NEW YORK STATE Economic Development Council

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# *MEMORANDUM*

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**TO:** Senate and Assembly Fiscal and Economic Development Committees

**FROM:** Brian McMahon

**RE:** 2012 budget testimony

Good Morning Chairman DeFrancisco, Chairman Farrell, and members of the legislative fiscal and economic development committees. I am Brian McMahon, Executive Director of the New York State Economic Development Council. It is a pleasure to be here this morning.

For the second year in a row, Governor Cuomo has proposed a state budget that closes a projected deficit without spending more money, raising taxes or fees, or increasing taxpayer supported debt. Just as the business community took notice of New York's fiscal mismanagement in past decades by leaving the state or not investing here, recent fiscal constraint has been recognized by the business leaders and site location consultants in and outside of New York, and will improve the state's competitive standing when the current economic cloud is lifted. Nothing will strengthen economic development efforts more in New York State than continued commitment to fiscal responsibility and lowering New York's cost of doing business.

While we have righted the ship, we have not yet turned it around. To do that, three overarching objectives must be achieved:

1. New York needs to reduce the cost of building and operating a business here. The Tax Foundation just released its 2012 Business Tax Climate Index. New York was 49th, just behind New Jersey. NYSEDC believes the state's priority should be to reduce the tax burden on manufacturers. They have the greatest economic development value, the highest multipliers, and pay the highest wages.

2. New York must begin to moderate its regulatory environment, which is considered one of the most hostile in the country. This does not necessarily mean relaxing standards, but it does mean providing timely responses to permit and funding requests. When regulatory approvals are prolonged, capital cannot be deployed and jobs cannot be created.

3. New York must unshackle its local governments by removing mandates that everyone knows are antiquated and debilitating to local taxpayers. Last year, the state enacted the real property tax cap, which restricts local taxing jurisdictions tax levies. This year, the state should give local governments the tools to effectively manage and reduce expenditures that are linked to current mandates.

Economic development has changed significantly in the last 15 years. Fifteen years ago, economic development focused on external business attraction using economic development incentives. But today, the ability to compete also means having a skilled workforce, shovel ready sites, partnerships with universities, and broadband access. Economic development today requires understanding the tech transfer process, the importance of historic preservation and affordable housing, principles of smart growth, and the importance of business retention and expansion as the main pathway to economic growth.

Economic development models aimed at external attraction projects have been replaced by economic development strategies that focus on "growing from within." We know that the best promoters of our communities are business leaders who make decisions to grow here because of a competitive, entrepreneurial environment. In order to create that environment, however, New York must integrate its state and local workforce, economic development, and higher educational services into a connected, seamless economic development delivery system that provides timely and relevant services to businesses that have the greatest opportunity to expand rapidly. We think this should be a priority focus of the Regional Economic Development Councils going forward.

**Regional Councils**

The Regional Council process consists of two component parts: strategic planning and the Consolidated Funding Application process.

**Strategic plans:** Without exception, the Regional Councils developed their strategic plans from the holistic perspective of economic development described above. While the time frame for developing strategic plans was compressed, the process brought together opinion leaders from throughout the regions to meet, discuss, and agree on a blueprint for economic growth for the region. The importance of this cannot be overstated. It places everyone on the same page and gives the public a basic understanding of how the region will grow in the future.

This process was very valuable, but the plan cannot be allowed to collect dust on a shelf. These plans should be periodically reviewed by the Regional Council members and working groups and revised based on changing conditions.

In addition to reviewing and updating strategic plans, the Regional Councils should also be tasked with developing strategies for achieving the integration described above with workforce, economic development, and higher educational institutions, the key economic development service providers.

**Consolidated Funding Applications (CFAs):** The purpose of the CFA is to have one standard application for all state-level economic development programs. While simple in concept, the process of reaching agreement from all agencies on intake information was exceedingly challenging for the Administration. The CFA process represents a necessary breaking down of walls among state agencies, but also the implementation of a process that can be improved.

The Administration Team which administers the Regional Council program understands the CFA process had glitches and can be improved; they have reached out to NYSEDC and others for input, which has been provided; and, I am confident they will make changes. They have been quite responsive.

