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RESEARCH REPORT

VIRGINIA'S ECONOMIC INCENTIVES:

Missed Opportunities for Sustainable Growth

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Virginia's Economic Incentives: Missed Opportunities for Sustainable Growth

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I. INTRODUCTION

This report examines several major economic incentive programs and funds used in the Commonwealth of Virginia to attract new businesses and to support the expansion of existing businesses. Virginia operates a number of programs that provide loans and grants to businesses for economic development and job creation purposes. The programs reviewed in this report provide nearly $30 million per year in government support to businesses.

Although the use of economic incentive programs has increased over the last decade in Virginia and in other states, surprisingly little attention has been paid to the effect of such programs on land use. For example, the effect of economic development subsidies on urban sprawl has only occasionally been addressed in the academic literature or by the media.[1]

This report describes Virginia's current business incentive programs and analyzes whether land use patterns and long-term development effects are considered when providing grant and loan awards. Specifically, it explores the possible link between the provision of government support to businesses and the consideration of the effects of these subsidies and investments on land use, urban and exurban development, and sustainability of the economic and social investment.[2]

The report finds that Virginia does not consider the impact of its economic incentive programs on land use patterns and sustainability. Furthermore, the information publicly available on these programs does not contain sufficient detail on the use of the funds to assess their effect on growth and land use patterns. Although this report does not attempt to evaluate the impact of these programs on growth patterns to date, including their contribution to sprawl in some parts of Virginia, it does identify the additional information that is needed to make such determinations.

Attention to land use and sustainability effects is critical for assuring that the Commonwealth of Virginia carries out its role under Article XI of the Constitution of Virginia to balance development and conservation of the environment, as well as to assure that State finances are expended in ways that protect Virginia's comparative advantages in a "new economy" environment. Thomas Jefferson counseled that economic prosperity lay on a "due balance between agriculture, manufacture, and commerce" while also warning that each generation should not through its choices encumber the earth to the detriment of future generations.[3] Similarly, wise

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[1] Sprawl can be defined as low density residential development outside of existing towns, cities, and commercial centers, typically in the countryside where little supporting public infrastructure exists. Environmental Law Institute, *Guiding Growth in Virginia*, Nov. 1998, 11.

[2] In broad terms "sustainability" is the ability to ensure that the future growth of the Commonwealth "meets the needs of the present generation without compromising the ability of future generations to meet their own needs." Typically it includes three elements: economy, community, and environment. Environmental Law Institute, *Blueprint for Sustainable Development of Virginia*, 1994, 1, 2.

[3] Letters: Thomas Jefferson to James Madison, December 20, 1787, Thomas Jefferson to Thomas Leiper, January 21, 1809.

stewardship of the Commonwealth's resources should include attention to the land use and sustainability effects of subsidies.

Encouraging sustainable growth can also be a positive step in retaining and attracting businesses. Quality of life is becoming an important factor in site location. Businesses understand that sustainable growth can help them maintain the long-term competitiveness and prosperity of their businesses and the communities in which they are located. For example, many corporations recognize that traffic congestion is a serious impediment to business. Accordingly, sustainable growth can complement and even foster the economic growth goals.

The report recommends that Virginia consider land use impacts in administering current economic incentive programs by funding growth in locations that are designed to maximize benefits to the surrounding communities. Virginia officials have a variety of options available to them for taking land use impacts into account in allocating funds. Possible approaches include giving preference to proposals that take sustainable land use and development into account, requiring sustainable land use as an element of these programs, disclosing impacts and potential impacts and advantages, and determining the amount of funding based in part on sustainable development criteria.

Furthermore, Virginia could make a substantial contribution to its competitiveness and to the corporate perception of Virginia as a cutting-edge "new economy" state by using a public process to identify key factors for the management of impacts on land use. The public, the business community, and local government officials should be given an opportunity to help select the factors that, in addition to statewide economic development and job growth, are considered in making Virginia's economic incentive programs the best in the nation. The factors could then be adopted as part of incentive program guidelines or help inform legislative changes to the programs.

Lastly, this report recommends that Virginia establish new programs that are specifically aimed at fostering sustainable economic development. Such programs could provide incentives to companies to locate in Virginia, and for Virginia businesses to expand, in a manner that is consistent with principles of sustainable development.

