Accounting

The Government Accounting Standards Board establishes accounting rules used by state and local governments. In this article, Greg LeRoy of Good Jobs First discusses the Board’s new accounting rule on tax abatement disclosures.

2017: A Landmark Year for Transparency on State and Local “Corporate Welfare”

BY GREG LEROY

In a landmark breakthrough in public finance, a new government accounting rule will soon start generating massive amounts of new data on “corporate welfare,” or tax breaks granted by localities and states in the name of economic development.

Thanks to Governmental Accounting Standards Board (GASB) Statement No. 77 on Tax Abatement Disclosures, costly giveaways like property tax abatements, income tax credits and sales tax exemptions for jobs and other community benefits will now show up in government spending reports.

In the history of government transparency, this is historic news: GASB has never before required any reporting of any kind of tax expenditures. That is, other kinds of state and local tax breaks, corporate or personal—such as itemized deductions or sales tax exemptions on groceries—are still not covered by any GASB Statements. That’s why state tax expenditure budgets are not uniform or comparable.

For many critics, from both the left and right, the economic development spending data is long overdue. They hope it will help balance a debate that has historically been dominated by politicians touting the benefits of job-creation subsidies while obfuscating their costs. Indeed, costs play out over decades and are usually buried in different state, county and city agencies, making it hard to see the big picture.

Taxpayers in Canton, Mississippi, for example, were surprised to learn that the Nissan assembly plant they thought cost $295 million in subsidies actually cost $1.3 billion. The smaller figure they remembered from a long-ago special vote by the state Legislature. But $1 billion more was evident in local records, where long-term property tax abatements were affecting schools, and in an obscure state program in which Nissan workers were effectively paying taxes to the company via a diversion of their withholding taxes.

The New Data Will Be Voluminous Yet Crude

Statement No. 77 took effect starting in calendar 2016, so as governments close their books on either calendar 2016 or fiscal 2017, they will issue their first Statement No. 77 records within the Notes section of their Comprehensive Annual Financial Reports (CAFRs).

Given how many jurisdictions adhere to GASB’s Generally Accepted Accounting Principles (GAAP), the data will be voluminous and far-flung: more than 50,000

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localities and state bodies are expected to comply. (Though GASB itself has no legal authority, most states require some school districts, counties and/or cities to obey GAAP. Many more do so to obtain optimal credit ratings.)

The data will also reveal enormous spending that has heretofore been invisible. A diligent academic study estimated total state and local spending at $70 billion per year, prior to the Great Recession. Interstate competition for jobs has only intensified since, in the protracted recovery, so even more spending may come to light.

Yet the data will also be crude: jurisdictions will only have to report how much revenue they lost to each economic development tax abatement program. Governments may voluntarily elect to disclose some large-recipient company names, but few likely will. (For company-specific incentive data, see Good Jobs First’s Subsidy Tracker database.)

There will also be ancillary information: the Notes passages must also explain where the program is legally enabled, which tax it reduces, how companies qualify, and whether there is a “clawback” safeguard to protect taxpayers with a refund if a company fails to deliver (but nothing about whether any clawbacks have been imposed).

Finally, if a government makes a large infrastructure commitment associated with a tax-abated project, it must also disclose that additional cost. For example, if a city agreed to build a new freeway off-ramp and water and sewerage lines for an abated industrial park, it would have to report those expenses.

Data Wrangling: The Wild West

Given how diffuse the CAFRs will be, and how varied state practices are in collecting and processing CAFRs, the new abatement data will hard to wrangle.

When local and state governments issue the data in the Notes section of their CAFRs, the numbers will be in PDF text, not a balance sheet or spreadsheet. What happens next will vary greatly by state. In most, local governments send their CAFRs to a state auditor, comptroller or treasurer. In some, school boards send their CAFR (or a less-detailed AFR) to a state education department.

Then state practices vary again. Some states collate the CAFRs and post them online, but most do not. Some states, including New York, pay close attention to CAFRs, but most do not. The Empire State rates localities for fiscal stress, watching for possible municipal bankruptcies.

So getting Statement No. 77 data into spreadsheet form to be analyzed is going to be tedious in most states. But two years from now, Good Jobs First predicts there will be a new cottage industry—composed of activists, academics and journalists—issuing powerful analyses with it. Especially those who care about equity will be able to explore: Do “the poor pay more,” as the economic development axiom goes?

Intergovernmental Accounting: Schools as Likely Beneficiaries

One of Statement No. 77’s most laudable aspects is its requirement for intergovernmental accounting of passive harms. That is, if a public body loses revenue passively, as the result of another (actively abating) government’s actions, it must compute that loss and report it.

For example, the New Mexico State Auditor’s office has described a hypothetical $1,000 abatement by Bernalillo County. The resulting losses would be suffered—and reportable—by the City of Albuquerque ($280), Albuquerque Public Schools ($250), the County ($210), the University of New Mexico Hospital ($150), Central New Mexico Community College ($80), and the State ($30).

This provision is especially relevant to school districts, which are usually helpless to stop cities and counties giving away tax breaks that typically harm education the most (even more so than the New Mexico example). Especially because local property taxes are still the largest single source of revenue for K-12, when municipalities grant abatements, create enterprise zones, or designate tax increment financing (TIF) districts, public education is the biggest loser.

Hence the new GASB Statement No. 77 data is likely to spark interest among those who have advocated for equity and adequacy in education funding. It may also strengthen the hand of those who argue that investments in public education should be shielded altogether from abatements because they are proven winners for long-term job and income growth.

Data in Fire-Hose Proportions by Late 2017

The data will start trickling this April, flow strongly by June, and reach fire-hose proportions by November and December of 2017, as governments, many closing their fiscal years on June 30, report several months later.

In the spring, cities such as Columbus, Denver and Fairbanks will report. June begins the flood, with Anchorage, Augusta, Charleston (S.C.), Fargo, Indianapolis, Little Rock, Minneapolis, New Orleans, Omaha, Pittsburgh School District, St. Louis County, Seattle, Sioux Falls, and Wichita disclosing—along with hundreds of smaller places.

By late fall, thousands of jurisdictions per week will be reporting these long-hidden costs, and the U.S. will enter 2018 finally ready to attach a national price tag to these controversial tax breaks.

Long-Term Effects of Tax Abatement Accounting

Explaining Statement No. 77 to diverse audiences since 2015 has provoked a wide range of responses that suggests the new data will stimulate healthy new debates.

Most immediately, the crude quality of the abatement data may prompt cries for better disclosure: for the number of abatement deals behind the dollars (a detail GASB inexplicably dropped late in its deliberations on Statement No. 77); for company-specific cost figures; for future-year program liabilities; and for clearer reporting of tax increment financing (GASB’s guidance on TIF reporting amounts to a split decision, even though TIF is the dominant form of tax spending for economic development in some states).
The arrival of tax abatement data may also underscore the need for accounting standards for other kinds of costly tax expenditures that are not tied to economic development (i.e., for truly comparable tax expenditure budgets).

Statement No. 77’s intergovernmental reporting requirement could have a positive effect in raising public literacy in how “the leg bone is connected to the hip bone” in public finance. With expected federal cuts in aid to education, housing, health care—and yes, even economic development—it is likely that groups seeking to defend public services will use the new data to raise the opportunity costs of tax abatements.

Over time, as the use and analysis of the data evolves, ratings agencies may embrace it as a credit risk variable. States may adopt it as a fiscal stress indicator. More governments may see additional value in adhering to GAAP. At the very least, there will be a more informed public debate about both the benefits and the costs of “corporate welfare.”

It’s about time.