NYSEDC's primary concern with the CFA process is that it created another layer in the project approval process. Instead of agencies acting on funding requests as they come in, CFAs were put into an end-of-year funding round, and applications were reviewed by the Regional Council and ESD, as well as each agency.

Economic development is a twelve month activity. To be competitive with other states in the delivery of its economic development programs, New York State must be able to respond to businesses interested in investing in our communities in a time frame that meets their decision-making requirements. We must act at the speed of business, not at the speed of government. This cannot be accomplished if funding decisions are deferred to annual or even quarterly CFA funding rounds.

For these reasons, NYSEDC also recommends that ESD regional offices be authorized to determine whether or not projects meet the parameters of the regional council's strategic plan. If projects do meet those targets, ESD should be given authority to fast track them through the process of gaining permits or funding approvals from other agencies and authorities. This would give added significance to the strategic plans, while at the same time expedite project approvals that are consistent with the plans.

There are also technical problems related to completing and reviewing the CFA by applicants, as well as customer service related issues. NYSEDC is happy to provide more information on these matters upon request.

**Economic development tools**

**Excelsior Jobs Program**. Since the repeal of the Empire Zones Program, New York has been without an effective project attraction incentive program. Tax credits under the Excelsior Jobs Program, the presumptive replacement for the Empire Zones Program, are capped at $50 million annually. This $50 million hard cap has been eroded because significant portions have been committed to the Regional Councils and the Buffalo high tech cluster initiative, leaving less than $40 million annually in economic development incentives available to attract investment and jobs throughout the state. This is a relatively small amount for a flagship economic development program in a state with an economy the size of New York's.

When the global economy improves, companies will begin to invest in new facilities. New York has many strengths and assets with which to compete for these projects. However, without the ability to reduce New York's high operating costs through economic development incentives, New York will sit on the sidelines as other states and countries reap the benefits of those large investments.

That is why NYSEDC urges the state to increase the Excelsior Job's program's annual funding cap by $50 million. Additional hard cap funding should come from other, less productive economic development programs, such as the Film Production Tax Credit program.

**Selling unused tax credits for high tech start-ups**. NYSEDC supports establishing a program to allow technology start-ups to sell Net Operating Losses (NOLs) and unused tax credits. This program, similar to one in New Jersey, would provide needed cash to start-up technology businesses, while providing a meaningful tax reduction benefit to businesses that purchase the NOLs.

Often, in the start-up stages of a business, little or no net income is generated, yet the business qualifies for significant tax credits that they cannot use. Allowing them sell these credits would provide another source of needed cash flow to these important high tech business start-ups.

NYSEDC would also recommend that the NOLs and tax credits be allowed to be traded in the private sector marketplace. In New Jersey, NOLs and tax credits are sold at market rates, which typically fall below the required 90 percent of full market value the business would be eligible to receive. Private firms serve as brokers between the selling and purchasing entities. The system is efficient, and would save the state money because NOLs typically sell for between 80 and 87 percent of market value. The floor should be set at 75 percent of full value, which is the same as New Jersey. Such a process should be authorized in New York State.

NYSEDC would recommend that a three year pilot program capped at $10 million be adopted.

**Tax Increment Financing (TIF).** By far, the most widely used economic development program in the country is Tax Increment Financing. That is why the New York State Economic Development Council supports legislation to allow municipalities to apply the school portion of real property taxes - with school district approval - to pay for debt service on tax increment financing bonds issued to redevelop blighted areas. The major obstacle with New York's TIF statute is that it does not require school district property taxes to be included in the tax increment calculation. Since school district taxes are usually the largest portion of the total local property tax, the absence of that portion significantly reduces the amount of TIF debt which can be leveraged.

New York has allowed tax increment financing since 1984, when voters approved a constitutional amendment. However, the legislature and Governor prohibited the use of school real property taxes in the enacting statute, thereby rendering the program not viable for development purposes. This legislation would address this short coming in the program and give New York's municipalities an important tool for redeveloping blighted areas.

Tax Increment Financing can be used to:

1. Aid municipalities in combating or preventing blight by enabling a municipality to incur or reimburse a developer for many of the redevelopment project costs that would normally fall upon the developer.

2. Aid developers in constructing projects by shifting the burden of all or part of certain construction costs onto a municipality.

