan was released, gubernatorial candidate Terry Branstad made a similar proposal, including the idea that the agency, which he dubbed the Iowa Partnership for Economic Progress, should be run by a CEO with a track record of “real world economic development success.”²

Arizona: Jan Brewer, who had been named governor in 2009 to replace Janet Napolitano (when she became U.S. Secretary of Homeland Security) and then won election in 2010 to remain in office, put forth a plan to scrap the state Department of Commerce and replace it with the Arizona Commerce Authority, which would be overseen by the private sector.

This sudden enthusiasm for the privatization of economic development agencies caught our attention at Good Jobs First. We looked into the issue and in January 2011 published *Public-Private Power Grab: The Risks in Privatizing State Economic Development Agencies*.³

The first thing we pointed out in the report was that economic development privatization was far from a revolutionary new concept. Instead, we found that it was a stale notion that over the course of two decades had been tried and abandoned in some states, while in others it had remained in place with a mixed track record. Ironically, one of the places where it had been tried and later dropped was Wisconsin—a fact that was conveniently ignored by Gov. Walker and other PPP proponents there in 2010.

Our report identified seven states—Florida, Indiana, Michigan, Rhode Island, Utah, Virginia and Wyoming—in which economic development PPPs overseeing business recruitment were still in operation as of early 2011. We examined their performance to see what lessons they offered to the four states looking to join their ranks. We also looked at Texas, which had turned over limited business recruitment functions to an entity called TexasOne.

The overall lesson was that privatization was not only not a panacea but in fact created a variety of problems. Among the issues we found were:

- Misuse of taxpayer funds (Rhode Island, Florida and Wyoming)
- Excessive executive bonuses (Virginia, Florida, Michigan and Wyoming)
- Questionable subsidy awards by the subset of PPPs that had a direct role in that process (Michigan and Rhode Island)
- Conflicts of interest in subsidy awards (Florida, Texas and Utah)
- Questionable claims by the PPP about its impact (Wyoming, Florida, Utah and Indiana)
- Resistance to accountability (Florida and Michigan)

Part of the problem, we found, is that the transfer of economic development functions from state agencies to public-private partnerships differs from what is typically meant by privatization: the contracting out of public services to for-profit companies

or the sell-off of public assets to private investors. Instead, economic development PPPs involve the creation of captive non-profit organizations and quasi-public entities that inhabit a gray area between the public and private sectors.

Proponents of PPPs see this as a virtue, arguing that these entities need to be free from bureaucratic strictures. Yet we found that the entities can end up lacking both the taxpayer accountability that is necessary in public agencies *and* the adherence to strict financial controls that is supposed to characterize well-functioning private-sector enterprises. The fact that PPPs often intermingle public funds and private contributions makes the problem even more pronounced.

We also argued that a case could be made that economic development PPPs are not examples of privatization at all. Given the control that governors have assumed over many of these entities, they can be seen instead as executive-branch power grabs over the economic development process. From this perspective, the point of the PPP is not to be “more nimble,” as proponents like to say, but instead to reduce or eliminate input and oversight from the legislative branch to which traditional

state agencies are subject. They also sidestep the integrity safeguards, including ethics laws and whistleblower protections, which apply to staffers protected by civil service regulations.

Based on these findings, we recommended that states fix their existing economic development agencies—if they actually have problems—rather than replace them with PPPs. In states where a PPP exists or is being proposed, we recommended that a series of safeguards be put in place:

- Maximum transparency in decision-making and finances, including adherence to state open records rules;
- For PPPs that oversee subsidy awards, maximum transparency concerning recipients of those awards and their performance;
- Strict conflict of interest rules regarding staff members and boards of directors;
- Strict rules barring favoritism and “pay to play” in connection with companies doing business with the PPP;

- Appointment of a public ombudsperson to monitor PPP activities and respond to outside complaints; and
- Respect for the rights of employees to organize a union (or to transfer a representation agreement that was in place when the entity was a government agency).

In this report we look at how things turned out in the states that, despite our warnings, proceeded to turn their economic development functions over to a PPP. We pay special attention to Wisconsin and Ohio, where the PPPs have turned out to be most problematic. We also examine new controversies in some of the states that already had PPPs when our previous report was published.

JobsOhio

JobsOhio, created in 2011 at the urging of newly elected Gov. John Kasich, has been plagued by accountability and transparency problems since the start. There have also been numerous political controversies, which is not surprising given that it is often difficult to distinguish between the agency and the governor's office. JobsOhio's first annual report featured Gov. Kasich prominently, and statements regarding the agency are as likely to be issued from his office as they are from JobsOhio itself.

Many of the transparency problems stem from the convoluted mix of public and private funding on which JobsOhio operates and the resulting confusion over the public's right to know how its funds are used. JobsOhio has also been embroiled in legal battles over the constitutionality of its structure.

Three months after taking office, Gov. Kasich held a press conference to reveal some details about the new agency. He outlined a transparency plan in which the agency would issue annual reports and hold quarterly public meetings, although it would

be exempt from public records and open meetings laws.⁴ Staff salaries would be made public and annual financial audits of JobsOhio's public funds would be performed by a certified public accountant. A chief investment officer, nominated by the board and approved by Gov. Kasich, would execute contracts, hire workers and spend private funds. After the initial \$1 million state appropriation for set-up and launch of the agency, the governor called for JobsOhio to eventually transition entirely to private funding.⁵

The Kasich Administration's proposed source of "private" funding for JobsOhio was as controversial as its announced transparency policies: profits from state-controlled liquor sales. The proposal called for "leasing" the state liquor profits (\$228 million the year prior) for up to 25 years to JobsOhio, which would eventually issue \$1.4 billion in bonds to pay for the use of the funds.⁶ Critics charged that this was not a fair market price for profits that could potentially amount to \$6 billion over the term of the agreement.⁷

While JobsOhio was ramping up, the state continued to award large subsidy packages to some major Ohio employers that threatened to leave the state. The headquarters of American Greetings Corporation, Inc., Diebold, Inc., and Bob Evans were awarded over \$200 million in combined subsidies in the spring of 2011 in controversial deals that were criticized for fueling suburban sprawl and succumbing to job blackmail.⁸ (Some of these deals ultimately failed to go through.) During his 2011 State of the State speech, Gov. Kasich announced that the state had already “clawed back” \$900,000 from subsidized companies that failed to meet job commitments. The statement was called misleading by Politifact Ohio, which determined that while notices of intent to recapture funds had been distributed, no funds had actually yet been recovered by the state.⁹

By April of 2011, ProgressOhio had filed a lawsuit (still currently pending) with the state Supreme Court, alleging that some key aspects of the law that created JobsOhio were unconstitutional, including the state’s position as a stakeholder in the corporation.¹⁰ The Kasich Administration responded in part to the lawsuit by introducing a number of amendments to the structure of the agency through the Senate

budget bill, including eliminating the Governor’s position as de facto board chairman and mandating that the Chief Investment Officer report to the board rather than directly to the Governor.¹¹ The state’s 2011 budget also authorized the plan to assign liquor profits to JobsOhio, which would receive an estimated \$100 million annually through the lease. (The remainder of the funds would be used to balance the budget.¹²)

The JobsOhio board of directors was announced at the agency’s first meeting in July 2011. Described by the *Columbus Dispatch* as “rich in business acumen and thick with ties to Gov. John Kasich,” the board included Mark Kvamme, a friend of and major campaign contributor to Gov. Kasich, and business leaders from subsidy recipients Bob Evans and Marathon Petroleum.¹³ Kvamme was appointed interim Chief Investment Officer. Six regional business groups and local economic development organizations would become affiliates of JobsOhio, providing business “leads” to the state agency, which would permit the smaller organizations to broker deals on its behalf as well as provide oversight.