The Commonwealth is missing a significant opportunity to take into account sustainable growth patterns in its current incentive programs. Some or all of the funds awarded through these programs could help assure that these investments are also contributing to the sustainability of the Commonwealth's communities and its environment.

II. ECONOMIC INCENTIVES AND GROWTH CHALLENGES

A. Virginia and the Use of Economic Incentive Funds

States across the country use economic development funds to attract and maintain businesses. Incentive programs vary from state-to-state, but over the last decade many states have adopted such programs in an effort to compete with other states for the jobs and revenue that businesses provide. Incentive programs typically are designed to reduce specific business costs, such as taxes, cost of capital, land, facility financing, training, and upfront operating costs. These subsidies are provided to businesses in a variety of ways, depending on the program, and may include direct cash payments, assistance with relocation or expansion costs, income tax credits, or credits to the firm's payroll tax. The amount of funds dedicated to economic incentive programs varies by state. A recent report estimated that in the aggregate, state governments spent approximately $10-$11 billion in 1997 on economic incentive efforts.[4]

The Virginia General Assembly has established many economic development incentive programs over the last twenty years. This report only focuses on those programs that provide loans and grants to businesses, although there are several other types, including corporate income tax incentives, industrial development bonds, community development block grants, infrastructure programs, and enterprise zone designations. In total, the Virginia economic incentive programs examined in this report provided nearly $30 million to businesses in 1999.

Virginia's early grant and loan incentive programs focused on small businesses and economically depressed areas. For example, the Virginia Small Business Financing Authority, which oversees several loan reserve programs for small businesses, was established in 1984. Similarly, the Virginia Coalfield Economic Development Authority, which encourages development in the coalfields region, was established in 1988.

A new type of subsidy program was initiated in the 1990s with the establishment of the Economic Development Contingency Fund and the Governor's Development Closing Fund. These Funds were then combined in 1996 to create the Governor's Development Opportunity Fund, a deal-closing fund used to attract new businesses. In 1999, the Virginia Investment Partnership Grant Fund, which provides incentives for existing businesses, was created. In 2000, the General Assembly created a new fund, the Governor's Economic Development Grant Fund, to provide funds to localities to address infrastructure stress resulting from State-sponsored economic development projects.

Thus, in Virginia, economic incentive funds have been increasingly used to attract and maintain businesses. The programs appear to be viewed by many in Virginia's government and business sectors as a crucial tool for maintaining economic competitiveness with other states. This view achieved considerable traction when in 1993 the Virginia Chamber of Commerce

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[4] National Association of State Development Agencies, *Evaluating Business Development Incentives*, August 1999, 17.

requested that the National Association of State Development Agencies (NASDA) assess Virginia's competitiveness for economic growth. The NASDA report provided the groundwork for the support and establishment of Virginia's current economic development programs. The numerous respondents interviewed identified a need to address development incentives for business expansion, retention, and attraction in a comprehensive and studied fashion and also expressed a growing sentiment that a more activist economic development program was needed.[5] Those interviewed stated that they preferred "a more aggressive Virginia competing for the investments being made by firms outside the state and for the expansion of industries within the state."[6] The report recognized that the other minimalist states were abandoning the old ways for more aggressive incentive programs and that Virginia was competing not only with southeastern but with mid-Atlantic and northeastern states that "boast a wide array of well funded incentive programs."[7] The report found that these types of programs needed to be developed in order for Virginia to stay competitive,[8] and indeed they were in the next several years.

While the use of economic incentive programs has increased over the last decade in Virginia and in other states across the country, surprisingly little attention has been paid to the effect of such programs on land use, including sprawl. In fact, the role of economic development subsidies in fostering urban sprawl has only rarely been addressed in the academic literature or by the media.[9]

B. Virginia's Growth Challenges

Virginia, like many states across the country and in the Southeast, is currently facing the challenges that increased growth presents for maintaining quality of life and for sustaining local and regional economies. Some parts of Virginia have already begun to experience the adverse effects of development patterns that produce transportation gridlock, delay, loss of open space, and weakening of older urban centers. These concerns are significant as firms become increasingly mobile and seek to offer high quality of life to their managers and employees. Virginia's substantial land base, transportation network, and scenic beauty has given the Commonwealth an advantage in the 1990s over some of its other state competitors, but this advantage is not assured long term without more concern to the location of growth and investment.

