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BEFORE THE
COMMITTEE ON ECONOMIC DEVELOPMENT OF THE CITY COUNCIL
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Chairman Sanders and members of the committee, thank you for inviting IBO to testify at this hearing today.

Last year, at a Councilmember's request, IBO reviewed the Economic Development Corporation's annual reports on its business retention/economic development agreements. IBO concluded that EDC's report, which is mandated under Local Law 69 of 1993, does provide a significant amount of data on tax incentive and financing agreements. However, because of significant shortcomings in its scope, methodology, and accuracy, the report does not offer the information needed to adequately assess and compare specific deals, nor to evaluate the underlying policies.

We also noted how often the reports were filed late, and how the distribution of the reports was so limited. These concerns have become less important. EDC is now up-to-date in the publications of the reports, and in contrast to the past IBO was able to obtain copies of recent reports quite easily.

Nonetheless, efforts to improve oversight of economic development deals and particularly compliance with the job retention commitments made by the businesses receiving benefits through such deals will likely be frustrated without major changes to the Local Law 69 report.

IBO's study found significant problems with how the fiscal costs and benefits of economic development agreements are estimated. Because costs tend to be understated and benefits tend to be overstated, the Local Law 69 report generally exaggerates the return on the city's investment in economic development agreements. To cite just a few of the reasons why the costs of the agreements are underestimated:

- *Costs are not reported for all years.* The report only includes costs for the first eight years of each deal, although many benefits continue well beyond the reporting period. For example, property tax exemptions can last 15 to 20 years.

- *Some agreements are omitted.* The report only covers deals that cost the city more than $250,000 or retain more than 25 jobs—smaller agreements are not included in the report and not reflected in the report's totals.

- Some types of costs are excluded. One significant type of foregone tax revenue— the tax exemption on interest income received by Industrial Development Agency (IDA) bondholders—is omitted from the report.

Similarly, the reports overestimate the benefits that flow from the agreements. The primary reason is that the report's methodology is based on the extreme assumption that if not for the deal, the firm, all of its employees, and many of its suppliers and their employees would leave the city. Under this assumption, even the property taxes paid by a firm on its land and its building are assumed to be lost without a deal—despite the fact that taxes are paid by property owners regardless of whether or not the space is occupied.

Employment data are keys to the oversight and evaluation of the economic development deals. An accurate projection of the number of jobs expected to be retained or created as a result of any business retention deal is the basis for calculating the agreement's potential economic and fiscal benefits. And the actual employment level of the firms must be compared to these projections to determine whether the deal has generated the projected benefits—and if not, whether any "clawback" provisions should be enforced.

Unfortunately, the Local Law 69 reports fall short in providing this needed employment information. Let's focus on two basic employment figures reported: the jobs retained (or base employment) projection made at the time that the deal is negotiated, and the actual number of jobs at the firm's project site in the years after the firm has received the benefits.

The "jobs retained" number in theory represents the number jobs that the beneficiary firm will be retained in the city as a result of the assistance provided by EDC, and it forms the basis of calculating the economic benefits that derive from the deal. Unfortunately, the job retention data shown in the reports are unreliable. Local Law 69 does not require that the job retention data be determined from a verifiable source such as the state's unemployment tax records. The job retention numbers in the report are based simply on information provided by the company receiving the benefits. A 1995 Comptroller's audit found that some firms deliberately under-reported their "base employment" projections, making any job creation above and beyond the base projection look good for the firm and, under certain deals, generate additional benefits. The projection for any particular deal is also inconsistent over time—once a firm reports its base level of employment when the deal is struck, there is no reason for that figure to change, though sometimes the figures change from year to year when a new volume of the Local Law 69 reports are produced.

To measure the potential benefits of any economic development incentive package, the projection of jobs being retained by the incentives needs to be as accurate as possible. If the projection is too low compared to the actual level of employment, then all calculations of that project's benefits will be overstated.

The data on the actual levels of employment occurring after benefits have been received—awkwardly labeled "Number of company jobs used in analysis"—are also unreliable. EDC's own documentation of the Local Law 69 reports concedes that the reporting of the actual employment numbers is spotty. The numbers are inconsistent in terms of how they are obtained—sometimes they are based on the numbers that the firms itself provides, and EDC does not take any steps to independently verify the numbers given to them. If no information is provided by the companies, the numbers are based on estimates made by EDC, with EDC employing three different methodologies for deriving its estimates. The Local Law 69 reports do not indicate which methodology is being used to derive the estimates or even whether the actual employment numbers are supplied or estimated. Even if the base employment projections are reasonable, without accurate information on the number of jobs actually retained it is not possible for the Council or the public to interpret a project's success or failure in creating or retaining jobs.

Finally, even if both the numbers for projected and actual employment level were reported accurately and consistently, the Local Law 69 reports do not detail the specific terms or performance requirements of the agreements, including any possible consequences, such as clawback provisions, for a firm which fails to meet its job retention and creation targets. Without this information, neither the Council nor the public can determine whether a firm is meeting its obligations and to broadly evaluate the success of EDC's economic development/business incentive deals.

Copies of IBO’s June 2001 report, *Full Disclosure? Assessing City Reporting on Business Retention Deals,* are available on our Web site at www.ibo.nyc.ny.us;