Ohio’s Third Frontier Commission also awarded \$24 million in public funds to JobsOhio and its regional

partners, which are also private non-profit organizations (including regional Chambers of Commerce).¹⁴ ProgressOhio revealed that various affiliates of the groups receiving Third Frontier funds—executives, member businesses, and their political action committees—contributed more than \$430,000 to Gov. Kasich and Republican legislative candidates since 2007.¹⁵

By late 2011, the state had awarded 154 tax credits or loans to companies that pledged to hire 10,430 employees and retain 20,460 jobs over their contract periods.¹⁶ A few very large awards prompted questions about how exactly JobsOhio would select which companies to subsidize. JobsOhio refused to disclose how the state determines whether a subsidy deal would yield a positive return on investment, arguing that revealing the formula (which was developed by the Kasich Administration) would allow competing states to undercut Ohio.¹⁷

Meanwhile, the bill to allow JobsOhio to assign the state's liquor profits was approved by lawmakers, at a price of \$1.4 billion over 25 years. Included in that legislation were additional exemptions for JobsOhio from the state's open records law, which prompted the Ohio Newspaper Association to oppose the bill, calling

the provision “an invitation to more ambiguity and misinterpretation.”¹⁸ Attorney General Mike DeWine also voiced his opposition, noting “if public records were requested by JobsOhio and sent by the Department of Agriculture or some other department... once it was sent to JobsOhio, it would be immunized from disclosure.”¹⁹ The Kasich administration agreed to remove the offending language from the law so that only JobsOhio would be exempt from disclosure.

JobsOhio faced more controversy when it was revealed that the Bob Evans restaurant chain, despite its large subsidy award and the presence of company CEO Steve Davis on the JobsOhio board, would be closing two food production plants in Ohio and adding capacity in Texas. Kvamme (who would step down later that year) defended Davis and called Bob Evans “a good corporate citizen.”²⁰

The Kasich Administration again drew criticism late in 2012 with an ad campaign funded by JobsOhio touting job growth in the state. The \$1.4 million campaign ran both in Ohio and in some national publications, leading to questions about whether Gov. Kasich was using JobsOhio's funds to boost his chances for reelection. Cuyahoga County Executive Ed

FitzGerald sent a letter to Gov. Kasich saying: “These ads are an improper waste of state funds and seem intended to boost your gubernatorial re-election effort rather than actually help with economic development here in-state.”²¹ (FitzGerald may seek to run against Kasich in 2014.)

Although JobsOhio’s private donors had remained secret, the *Columbus Dispatch* determined through federal tax records that American Electric Power (AEP), a major utility provider for much of the central and southern parts of the state, donated \$2 million to JobsOhio in 2011.²² In an interview with the *Dispatch*, Kvamme’s successor John Minor claimed that once the liquor deal was finally complete the agency would not seek private donations any longer, contradicting Gov. Kasich’s original claim in 2011 that JobsOhio would rely only on private donations.²³

JobsOhio released its first annual report in the spring of 2013. It revealed that the agency received \$6.9 million in private donations during 2012, but JobsOhio would not identify the donors. It also redacted a three-page list of lost or cancelled projects, citing “trade secrets.”²⁴ The report also revealed that some employees of the agency were being paid in excess of \$225,000 per year—far more than

Gov. Kasich’s annual salary of about \$149,000.²⁵

In an analysis of public funds contributed to the young agency, the *Columbus Dispatch* identified a number of discrepancies between what JobsOhio reported it had received in start-up funding from the state, and what was reported in a federal tax filing by a subsidiary of JobsOhio. Multi-million dollar discrepancies were also identified between documents supplied pursuant to a public records request by the *Dispatch* and the agency’s annual report.²⁶ Ultimately, it was determined that JobsOhio was given a \$5.3 million *carte blanche* grant by the Development Services Agency (the successor to the Department of Development) to sustain itself prior to the arrival of the state’s liquor-based funds. Legislators had no knowledge of the funds transfer.

Prompted by claims that public money had been used by JobsOhio without lawmakers’ approval, state Auditor Dave Yost (like Gov. Kasich, a Republican) announced he had issued a subpoena for the agency’s financial records.²⁷ Proponents of the agency claimed that the state had no standing to audit private corporations or private funds, while Yost maintained that there was no way to determine

which funds are privately or publicly contributed. Amidst the growing public debate over the disputed right to audit the agency, Development Services Agency Director Christine Schmenk resigned.

Ultimately, JobsOhio delivered the requested records to Yost, but it simultaneously announced that it would be repaying over \$7 million in state funds, presumably to signal that there would be no further question about whether JobsOhio should be subject to audit by the state. The question of whether the state's liquor profits should be considered private or public funds remained, however.²⁸ JobsOhio and the Kasich Administration argued that the agency needed to be shielded from scrutiny by the state auditor's office, threatening that public transparency would damage Ohio's economy. The Governor's spokesman Rob Nichols implored lawmakers to "act quickly to prevent a chilling effect on job creation caused by a mistaken, overly intrusive interpretation of the auditor's duties."²⁹

By mid-2013, Gov. Kasich's wish was granted. A measure to prohibit the state audit was introduced and approved in the House within a few hours. The Auditor's office asked that Yost be allowed to testify prior to

the bill's passage but was ignored.³⁰ Less than 24 hours later, the Senate also passed the bill and sent it to the Governor.³¹ Yost delivered his objections to the fast-tracked bill in a letter to Senator Bob Peterson:

The amendment is complex, cross-references multiple other sections of the Revised Code, contains numerous exceptions, and features somewhat dense language. With only a few hours to review it, I am uncertain as to all its legal implications and its impact on other matters wholly unrelated to JobsOhio.³²