In general, the Southeast is experiencing an explosive population growth and economic development boom. While the nation as a whole lost 6% of its farmland between 1982 and 1997, the Southeast lost 14% – more than ten million acres.[10] Virginia is experiencing sprawl

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[5] National Association of State Development Agencies, *Virginia Economic Development Competitiveness Study*, 1993, 10.
[6] *Id.* at 11.
[7] *Id.* at 26.
[8] *Id.* at 24.
[9] For an example of a report that does address this issue, *see* Good Jobs First, *Another Way Sprawl Happens*, January 2000. Good Jobs First, a project of the Institute on Taxation and Economic Policy, has studied the effect of tax increment financing on urban sprawl and its relationship to the quality of jobs created.
[10] Environmental Law Institute and Southern Environmental Law Center (ELI/SELC), *Smart Growth in the Southeast*, 1999, 4.

development in many of its high growth localities – the Piedmont, Northern Virginia, localities along I-95 from Washington, D.C. to the Richmond metropolitan area and along I-64 from the Hampton Roads metropolitan area to Charlottesville.[11] Virginia's population has increased by 900,000 in just the last ten years according to newly released census figures – an astounding 14% increase in population.[12]

In many communities in Virginia, past and current patterns of growth have led to sprawling residential developments, which produce tangible and intangible costs. The most obvious costs are the costs to local governments and to taxpayers to supply public facilities, such as sewers, schools, and new roads.[13] Less direct costs include a lower quality of life, economic decline in city centers, damage to the rural economy, and environmental harm.[14] For example, residents may spend more time in congested traffic, experience an increasing number of "ozone alert" days, and see their property taxes rise.[15] Furthermore, older towns and cities may find it difficult to compete with nearby areas for new construction, and farmland and forest land may be converted to low density residential developments.[16] Sprawl can also lead to increased water and air pollution and threats to wildlife habitat.[17]

Opinion polls in Virginia have consistently shown deep concern about the consequences of current growth patterns, and strong support for preserving open space and farmland and revitalizing existing communities.[18] In a recent poll, 70% of the respondents believed that traffic problems caused by rapid development should be alleviated by managing new growth so that existing roads and mass transit could accommodate transportation needs.[19] Likewise, a majority of respondents believed that the loss of open space was a problem the Commonwealth should try to prevent and was not the inevitable result of market forces.[20]

Perhaps most important is the fact that encouraging sustainable growth can also be a positive step in retaining and attracting businesses. Quality of life is becoming an important factor in site location. Businesses increasingly understand that sustainable growth can help them maintain the long-term competitiveness and prosperity of their businesses and the communities in which they are located.[21] For example, many corporations recognize that traffic congestion is a serious impediment to business. Accordingly, sustainable growth can complement and even promote economic growth goals.

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[11] ELI, *Guiding Growth in Virginia*, 11.
[12] U.S. Census Bureau (last modified Dec. 28, 2000) <http://www.census.gov/population/cen2000/tab04.pdf>.
[13] ELI, *Guiding Growth in Virginia*, 12.
[14] *Id.*
[15] *Id.*
[16] *Id.*
[17] *Id.* at 11.
[18] ELI/SELC, *Smart Growth in the Southeast*, 7.
[19] *Id.*
[20] *Id.*
[21] Urban Land Institute, *Smart Growth Myth and Fact*, 1999.

Over the last several years, community groups, members of the General Assembly, and other public and private sector stakeholders have attempted with varying degrees of success to address Virginia's growth challenges. For example, in the 2000 General Assembly session, several bills were aimed at addressing sprawl.[22] In addition, both the House and the Senate presented resolutions calling on the Joint Subcommittee Studying the Future of Virginia's Environment to recommend legislation to ensure that state spending on economic development, infrastructure, and transportation would discourage sprawl and encourage the redevelopment of central cities and the protection of the Commonwealth's rural landscapes.[23] These resolutions were not adopted and the Commission was instead simply directed to study environmental issues that may require legislative action.[24]

Virginia, like many states, is faced with the challenge of how to grow and foster economic development while simultaneously avoiding unsustainable land use. This report suggests that a key step in facing this challenge is for Virginia *explicitly* to take into account the growth impacts of Virginia's economic incentive programs in allocating grants and loans.