3. Aid the general public by redeveloping depressed areas, thereby improving the community and its economy without the necessity of raising property taxes.

This legislation remedies a major defect in New York's TIF program, and would provide municipalities with a major new tool with which to redevelop blighted areas. NYSEDC supports this legislation and urges its adoption.

**"Economic gardening."** Economic gardening" was first introduced as an economic development strategy in 1989 in the city of Littleton, Colo., a community that in the ensuing 15 years saw a 136 percent increase in new jobs. This model has emerged as a prototype for a rapidly expanding movement to generate truly sustainable economic growth for communities, regions and states.

Economic gardening is an innovative entrepreneur-centered economic growth strategy that offers balance to the traditional economic practice of business recruitment, often referred to as "economic hunting." While it was first introduced as a demonstration program in Littleton, Colorado to deal with the sudden loss of the largest employer in the city at that time, it has emerged as a prototype for a rapidly expanding movement of like-minded economic developers looking for additional methods to generate truly sustainable economic growth for their communities, regions or states.

The four basic elements of "economic gardening" are:

1. This economic development model recognizes that most of a region's economic growth will come from existing businesses and start-ups. An estimated 80 percent of new jobs will come from these sources.
2. Economic gardening provides critical information and services needed by businesses to survive and thrive. (The foundation of a BR&E program). This "internal harvesting" model reflects private industry "best practices," where smart businesses routinely use sophisticated "customer databases."
3. This model cultivates an infrastructure that goes beyond basic physical infrastructure and includes quality of life, a culture that embraces growth and change, and access to intellectual resources, including qualified and talented employees. "Economic gardening" focuses primarily on stage two companies (10 – 99 employees) because these businesses statistically have the greatest potential for rapid growth.
4. Economic gardening develops connections through sophisticated customer relations management software between businesses and the people and organizations that can help take them to the next level — business associations, universities, roundtable groups, service providers and more. Services provided to these businesses are similar to those provided by sophisticated business consultants, and relate far more often to workforce, market expansion, strategic planning, and use of information technology than access to capital and providing incentives.

The Edward Lowe Foundation is the leading think tank advocating and teaching the principles of "economic gardening." States such as Michigan, Colorado, and Florida are making "economic gardening" a major part of their economic development efforts.

The Finger Lakes Regional Council included as a priority project in its strategic plan the establishment of an economic gardening program. While the funding requested by the Regional Council was $500,000, only $200,000 was awarded. NYSEDC strongly urges the legislature to fully fund this important initiative, which could serve as a pilot program for the rest of the state.

**"Open for Business" campaign.** NYSEDC is pleased that Governor Cuomo has proposed creating a campaign to promote New York's economic strengths. The program, The "Open for Business" campaign, is long overdue and should have the following characteristics:

1. Funding should be significant and there should be a commitment to a multi-year program.

2. The program should focus much more on business marketing than advertising.
3. The program should leverage the business marketing investments being made by the regional economic development organizations, such as BNE, GRE, CEG, and HVEDC.

Most business marketing activities over the past decade have been funded and conducted by regional EDOs. These initiatives have largely been funded by the private sector with some state and local government support. Over the past decade, for example, BNE, CEG, and HVEDC have cumulatively invested more than $35 million in external business marketing. Results from these marketing efforts have been significant, especially given the business environment in which they were conducted.

New York State now invests more than $7 million annually to attract tourists to the state and its communities. However, it invests little to market its high tech advantages, which are considerable. Consequently, the quality and breadth of New York's high tech assets are a relatively well-kept secret.

This fact was demonstrated in a competitiveness study that NYSEDC published five years ago, which concluded that NY's high tech advantages outside of New York City are underappreciated.

For these reasons, NYSEDC recommends that a meaningful portion of funding for the "Open for Business" campaign be directed to leverage the business marketing investments currently being made by the large regional economic development organizations in the state.

While we understand the value of advertising, we also know that the best outcomes will result from a long term commitment to business marketing that leverages the work of regional EDOs. Market research; market segmentation; trade show participation; development of marketing collateral material; familiarization tours; media relations; targeted industry trade missions are the core functions of business marketing in which the state should be engaged if it is to have a serious presence in the global marketplace.

Thank you for the opportunity to testify this morning. I look forward to your questions.