Blowback in the press was immediate. The *Plain Dealer* categorized the act as "shameful" in an editorial.³³ The *Columbus Dispatch*, citing Kasich's need to raise reelection campaign funds in a similar staff editorial, noted that with the stage set, the "environment is ripe for mischief."³⁴

Fears of cronyism were fueled a couple of months later when the *Dayton Daily News* revealed that six out of nine members of the JobsOhio board of directors had direct financial ties to state-subsidized companies, including Bob Evans, Sherwin Williams, Manta Media, Marathon Petroleum, and Procter & Gamble. (Some of the companies had received subsidies prior to their executives joining JobsOhio's board.)³⁵ A state Ethics Commission report released

in September 2013 found potential conflicts of interest with nine out of 22 JobsOhio employees, including six board members.³⁶

One JobsOhio leader responded by attacking the news media. “The people who are writing about us don’t know what the hell they’re talking about, and we’ve got to educate them,” board member and Cleveland Cavaliers CEO James Boland told the *Columbus Dispatch*.³⁷

That education may prove difficult in an environment now permeated with a culture of secrecy. JobsOhio’s

insistence that it be immune from public transparency has spread. Citing “trade secrets,” the Development Services Agency recently removed the dollar value of previously disclosed tax incentive awards from its disclosure website. Recognizing the public image problems caused by this secrecy, Gov. Kasich has ordered the Agency to provide this information to the public upon request.³⁸ It remains unclear whether the Development Services Agency will restore the subsidy-dollar data to its website. This is a significant setback for a state that was an early practitioner of online subsidy disclosure.

Wisconsin Economic Development Corporation

Gov. Walker and his allies in the state legislature restructured the Department of Commerce and transferred the state's economic development functions to a new privatized entity called the Wisconsin Economic Development Corporation (WEDC). Gov. Walker said that the WEDC would be central to his pledge to create some 250,000 new private-sector jobs in the state.

Unfortunately, many of the problems with PPPs we cited in our 2011 report came to fruition at the WEDC. It has been revealed that the agency has mismanaged public money, made questionable subsidy awards, lacked adequate transparency, resisted accountability, had conflicts of interest in awarding of subsidies, given management lavish executive pay, and made questionable claims about job creation. While all this was going on, over a fifth of WEDC employees were awarded merit bonuses.³⁹

Management of the WEDC has been in a constant state of flux. The first CEO, Paul Jadin, resigned amid two scandals in September 2012, saying he wanted a less public position.⁴⁰ The scandals

involved a subsidy award to an ineligible company and unauthorized expenditure of federal monies.

Prior to the scandals, Jadin claimed the agency had an advantage in its flexibility given to staff in tailoring subsidies to the needs of businesses.⁴¹ He also touted the fact that the WEDC was free from various state rules governing public entities, including procurement rules. But this "flexibility" almost immediately became problematic: the agency awarded a tax break to a company that was simultaneously bidding on a \$15 million state contract, a violation of state procurement rules.

Jadin stated publicly that the WEDC legal staff advised him that the offer to the company Skyward, Inc. was legal, because the WEDC was exempt from the state procurement rules. Gov. Walker disagreed with Jadin's decision, canceled the contract award, and restarted the subsidy award process for the company. This prompted state legislators to begin questioning the transparency of the WEDC. Gov. Walker attempted to rectify the matter by moving his deputy chief of staff,

Ryan Murray, into the role of Chief Operating Officer at the WEDC.⁴² The WEDC's Chief Financial Officer, Eric Schroeder, also left the agency.

Just after the questionable subsidy award was revoked, the federal Department of Housing and Urban Development (HUD) gave notice that WEDC had spent almost \$10 million in HUD funds without the legal authority to do so. It also said WEDC did not underwrite assistance given to businesses as required by federal rules, nor did it impose adequate fiscal controls and as a result transferred \$8.6 million into an account without HUD approval.⁴³

WEDC board members were furious to learn of the scandal in the newspapers.⁴⁴ Gov. Walker defended the decision not to inform the WEDC board, stating that the federal government routinely corresponds with the state and not all correspondences require communications with the board. Other board members saw it differently: "There appears to be a pattern emerging where they're just not providing full disclosure to the board of the key issues that they're dealing with," said Assembly Minority Leader Peter Barca.⁴⁵ Another board member stated, "The legislators on the WEDC

Board are supposed to be providing oversight of taxpayer dollars, but we can't play that role if important information like this is withheld from us."⁴⁶

When HUD directed the state to hire an administrator to adequately oversee federal money, Gov. Walker's appointee tasked with the matter resisted. Gov. Walker's Department of Administration secretary Mike Huebsch claimed that the WEDC had enough staff assigned to handle the matter.⁴⁷

As the scandal broke, Paul Jadin announced his resignation and took a job with a regional economic development organization. He denied that his resignation was tied to the HUD scandal. Gov. Walker named Reed Hall as his interim successor. The following month, October 2012, the WEDC's CFO, Mike Klonsinski, resigned his \$109,500 job, the second CFO to leave the agency. Later, after an expensive national search to find a successor CEO for the WEDC fell short, the governor named Hall as the new permanent CEO.⁴⁸ By February 2013, Hall was awarded a 54 percent raise, boosting his salary from \$120,000 to \$185,000.⁴⁹ By contrast, the governor of Wisconsin is paid less than \$145,000.⁵⁰

Also in October 2012, another scandal broke: a freedom of information request made by the *Milwaukee Journal Sentinel* revealed that the WEDC failed to track 99 past-due loans to businesses worth a total of \$12.2 million.⁵¹ At the time, borrowers were delinquent on \$2.5 million in payments to the state. The WEDC responded by firing the consulting firm charged with improving the agency's financial reporting. According to COO Ryan Murray (the governor's former deputy chief of staff), the agency knew of the tracking discrepancies for over a year and a half, but did not adequately act to address the problems. Murray admitted publicly that tracking on loans had stopped in June 2011, just before the WEDC launched.⁵²

Just one week before this information was made public, Jadin testified before the Legislature's Joint Audit Committee regarding the transparency and accountability of the WEDC, but did not mention the lack of loan repayment tracking. A state legislator on the committee called the incident, "a horrendous abuse of public trust," and was particularly disgruntled by the failure to inform lawmakers about the loan issue: "Now it just looks like they're hiding something. It's fishy."⁵³

In December 2012, following Jadin's departure, the non-partisan

Legislative Audit Bureau issued an audit documenting numerous problems that collectively portrayed a loose organizational culture at the WEDC. The audit stated that missing safeguards, staff turnover and sloppy accounting eventually resulted in delinquent past-due loans, and erroneous or unrecorded financial deals. It also found poor internal controls on staff spending, including a failure to approve one-fourth of staff check credit card transactions. These are "material weaknesses" and "significant deficiencies," the audit concluded. As the *Milwaukee Journal Sentinel* reported, these missing safeguards left taxpayer money "vulnerable to everything from simple mistakes and mismanagement to embezzlement."⁵⁴