C. Other State Approaches to Economic Incentive Programs

ELI surveyed several other states often regarded as competitors with Virginia, including Maryland, New Jersey, Tennessee, and North Carolina, in order to determine whether their state economic incentive programs take sustainable growth into account as a factor in allocating funds. Several of these states are beginning to – or have already – taken into account the effects of their incentive programs on patterns of growth and land use.

These state approaches are not presented as models for Virginia to follow. Rather, they are outlined to demonstrate that many states, including those with which Virginia competes to attract businesses, are facing similar challenges and are trying to address them. The examples are also included to show the wide range of approaches currently used and to emphasize the flexibility Virginia has in developing its own approaches to integrating land use considerations into its economic development programs.

Maryland's smart growth legislation allows the state to direct its state funding to support locally designated growth areas and to protect rural areas. The centerpiece of the program is the state's 1997 Priority Funding Areas legislation, which limits most state infrastructure funding and economic development program monies to Smart Growth Areas that local governments designate for growth.[25] The Maryland legislation specifically restricts the use of some economic

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[22] House Joint Resolution 189, 2000, which would have established a joint subcommittee to study the connections of access highways and entrance roads to state primary and secondary highways and House Joint Resolution 376, 2000, which would have established a joint subcommittee to study ways of preserving farmland in urban areas.
[23] Offered Senate Joint Resolution 76, 2000 and House Joint Resolution 102, 2000. The resolutions also requested that the Joint Subcommittee make recommendations on whether any of the five components of Maryland's Smart Growth and Neighborhood Conservation Initiatives could be employed effectively in Virginia. The final bill that was adopted omitted any specific mention of Maryland's Smart Growth and Neighborhood Conservation Initiatives.
[24] Adopted Senate Joint Resolution 76, 2000.
[25] Md. Code Ann. § 5-7B-04.

development incentive programs except in priority funding areas.[26] Additionally, some of the regulations implementing Maryland's other economic development incentive programs specifically contain limiting provisions to allow funding only in priority funding areas.[27]

New Jersey has also implemented tools to encourage sustainable growth as part of its economic development incentive programs. Businesses in designated areas are required to create a fewer number of jobs in order to qualify for some programs than if the businesses were to be located elsewhere. For example, under New Jersey's Business Employment Incentive Program (BEIP), businesses creating at least twenty-five new jobs in designated areas may be eligible to receive a BEIP grant; however, businesses locating elsewhere must create seventy-five jobs before they are eligible for BEIP grants.[28] Second, under the New Jersey Local Development Financing Fund Act, a fund to provide financial assistance to local commercial and industrial projects, the "other" criterion for ranking applications for financial assistance includes whether the project is located in an area targeted for economic development, the extent to which the project will contribute to the economic revitalization of a municipality, the degree to which the project will advance state or regional planning, and the extent to which the location of the project is accessible to public transportation.[29] These tools provide a basis for differentiating among projects with different local effects.

Tennessee also attempts to encourage sustainable land use and growth as part of its economic development incentive programs. The Tennessee legislation ties the granting of certain economic development incentives to the approval of local growth plans. The legislation provides an additional five points on a scale of 100 points, or a comparable percentage increase, on evaluation forms for certain grant and loan programs for counties and municipalities that have an approved growth plan by July 1, 2001.[30] The legislation also makes certain economic development incentive grants aimed at local governments unavailable to counties and municipalities that do not have an approved growth plan by July 1, 2001.[31]

North Carolina does not yet have policies in place to encourage sustainable growth as part of its economic development incentive programs. However, the North Carolina Quality Growth Task Force was established to investigate how state government programs and investments influence the quality of growth in North Carolina.[32] The Task Force's 1999 report concluded that the state economic development incentive programs definitely have an impact on sprawl.[33] The report stated that the Industrial Development Fund "could promote sprawl if it provides funding for extension of water, sewer and other infrastructure to unserved areas."[34] To

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[26] Md. Code Ann. § 5-7B-01.
[27] Md. Code Ann. § 7-314(a), Md. Regs. Code tit. 24, § 05.21.04, Md. Regs. Code tit. 24, § 05.22.04, Md. Regs. Code tit. 24, § 05.23.05.
[28] N.J. Stat. § 34:1B-127.
[29] N.J. Stat. § 34:1B-41.
[30] Tenn. Code Ann. § 6-58-109.
[31] Tenn. Code Ann. § 6-58-110.
[32] Quality Growth Task Force, *Inventory of State Government Programs that Influence Growth in North Carolina*, 1999.
[33] *See generally*, Quality Growth Task Force, *Inventory of State Government Programs that Influence Growth in North Carolina*, 1999.
[34] *Id.* at 11.

encourage more compact development and more efficient use of existing infrastructure, the report concluded that "the program could place a priority on funding locations within existing urban areas already served by water and sewer and other infrastructure or areas defined in local land use plans, capital improvement programs or growth management plans."[35] The Task Force was disbanded with the creation of the Joint Legislative Commission on Future Strategies for North Carolina and its conclusions were not pursued.