The audit also found that the agency didn't adequately follow up to determine whether recipients of public subsidies were meeting job-creation pledges.⁵⁵ Concerns about those pledges were nothing new. An October 2012 report by WISPIRG detailed the WEDC's failure to account for monies clawed back (or recaptured) from companies that failed to meet performance requirements. In the agency's response to WISPIRG, it claimed that it lacked the staff capacity to compile such data.⁵⁶

Scandals had so tarnished the reputation of the WEDC by late 2012 that finding a third CFO was difficult. The job sat vacant for six months without a permanent CFO. In April 2013, the WEDC hired Scott Bowers, the former CFO of a lumber company to take the post, but just 24 hours later he resigned to become CEO of his old company.⁵⁷ The following month Stephanie Walker, an accountant with public and private sector experience, became the fourth CFO (no relation to the governor).⁵⁸

A second audit by the Legislative Audit Bureau was issued in May 2013, and it again found serious problems:⁵⁹

- For the first year and a half of operation, the WEDC did not verify whether companies getting subsidies had adequately met performance requirements as required by statute;
- During FY 2011-2012, the agency had failed to establish expected results for 10 of the WEDC's 30 economic development programs;
- The WEDC failed to indicate the purpose of over half the agency's credit card transactions, including season

football tickets the Governor purchased at a cost of \$1,789;⁶⁰

- The WEDC's board passed a resolution enabling the agency to create a non-profit dedicated to soliciting donations for economic development purposes. The WEDC failed to adequately clarify whether taxpayers would subsidize such efforts and whether the legislature would have oversight;
- The agency failed to disclose to the public known conflicts of interest regarding an IT consultant who was awarded a no-bid contract;⁶¹ and
- The WEDC hired an auditing firm even though the company was negotiating a subsidy deal on behalf of a client with the WEDC.⁶²

Legislators from both parties publicly expressed serious doubts about the agency. Sen. Robert Cowles, a member of the Governor's own party, stated, "I hope they can get their act together, but this is pretty darn bad... I'd say the jury is out whether this was a good idea to create this whole entity. . . I don't think there can be any more excuses. They've got to fix this thing."⁶³

Speaking to another news outlet, Sen. Cowles stated: “this audit shows there is a significant disconnect between our expectations of WEDC and the reality of their performance with regard to transparency and accountability.”⁶⁴ Senate minority leader Chris Larson, of the opposing party, said: “This is what we were saying from the beginning...there needs to be more accountability... more reporting...When you create a pseudo-government corporation, you want to make sure that you’re having the benefits of both, not the downsides of both.”⁶⁵

Just days later, another controversy erupted when the agency hired a new Public Information Officer, John Gillespie. A Madison television station revealed that Gillespie owed \$36,047 in back taxes to the state of Wisconsin.⁶⁶ Court records from Outagamie County also revealed that the Department of Workforce Development filed a warrant against Gillespie for \$7,770 in illicit unemployment insurance benefits. Gillespie resigned after the story broke, and the Governor’s office distanced itself from the episode. Within a week, legislators from the opposition were calling for better accountability at the troubled WEDC, including having a bi-partisan committee overhaul the agency. But

members of the Governor’s party blocked the proposal.⁶⁷ Legislator and WEDC board member Julie Lassa expressed displeasure with the structure of the board, stating that, “the board was designed to be a rubber stamp and doesn’t have any control over the agency.”⁶⁸

In June 2013, three Democratic senators called for a criminal investigation after the non-partisan advocacy group One Wisconsin Now issued a report revealing that executives at companies receiving subsidies from WEDC had contributed \$429,060 to Gov. Walker.⁶⁹ WEDC CEO Reid Hall defended the agency, without denying the accuracy of One Wisconsin Now’s accusations, claiming that he had been unaware of the contributions and insisting they played no role in decisions about subsidy awards.

By July 2013, Gov. Walker, apparently worried about the conflict appearances, signed into law a modest ethics reform bill.⁷⁰ It subjects WEDC to the same ethical standards as state agencies, and it requires members of the WEDC board and staff to notify the WEDC legal counsel of any controlling interests in a company negotiating, bidding for, or entering into a contract with the agency. It also prohibits employees or board members with financial interests in companies

seeking subsidies from negotiating deals or entering into contracts with those companies. The WEDC board also took away the Governor's power to hire and fire its top officials, reserving that authority for itself.⁷¹

Currently, the WEDC website claims that a total of 23,759 jobs will have been "impacted directly by investments made by WEDC in FY 12."⁷² This is unusually ambiguous language that clearly does not refer to job creation and does not even clearly take credit for jobs retained or improved by subsidy packages. The *Wisconsin Journal Sentinel's* Politifact website has been tracking job creation

progress in the state; through August 2013, it reported that the state had gained fewer than 90,000 jobs since Gov. Walker took office (towards his stated goal of 250,000).⁷³

The recurring news of problems at the WEDC have soured public opinion on it. A poll conducted by the University of Wisconsin at Milwaukee in July 2013 "shows a dramatic decrease in the public's confidence in the WEDC since November [of 2012]."⁷⁴ It found that 60 percent of Wisconsin residents have little or no confidence in the ability of the WEDC to bring jobs to the state, a 12 percent increase.

Arizona Commerce Authority

The Arizona Commerce Authority (ACA), created at the urging of Gov. Jan Brewer, replaced the state's Department of Commerce in early 2011. It is directed by a board comprised of state business leaders that is co-chaired by the governor. The Authority is funded by both public funds and private donations, and it controls a \$25 million "deal-closing fund" that is specifically used for infrastructure improvements to help lure out-of-state companies.

It wasn't long before the ACA stirred up controversy typical of economic development PPPs. In August 2011, Don Cardon was hired by the board for the CEO's job with a compensation package worth nearly \$1 million for a three-year term. Cardon's base salary was \$300,000 per year, plus a signing bonus of \$50,000 and a \$1,000 monthly vehicle allowance. Those funds were all provided by the state, plus Cardon was eligible to receive a \$75,000 performance bonus paid for by private funds subject to the approval of by the ACA board.⁷⁵ By comparison, the governor of Arizona is paid \$95,000 annually.⁷⁶

Cardon announced in January 2012 that he would resign and return to the private sector. With two years left on his ACA contract, he was compelled to

return his signing bonus (minus taxes paid on it).⁷⁷ It was later revealed that Cardon would receive a separate discretionary bonus worth over \$60,000 to be paid by the state, which would be reimbursed by the private nonprofit fundraising organization closely associated with the ACA, known as "Team ACA."⁷⁸ He has since moved from that group into real estate development.

However, instead of returning to the private sector, Cardon joined Team ACA as executive director. Team ACA collects private donations for the ACA and does not disclose the identities of its donors. Two known corporate contributors are Alliance Bank of Arizona and Apollo Group, which have together committed \$600,000 to the organization for economic development activities. Presidents of both companies sit on the board of Team ACA.⁷⁹

The ACA is again embroiled in controversy over its decision to loan \$2 million to the Snowflake Community Foundation for the purchase of a rail spur in Navajo County. Critics claim that the loan is outside the original mission of the Arizona Competes deal-closing fund, and that its approval opens the door for using the fund for other special projects in the future.

Indiana Economic Development Corporation

The controversy over exaggerated job-creation claims by the Indiana Economic Development Corporation (IEDC), which we discussed in our 2011 report, has continued to cast a shadow over the PPP. During the past three years there have also been allegations of foreign bribery solicitations by an IEDC contractor. The scandals prompted the state legislature to enact some transparency reforms in 2013.

The job-creation controversy first erupted in 2010, when investigative reporting by Indianapolis television station WTHR found that many of the deals IEDC took credit for had never happened, had fallen short of job-creation pledges, or had shut down.⁸⁰ WTHR's series, "Reality Check: Where Are the Jobs?" was led by reporter Bob Segall and won multiple awards (including an Emmy, a Peabody and a duPont). It estimated that only about 60 percent of the jobs claimed by IEDC were likely to materialize.

The IEDC and then-Gov. Mitch Daniels resisted answering questions about the issue. The governor's office refused multiple requests from WTHR to

discuss the job statistics, referring the queries to IEDC director Mitch Roob. Although Roob released additional data about shortfalls in aggregate job creation, he refused to release company-specific data, stating: "Most of what IEDC has is sheltered from public disclosure for competitive reasons."

After WTHR aired its initial investigation, Gov. Daniels reluctantly addressed the issue, but he continued to sidestep the central question by saying: "You seem to have discovered the obvious, namely that none of these jobs were ever scheduled to happen in the first year." Contrary to the governor's assertion, WTHR's reporting looked at job-creation promises and outcomes going back to 2006.

A 2011 state audit that was prompted by the WTHR series confirmed the station's findings.⁸¹ At companies described as "Indiana Economic Successes" in IEDC annual reports, 44 percent of the jobs never actually materialized. When the agency released its response to the audit, it offered alternative calculations that

excluded some 200 companies that had been designated as “not active” because they were not creating jobs.

When WTHR asked Roob to explain why he excluded the non-active companies, he replied: “You are blatantly misrepresenting the information and intentionally creating an incomplete picture of Indiana’s economic development successes.”⁸² By this Orwellian “successes” code language, Roob was apparently suggesting that IEDC could cherry-pick only those deals that panned out and brag about them while excluding many other costly failed deals.

Morton Marcus, former director of the Indiana Business Research Center at Indiana University, took issue with Roob: “I think the public wants a more full picture – not just the numbers that make IEDC look best”⁸³

As Gov. Daniels left office in 2012, the IEDC was seen as a blemish on his record. As the *Indianapolis Star* said in a staff opinion round-up of his record:⁸⁴

The first bill Daniels signed as governor created the Indiana Economic Development Corp., a public-private enterprise designed for speed and flexibility in pursuing businesses. The agency has played an increasing role in drawing new businesses to Indiana or

encouraging existing firms to expand. But overall, Indiana has lost private-sector jobs over the past eight years, and the IEDC has backed several troubled companies or entrepreneurs, including a “special assistant” to the commerce secretary who was accused of fraud and extortion in China. Even some in the governor’s own party, having grown concerned about accountability at the highly secretive agency, proposed a bill last week aimed at making the IEDC more transparent.

The *Star*’s editorial reference to fraud and extortion was to Monica Liang, who had been given a contract by IEDC to help recruit companies from China. In 2011 Chinese officials sent a complaint to Gov. Daniels accusing Liang of abusing her position. She allegedly solicited what amounted to an \$8,000 bribe from one company and got a Chinese businessman to wire \$50,000 into her personal account.

IEDC terminated Liang’s contract but did not refer the matter to law enforcement officials. On the same day that termination took place, Roob announced his resignation from the IEDC. Asked by a reporter whether the two events were linked, Roob said, “Don’t be preposterous.”⁸⁵

The Monica Liang incident prompted even lawmakers from Daniels’ own party to demand reforms at IEDC,

something their opponents had been pushing for since the WTHR investigation. A key issue was whether the state exercised adequate oversight over IEDC: Liang's \$100,000 contract, for example, was beyond oversight of both the attorney general and the Department of Administration.

In March 2013, Gov. Mike Pence signed into law a new transparency bill which addressed some issues at the IEDC. The bill makes incentive agreements subject to open records requests, posts more data online in a transparency portal, requires the IEDC to more accurately report both projected jobs and actual job outcomes as well as the compliance status of recipients

and whether clawbacks occurred. However, in a major shortcoming, the new law allows IEDC to post job-creation numbers only *in aggregate*, not on a company-specific basis.⁸⁶ The transparency portal does not yet reflect all these changes.⁸⁷

The reforms have also not put an end to IEDC controversies. In April 2013, it was revealed that \$345,000 in subsidies were made available to a company owned by the son of a prominent legislator, Mainstreet Property Group.⁸⁸ Gov. Pence asked IEDC to conduct further review on the subsidy package, and a review committee approved the deal.⁸⁹

Enterprise Florida

Florida started to privatize its economic development functions in 1992 with the enactment of Enterprise Florida, Inc. (EFI), a public-private partnership responsible for recruiting companies to the state. The Florida Department of Commerce was abolished in 1996 when most of its responsibilities were transferred to a greatly expanded EFI.⁹⁰

Associated Industries of Florida (AIF) wrote to its members during the original 1992 enactment debate that: “If it works, Enterprise Florida will help the state’s economic future. If it fails, Enterprise Florida will be a boondoggle to the entities represented on the board, and an embarrassment to the state.” AIF eventually supported the legislation creating EFI but “with reservations because AIF is not satisfied that sufficient safeguards against abuse by board members were built into the structure of Enterprise Florida.”⁹¹

AIF’s skeptical language likely reflected the fact that the EFI legislation was based in large part on recommendations made by AIF’s leading competitor, the Florida

Chamber of Commerce, which had published a report in 1991 outlining the idea, entitled “Enterprise Florida: Partnership for a Competitive Economy.”⁹² EFI’s founding was wrapped in rhetoric about addressing wage stagnation by developing higher value-added technology clusters, but it also offered private donors the ability to keep their identities secret.⁹³