Virginia varies considerably from the states surveyed in terms of its approach to land use planning and its growth priorities and, therefore, these other state approaches may not provide models for Virginia to follow. However, these examples demonstrate that other states recognize that economic incentive programs are influencing growth patterns. They also suggest that a variety of approaches exist to provide business incentives while fostering sustainable growth.

[35] *Id.*

III. EXISTING VIRGINIA INCENTIVE FUNDS

A. Governor's Development Opportunity Fund (GOF)

The Governor's Development Opportunity Fund, administered by the Virginia Economic Development Partnership (VEDP)[36], is described as a "deal closing fund" to "secure a location or expansion for Virginia in the face of competition from other states or countries."[37] Similarly, the Fund's implementing statute, enacted in 1996 by the Virginia General Assembly, provides that the GOF "is to be used by the Governor to attract economic development prospects and secure the expansion of existing industry in the Commonwealth."[38]

Funds under the GOF are awarded as grants or loans to political subdivisions, which in turn provide funds directly to businesses. The loans are interest free unless otherwise determined by the Governor and must be repaid to the general fund or State treasury. The grants or loans must be approved by the Governor in accordance with procedures established by the VEDP and approved by the Comptroller.[39] Funds may be used for a wide variety of purposes including:

- "public and private utility expansion or capacity development on and off site;
- road, rail, or other transportation access costs beyond the funding capability of existing programs;
- site acquisition;
- grading, drainage, paving, and any other activity required to prepare a site for construction;
- construction or build-out of publicly owned buildings;
- grants or loans to an Industrial Development Authority, Housing and Redevelopment Authority, or other political subdivision pursuant to its duties or powers;
- training; or
- anything else permitted by law."[40]

1. *Criteria for Awarding Grants*

The statute describes the two basic criteria that must be met in order for the Governor to award a grant to a locality.[41] The first criterion is that a minimum private investment of $10 million must be met. A smaller private investment of $5 million is required in localities with a

[36] VEDP, created in 1995 by the Virginia General Assembly, is a state authority governed by a 15-member Board of Directors appointed by the Governor to encourage, stimulate, and support the development and expansion of Virginia's economy.
[37] Virginia Economic Development Partnership, *A Virginia Guide to Business Incentives*, April 2000.
[38] Va. Code § 2.1-51.6:5.
[39] *Id.*
[40] Va. Code § 2.1-51.6:5(C).
[41] Va. Code § 2.1-51.6:5(D).

population between 50,000 and 100,000.[42] A minimum private investment of $2.5 million is required in localities with a population of 50,000 or less.

The second criterion is that a minimum number of jobs must be created. Projects generally must create a minimum of 100 jobs. Only 50 jobs are required in localities with a population between 50,000 and 100,000 and 25 jobs in localities with a population of 50,000 or less. The statute was amended in 1999 to allow a grant award when only half the number of required jobs are created, if the average wage of the new jobs is at least twice the prevailing wage for that locality or region.[43]

According to the guidelines developed for the program by VEDP, grant amounts are determined by considering employment, investment, area unemployment, community fiscal stress,[44] community commitment, and industry or company growth potential.[45] In those cases where the project involves job preservation, "jobs saved" will be used to help determine the amount of the grant; however, the project still must meet the minimum job creation requirements.[46] Additionally, grants will only be awarded for "projects that would bring additional income into the Commonwealth."[47]