EFI is governed by a 61-member Board of Directors composed of public and private sector leaders; the Governor is the chairman. The board hires the EFI President & CEO, who also holds the title of Secretary of Commerce and serves at the pleasure of the governor. However, despite a title which normally connotes a cabinet position, he is “not a state official and is not a state employee.”⁹⁴ (The executive director of DEO is subject to Senate confirmation.) Gov. Scott’s official organizational chart shows that the EFI President & CEO/Secretary of Commerce reports directly to the Governor, not the Department of Economic Opportunity (DEO).⁹⁵

EFI operates as a vendor to DEO, a state agency. EFI’s staff works with

prospect companies, negotiates subsidy deals and recommends them to DEO, which in turn approves, administers and monitors the economic development subsidy deals.⁹⁶

In the last few years, EFI has been criticized for serious shortfalls in job creation results at the companies it recruited. In October 2011, DEO released a report disclosing that about one-third of the 729 subsidy contracts that Florida had signed with businesses over the past decade did not bring promised results.⁹⁷ A few weeks later the *Orlando Sentinel* reported that since 1995 only one-third of 224,000 promised jobs materialized.⁹⁸

Integrity Florida, a government watchdog group, has been highly critical of EFI's transparency and accountability record. In an April 2012 report, the group listed a series of "corruption risk indicators" for EFI including: EFI's emphasis on confidentiality; the fact that its board members may also receive subsidies and are also allowed to be vendors for the organization; the failure to hold all of its board meetings in public; and the ability of companies to buy their way onto the board.⁹⁹ Dan Krassner, the Executive Director of Integrity Florida, noted that more than \$20

million in subsidies has gone to EFI board member companies, including Publix, Darden, Embraer, Harris, and Lockheed Martin. He also pointed out that the EFI board had approved vendor contracts to other board member companies, including Wells Fargo, TD Bank, and Blue Cross Blue Shield (Florida Blue).¹⁰⁰

In a February 2013 study, Integrity Florida found that EFI has failed to meet its original job-creation objectives and had not been able to secure the required amount of private funds. (EFI is obligated to obtain 50 percent of its funding from private sources.)¹⁰¹ In the fiscal year ending June 30, 2013, more than 80 percent of EFI and its consolidated entities' total revenues came from state funds while a little more than 2 percent came from private investment contributions.¹⁰²

Despite these issues, for the 2012-2013 year Enterprise Florida President & CEO/Secretary of Commerce Gray Swoope received a \$70,000 performance bonus on top of his \$230,000 annual salary from the Enterprise Florida board.¹⁰³ Integrity Florida, Progress Florida and The Tea Party Network criticized the fact that the bonus was based on *promised* jobs rather than the number actually created.¹⁰⁴ By contrast, the governor of Florida is paid a little more than

\$130,000 a year, although Gov. Rick Scott, a wealthy former businessman, accepts only one cent per month.¹⁰⁵ The EFI staff was paid more than \$2.1 million in bonuses in the 2008-2009 through the 2012-2013 budget years, with the annual total almost doubling—to \$630,000—over those five years.¹⁰⁶

The state legislature, suspicious of the way EFI was handling public money for business recruitment, cut the 2013-2014 budget for EFI-bargainable subsidies from \$111 million to \$45 million (EFI and Gov. Scott had requested \$278 million). “The reduction in the subsidies budget could be related to Enterprise Florida’s built-in conflicts of interest and questionable results...Lawmakers may be losing confidence in the entity,” Krassner commented.¹⁰⁷

EFI’s negative press coverage also pushed Florida lawmakers to increase the transparency and accountability of economic development efforts. In 2012, the legislature renewed a law allowing confidentiality of subsidy deals but shortened the secrecy period after a deal is negotiated from two years to six months.¹⁰⁸ In 2013, the legislature enacted measures requiring subsidy programs and deals to be regularly reviewed for effectiveness by an outside auditor and requiring online posting of the evaluations.¹⁰⁹

Swoope’s salary is once again the focus of controversy following reports that EFI’s board is expected to approve a new employment contract that will boost his base pay to \$275,000 and allow for a bonus of \$100,000.¹¹⁰

Privatized Agencies in Other States

Along with Indiana and Florida, there have been controversies over the performance of older public-private partnerships in several other states. The most notable scandals have been in Rhode Island, Michigan and Texas.

Rhode Island Economic Development Corporation

In our 2011 report, we mentioned the scandal stemming from a \$75 million loan made by the Rhode Island Economic Development Corporation (RIEDC) to a risky video game start-up called 38 Studios founded by former Boston Red Sox pitcher Curt Schilling. Since then, the company has gone bankrupt and fallout over the deal has been a major story in the state.

Missteps were present from the beginning. The RIEDC rushed the loan through without adequate due diligence.¹¹¹ In fact, officials began drafting the deal nearly two months before the state legislature even enacted the loan program used to subsidize the company. It later came to

light that an RIEDC official who played a significant role in the deal sought employment at 38 Studios just 6 weeks after the transaction closed.¹¹²

In May 2012, 38 Studios went bankrupt and the company failed to pay back the loan secured by taxpayers. Despite an initially reported price tag of \$75 million, it was later revealed that the state would be on the hook for more, possibly as much as \$112.6 million, because estimates did not include interest payments on the bonds.¹¹³ Taxpayers will continue paying off the bonds for the failed loan deal for years into the future, primarily to avoid risking a diminished bond rating.¹¹⁴ In recent months, the state has eliminated the loan program created to subsidize 38 Studios.¹¹⁵

After the company went into bankruptcy, RIEDC executive director Keith Stokes resigned.¹¹⁶ Later, multiple RIEDC board members left after the Governor asked all board members to resign.¹¹⁷

The RIEDC has recaptured little of taxpayer subsidies in the bankruptcy: it auctioned off the 38 Studios

headquarters for just \$650,000.¹¹⁸ A state Senator said of the 38 Studios debacle, “You’ve never seen a scandal of such historic proportions essentially disappear with little or no accountability for the havoc that was wreaked.”¹¹⁹

In September 2012, the Rhode Island Public Expenditure Council, a business-backed group, released a report blaming much of the failures at the RIEDC on its quasi-private structure.¹²⁰ The report lays out several options, but ultimately concludes that the best option is to bring economic development functions back into state government.¹²¹

Investigations and legal actions around 38 Studios continue. The federal Securities and Exchange Commission recently announced its own investigation.¹²² Since June 2012, the RIEDC has spent \$707,691 on legal fees. The agency is currently suing 14 defendants, including Schilling, over the failed loan deal.¹²³

Michigan Economic Development Corporation

In June 2011, Michigan eliminated or reduced some of the most heavily used economic development subsidy programs administered by the

Michigan Economic Development Corporation (MEDC).¹²⁴ During the previous Governor’s term in office, MEDC had a role in subsidizing some 500 companies to the tune of \$3.5 billion. The elimination of major programs such as Michigan Economic Growth Authority tax credits and Advanced Battery Tax Credits seemed to represent a new “economic gardening” approach to economic development. Unfortunately, problems still persist.

A recent report from the Michigan Auditor General found that the MEDC had made inflated job-creation claims for its Michigan Strategic Fund program.¹²⁵ In a vaguely worded report, Auditor General Thomas McTavish said that, regarding eight Strategic Fund-subsidized companies, MEDC had told legislators they had created 75 percent of projected jobs. But the audit found only 19 percent of jobs had materialized—and that excluded one company that had gone bankrupt.

TexasOne

TexasOne, the primary activity of the state’s privatized economic development marketing arm created under Governor Rick Perry, continues to undergo scrutiny. In a September

2013 report, Good Jobs First examined Gov. Perry's unprecedented partisan job-piracy trips to six states, all led by governors of the opposing political party.¹²⁶

Between February and September 2013, Gov. Perry staged the high-profile trips to California, Connecticut, Illinois, Maryland, Missouri, and New York. The trips were accompanied by about \$1.8 million in paid radio and television advertisements, featuring the Governor himself. TexasOne sponsored the trips and advertisements. Although Gov. Perry's press releases state that no state taxpayer money is used for the ads or his travel and accommodations, the Good Jobs First report revealed that local sales tax dollars are a major source of funding for local economic development corporations, the most numerous dues-paying members of TexasOne.

TexasOne is also supported by corporations, some of which have received or negotiated subsidy packages or contracts from the state of Texas. For example, Shell Oil pays \$50,000 into TexasOne each year and recently received a \$2 million subsidy award for its Motiva joint venture refinery.¹²⁷ One of the largest contributors to TexasOne is tax-break consultant G. Brint Ryan's

firm, Ryan LLC. It has represented major companies seeking subsidy packages, including Exxon Mobil.¹²⁸ In fact, the *New York Times* reported, 82 out of 222 enterprise zone subsidy packages were awarded to companies represented by Mr. Ryan's firm. TexasOne contributing companies also include executives who have received prestigious appointments to boards of universities by Perry.

North Carolina Partnership for Prosperity (Proposed)

The idea to privatize the North Carolina Department of Commerce emerged immediately after Pat McCrory was elected governor in November 2012. In a private white paper, McCrory's transition team made a case for the privatization of the state's economic development functions.¹²⁹ The paper argued that the new approach was required by shrinking federal and state budgets for economic development, by increasing global competition, and by the need for better "sales and customer service experience" for businesses. After reviewing the public-private-partnership models in Florida, Indiana, Michigan, Missouri, Utah, and Virginia, the paper outlined a new entity to be called the North Carolina Economic Development Partnership.

As proposed, the Partnership would have been a private non-profit corporation that would enter into a contract with the Department of Commerce to perform its functions. The board would include the governor's and the House and Senate leaders' appointments, business leaders, and local economic developers. An Executive Committee

would be responsible for managing projects, determining strategic direction of the organization, and hiring and supervising executive officers. The Governor would chair both the board and the executive committee.

To avoid over-reliance on business, a major portion of the Partnership's funding would come from the State's General Fund. Private funds would come from the sale of memberships and from donations by companies represented on the Board of Directors. The Partnership was justified by its ability to raise private money and streamline the recruitment process.

The transition proposal, apparently mindful of the recurring accountability problems at other states' PPPs, called for "provid[ing] maximum transparency relating to the incentive decision-making process and the use of funds" and "rigorous disclosure and accounting practices...and public and private accountability for all state funds."

The privatization effort was officially announced on April 8, 2013 by Gov.

McCrory and Secretary of Commerce Sharon Decker.¹³⁰ They unveiled only a broad plan but it was consistent with the recommendations of the transition paper, which had not yet been made public (it was leaked to Raleigh TV station WRAL a month later¹³¹).

The governor chose a slightly different name, the North Carolina Partnership for Prosperity, but he followed the white paper in recommending that the entity operate as a non-profit corporation with a board headed by the governor and composed of “legislative appointees and private-sector officials.”¹³² The Partnership would raise private dollars for economic development purposes (however, the plan did not mention private membership dues that the white paper had outlined). It would take over efforts to recruit, retain, and expand businesses in the state from the Department of Commerce. The plan would also eliminate regional organizations, an idea not included in the white paper.

The legislative version of the plan, Senate Bill 127, offered more details.¹³³ Besides privatizing many state economic development functions, the bill proposed to reorganize regional development by defunding seven publicly and privately sponsored regional development partnerships

and by eliminating 16 state-chartered Councils of Governments. In their place, the bill called for eight new Collaboration for Prosperity Zones, which would be under the authority of the Department of Commerce. Each zone would be responsible for the creation and coordination of regional economic development strategies. Staff from departments of Transportation, Natural and Economic Resources, and Commerce would share office space in each zone.

One of the existing partnerships the bill would have eliminated is the Charlotte Regional Partnership, whose membership includes both North and South Carolinas counties. A new Prosperity Zone in the Charlotte area would have ended this interstate cooperation.

The main goal of the SB 127 was to establish a framework for a public-private partnership and give the Department of Commerce authorization to contract out most of its functions to the Partnership, from tourism and marketing to business recruitment and recommendation on subsidies. Excluded would be the handling of federal funds, such as Community Development Block Grants, and functions of the Division of Employment Security, which administers unemployment insurance.

The legislation would have allowed the Department of Commerce to retain control of subsidy programs like the One North Carolina Fund and Job Development Investment Grants. The public-private partnership, however, would negotiate and recommend subsidy recipients to the Department of Commerce.

The board of the Partnership was to be chaired by the governor and composed of 16 additional voting members, half appointed by the governor, and one-fourth each by the heads of the House and Senate (so that the governor would have a controlling bloc of nine). The board members were to represent a variety of business sectors and geographic areas of the state. They could not be state officials or employees.

The legislation included safeguards to deter pay-to-play and to ensure transparency and accountability. Leaving final approval and administration of subsidy programs to the state agency was one of them. Another important one was a provision that bans any board member or his or her family and businesses from profiting from any action of the board (thus, board members apparently could not receive subsidies for their companies¹³⁴).

Other safeguards include creation of an Economic Development Oversight Committee (composed mostly of state officials), which would be required to audit the Partnership at least biennially (the audit would be performed by either the State Auditor or internal auditors of the Department of Commerce) and would monitor and oversee its contracts with the state. Any violation of the contract would be enforced by the state attorney general. There would also be a limit on the amount of public funds that could be used for salaries, a requirement that the Partnership would be a subject to public records laws, and a requirement to develop and to publish a code of ethics. The Secretary of Commerce also publicly declared that the corporation “will be subject to all the same records laws and ethics laws that the state of North Carolina is exposed to...It’s only smart because we need to operate with full disclosure.”¹³⁵

Despite these safeguards, the bill was criticized from both the left and the right. The Budget and Tax Center at the North Carolina Justice Center issued a report outlining problems in the legislation.¹³⁶ It noted that, since the Partnership would be responsible for proposing subsidy awards and the governor would chair the Partnership board, it might be difficult for the Commerce Department to reject the

Partnership's suggestions. Thus, the report pointed out, there was still room for conflicts of interest in the prospect selection and subsidy-granting processes. The report argued that the legislature should improve accountability measures for the Partnership and for the new Prosperity Zones.