The guidelines also impose requirements on the localities receiving the grants. Localities are required, at a minimum, to match the amount requested from the Fund with local funds on a dollar-for dollar basis. Matches may come from local enterprise zone incentives if the locality makes actual expenditures within five years to benefit the specific project. For a locality to receive more than two grants in a fiscal year, it must show that unemployment rates, poverty levels, or other acceptable indicia of fiscal stress or need are significantly higher than the state averages. For a third GOF grant, a locality may demonstrate exceptional need using other acceptable factors besides traditional fiscal stress.[48] In addition, communities are expected to enter into performance agreements with companies upon receipt of a grant to ensure that the job and investment levels agreed to by companies are met, or the communities will be held responsible for returning the grants to the Commonwealth.[49] If funds are made available for site development and a party other than the industry creating the employment also benefits from the grant, the locality must demonstrate how that financial benefit will be passed along to the

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[42] The statute treats central cities and urban cores the same as communities with populations of 50,000 to 100,000 for eligibility purposes. Va. Code § 2.1-51.6:5(D). The intent of this treatment is to reduce the stringency of the requirements for cities with blighted cores. Each locality's identification of its central city/urban core is reviewed on a case-by-case basis. Virginia Economic Development Partnership (VEDP), *Governor's Opportunity Fund Guidelines*, 1999.

[43] Va. Code § 2.1–51.6:5(D).

[44] The fiscal stress index "utilizes three jurisdictional measures denoting (1) the level of revenue capacity per capita during a specified fiscal period, (2) the degree of revenue effort over the same time span, and (3) the magnitude of median adjusted gross income for individuals and married couples in the pertinent calendar year" in order to produce an expression of a locality's fiscal strain relative to other Virginia cities and counties. Commission on Local Government, *Comparative Revenue Capacity, Revenue Effort and Fiscal Stress of Virginia's Counties and Cities*, May 1999.

[45] VEDP, *Governor's Opportunity Fund Guidelines*, 3-4.

[46] *Id.* at 1.

[47] *Id.* at 3.

[48] *Id.*

[49] *Id.* at 4.

industry.[50] Finally, if the funds are requested for a relocation of a business from one Virginia locality to another, the community from which the business is moving must be notified by the community applying for the funds.[51]

The guidelines also specify the application process. In addition to information that determines whether the statutory criteria are met (*e.g.* job creation, use of grant, private investment amounts, and salary levels), the guidelines also request information from applicants about:

- local financial participation and how new monies will be used;
- a summary of the importance of the project to the community and why support from the Fund is sought;
- documentation from companies that without support from the Fund there is a possibility that the project could be located outside of Virginia and that only one site in Virginia is under consideration for the project;
- information relevant to whether state funds would be used to help a company relocate or expand its operations in one or more Virginia communities when the same company is simultaneously closing facilities in other Virginia communities.[52]

2. *Reporting Requirements and Results*

The Governor is required to provide periodic reports to the legislature (*i.e.*, within thirty days of each six month period ending June 30 and December 30). These reports are required to include the name of the company and the type of business in which it engages, the location (city, county or town) of the project, the amount of the grant or loan made from the Fund and the purpose for which it will be used, the number of jobs created or projected to be created, the amount of the company's investment in the project, and the timetable for the completion of the project and jobs created.[53]

The Governor has filed 14 semi-annual or quarterly reports since September 1993 when the fund was known as the Economic Development Contingency Fund and the Governor's Development Closing Fund. Fiscal year 1997 was the first year in which reports were filed under the name Governor's Development Opportunity Fund. The reports provide information on the program in general as well as on individual projects. Overall, the reports contain all of the information required by the statute except for the timetable for the completion of the project and the jobs created. For the projects that have been announced, the reports to the General Assembly also include a profile, an analysis and recommendation by VEDP, and a scoring sheet. The profile, analysis and recommendation, and scoring sheet are all confidential and thus not available to the public. Further information on how the Fund operates is also provided in the Report to

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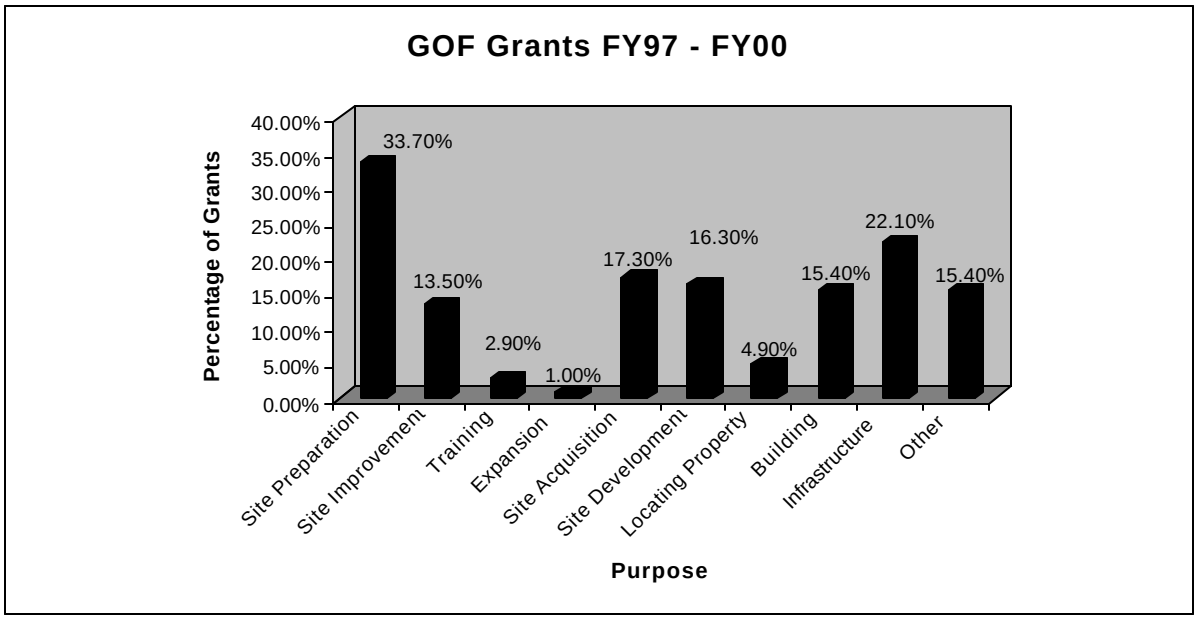
[50] *Id.* at 1.
[51] *Id.* at 2.
[52] *Id.*
[53] Va. Code § 2.1-51.6:5(F).

the Chairmen of the House Committees on Appropriations and Finance and the Senate Finance Committee.[54]

An analysis of the reports from the Governor to the General Assembly suggests that 33.7% of the businesses receiving GOF grants between 1997 and 2000 planned to use some or all of the funds for site preparation. In the same period of time, 22.1% of businesses planned on using GOF money for infrastructure (which includes traffic and road improvement, parking, and utility extension), 17.3% planned on applying GOF funds toward site or land acquisition, 16.3% toward site development, 13.5% toward site improvement, 4.9% toward locating property, 2.9% toward training, and 1.0% toward expansion. In addition, 15.4% of the businesses receiving a GOF grant planned on applying the funds to other activities, such as new equipment, loan financing, and equipment relocation. The letters provide no further explanation of these descriptions nor do they provide specific information such as land acreage or exact location of the project.

In addition to the semi-annual and quarterly reports, the annual reports begun in 1997 provide information on how the Fund has been used. Since 1997, the General Assembly has appropriated approximately $15,000,000 per year to the program. Also since 1997, 88 grants have been awarded from the GOF. In this time period, grants awarded totaled $42,392,000 and were credited with 33,819 new jobs with $2,854,998,000 of related private investment.[55]



[54] In the 1999 Appropriations Act, the General Assembly requested the Secretary of Commerce and Trade to report to the Chairmen of the Senate Finance Committee and House Committees on Appropriations and Finance on the "use and efficacy of state incentives in creating investments and jobs in Virginia." Chapter 935 of the Acts of Assembly, at Item 89 B.

[55] Barry E. DuVal, *Report on Business Incentives: 1997-1999*, Nov. 4, 1999, 8 and Barry E. DuVal, *Report on Business Incentives: 1999-2000*, Nov. 4, 2000, 11.