The executive director of the N.C. Institute for Constitutional Law, Jeanette Doran, argued in a *News & Observer* op-ed that, instead of privatizing the Department of Commerce, the state should reform transparency and accountability of its subsidy negotiation process. She recommended that the state mandate “public disclosure of negotiations and incentive promises at least 30 days prior to legislative or executive action committing us to any economic development package” for both the state and local government agencies. She also recommended the state create an independent ombudsman position to scrutinize deals, and that state press releases announcing deals include hard job-commitment numbers instead of high-end estimates including ripple-effect jobs.¹³⁷

Another limitation of the accountability provisions of the bill is that they do not address the rules surrounding corporate contributions to the Partnership.

SB 127 was moving ahead in the Legislature without an organized opposition. It seemed that the bill would soon become law. However, two days before the legislative session ended and before the final vote on the bill, an amendment was added to it that would lift a state moratorium on hydraulic fracturing (commonly known as fracking) and to use taxes on the process as a new revenue stream for economic development subsidies. The amendment did not include details about the new subsidies or project how much money would be raised. The amendment was supported by the Secretary of Commerce, but lawmakers did not feel comfortable making such a quick decision on it (fracking has provoked a lengthy debate in North Carolina, as it has in other states such as New York, Pennsylvania and Ohio). As a result, SB 127 remained in limbo as the session ended.¹³⁸

The use of fracking to fund new subsidies became more controversial in the wake of press reports that during a meeting with business and community leaders, Secretary Decker said she wanted a big deal-closing fund similar to what Gov. Rick Perry has in Texas, adding that “‘energy partners’ are ready to ‘provide us with the money.’”¹³⁹ She also told the group: “I’m very selfish – the governor gets tired of hearing it...He says, ‘Lord,

mercy, you're the greatest advocate for fracking I've ever seen.' And I said it has nothing to do with fracking. I want those dollars in economic development."

Even though SB 127 did not pass, the privatization of the Department of Commerce is not derailed. The state budget for FY2014 includes a one sentence provision that allows the Department of Commerce to use up to \$1 million to "reorganize positions and related operational costs within the Department to establish a public-

private partnership which includes cost containment measures."¹⁴⁰ The N.C. Economic Development Board is working on a strategic plan for the new entity, the Secretary of Commerce is about to hire a new executive director for it, and, as of early September 2013, the Partnership was incorporated as a 501(c)(3) organization.¹⁴¹ Ominously, the terse budget bill language contains none of the accountability safeguards that SB 127 included.

Policy Conclusion

We conclude that the privatization of economic development agency functions is an inherently corrupting action that states should avoid or repeal. It is another aspect of how, in a soft economy, some public officials seek to exploit people's need for jobs. We base this conclusion on both the recurring—and frankly predictable—abuses we document here and upon our analysis of the site location process and the economic development profession. Specifically, we conclude that:

Economic development in the United States is already corporate-dominated. The system of corporate site location that evolved in post-war America, as shaped by site location consultants Fantus and its progeny who have a direct financial self-interest in stoking the economic war among the states, already makes for highly asymmetrical bargaining power. Companies play states and cities against each other with ease as public officials remain confined in a “prisoners’ dilemma.” Even without privatization, taxpayers are already represented by public officials who are hamstrung.

Creating a new, corporatized layer of bureaucracy is antithetical to accountability. When private executives become governing directors of sole-source corporations that are performing inherently governmental functions, when public and private monies are intermingled, or when transparency or ethics or audit and oversight systems are in any way compromised or become subject to the whims of the current governor, what is already a corporate-dominated system becomes riper for corruption.

As our case studies repeatedly document, the cultures of these private development corporations fail on such basic competencies as vetting deal applications or accurately monitoring and honestly reporting job-creation outcomes on costly subsidy packages—not to mention vetting of staff and oversight of spending. Creating a captive contractor also creates redundancies and inefficiencies between the private entity and commerce department.

Deal flow is depressed, giving companies even more power;

megadeals are increasing. As we recently documented *The Job-Creation Shell Game*, the numbers of deals for which states and cities can compete were markedly depressed even *before* the Great Recession and have yet to recover to even *half* of their peak levels of 1998-2000. That means corporations and site location consultants have even more asymmetrical bargaining leverage, and it apparently accounts for the sharp surge in the number and cost of “megadeals”—or big-ticket subsidy packages—since 2008 that we documented in our recent *Megadeals* study.

Privatization favors big business when small business deserves more help. The privatization structures we describe here, including the increasing use of corporate seats for sale on governing or advisory boards, absolutely favor large businesses that have the money and executive staff time to pay and play at such levels. But small businesses already get short shrift in economic development resource allocation, and they are still suffering the most in the Great Recession’s aftermath.

There is no evidence that public agencies are not “nimble.” Finally, we cringe at knee-jerk talking points about a privatized development

corporation being more “nimble” than a state agency. In all of our years tracking development deals, we have yet to hear of a state agency that lost an important deal because it failed to provide labor market or real estate or incentive data in a timely manner. The vast majority of best-known “trophy deals,” or high-profile projects landed by states (think Mercedes in Alabama, Boeing in Washington State, or Toyota in Kentucky) were landed by public agencies. Far less glamorous are the thousands of deals, big and small, that public agencies and their dedicated staffers put together every year.

To be sure, the work has changed. Everyone in the public sector economic development profession knows that the pace of such work has accelerated with the rise of the internet and ensuing business practices, and they have adapted accordingly, often creating innovative new web-based tools and information systems.

There is nothing inherently inferior about public employees’ ability to perform the kinds of analyses that inform smart economic development strategies, such as industrial clusters, technology adoption or customized training. In economic development, institutional memory and cumulative expertise matter, and so does close

integration between offices that recruit companies and those that provide training and technical assistance. Indeed, we suspect that experienced public employees are insulted and demeaned to see their expertise cast aside and their work given to less-qualified people, perhaps for higher pay.

In these times of severe economic development bargaining asymmetry between the private and public

sectors, taxpayers are best served by experienced public-agency employees who are fully covered by ethics and conflicts laws, open records acts, and oversight by auditors and legislators.

Amidst lingering high unemployment, painful budget cuts and struggling small business prospects, taxpayers deserve job-creation agencies that are transparent, ethical and effective. Privatization delivers none of these qualities.

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