Year	Total GOF Investment	Number of Grants	Average Grant	Number of Jobs Created	GOF Investment per Job
2000	$12,782,000	30	$426,067	9,632	$1,327
1999	$18,810,000	34	$553,235	15,804	$1,190
1998	$10,800,000	24	$450,000	8,383	$1,288

The 1997-1999 report concludes that the efficacy per dollar of state GOF incentive increased from FY 1998 to FY 1999 and that the performance measure for job creation using the GOF compared "favorably" with the national range of $2,000-$5,000 of state investment per new job created.[56] The report attributes this in part to the "aggressiveness of recruitment and expansion efforts."[57] In FY 2000, the dollar per job ratio increased from $1,190 in FY 1999 to $1,327, nearly $200 more per job compared to the FY 1999 figure.[58]

An attempt to amend the Fund's statute to broaden its traditional economic development focus was initiated in the 2000 General Assembly session through House Bill Number 189. The bill would have allowed the GOF to be used for the funding of natural resource-based development, including the construction of oyster reefs or fish hatcheries, the construction of hiking or biking trails and the promotion of travel or tourism.[59] The bill, sponsored by Delegates Pollard, Bloxom and Morgan and Senators Bolling and Chichester, was tabled in the Conservation and Natural Resources Committee on January 26, 2000.

B. Virginia Investment Partnership (VIP) Grant Fund

The VIP Grant Program, established by the Virginia General Assembly in 1999, provides an investment grant incentive for existing Virginia businesses. The program establishes the Virginia Investment Partnership Grant Fund, comprised of the "Major Eligible Employer Grant Subfund" and the "Investment Performance Grant Subfund."

The Investment Performance Grant Subfund provides grants of up to $25 million to Virginia manufacturers that make a capitalized investment[60] of at least $25 million to increase the productivity of a Virginia manufacturing facility or to utilize a more advanced technology. Such manufacturers are eligible to receive an investment performance grant in five installments beginning in the sixth year after the capital investment is complete.[61] Manufacturers are not eligible if they participate in any other state production grant programs. Although no minium job creation is required for the Investment Performance Grant, manufacturers are not eligible if the

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[56] *Report on Business Incentives: 1997-1999*, 9.
[57] *Id.*
[58] *Report on Business Incentives: 1999-2000*, 11.
[59] House Bill 189, 2000.
[60] The capital investment required under the program is defined as "an investment in real property, personal property or both, at a manufacturing or basic non-manufacturing facility within the Commonwealth that is capitalized by the company and that increases the productivity of the facility, results in the utilization of a more advanced technology than is in use immediately prior to such investment, or both." Va. Code § 2.1-548.43:2.
[61] Va. Code § 2.1-548.43:3(G).

investment results in any net reduction in employment within one year after the capital investment has been completed and verified.[62]

The amount of the Investment Performance Grant is determined by the Secretary of Commerce and Trade pursuant to the recommendation of VEDP and contingent upon the Governor's approval.[63] Guidelines issued by the VEDP set out the application process and how VEDP will use the data required from applicants to determine the net present value to the Commonwealth over a 20 year period of the direct investment.[64] The negotiated amount of the investment grant is based on the calculations of the added revenue, or "relative value", to the Commonwealth.[65] Individual grants to any eligible manufacturer may not exceed $3 million or ten percent of the amount appropriated by the General Assembly in the year that the terms of a grant are determined. Furthermore, the aggregate amount of grants from the Investment Performance Grant Fund in any year may not exceed $6 million.[66]

To qualify for a grant from the Major Eligible Employer Subfund, businesses must make a minimum capital investment[67] of $100 million and create at least 1,000 new full-time jobs.[68] Under an April 2000 amendment to the law, non-manufacturers, in addition to manufacturers, can now qualify for such grants. Major eligible employers are eligible for up to $25 million from the Subfund payable over a period of not less than five years and not more than seven years beginning in the sixth year after an application is approved.[69] The statute also provides for the Commonwealth to enter into memoranda of understanding with major eligible employers that set forth terms and conditions of the payment of grants. The House Appropriations Committee and the Senate Finance Committee must be given the opportunity to review any memorandum of understanding prior to adoption.[70] While both the Major Eligible Employer Subfund and the Investment Performance Grant cap the grants at $25 million, the application process under the Major Eligible Employer Subfund is much simpler and the grant is not based on the "relative value" to the Commonwealth.

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[62] Va. Code § 2.1-548.43:2.
[63] Va. Code § 2.1-548.43:3(C).
[64] VEDP, *Virginia Investment Partnership Guidelines*, July 2000.
[65] Va. Code § 2.1-548.43:2. Note, the statute defines "net present value of benefits to Virginia" as the "present value of the amount by which (i)the anticipated additional state tax revenue is expected to accrue to the Commonwealth as a result of the capital investment and jobs created, over a period following the completion of the capital investment not to exceed twenty years, exceeds (ii)the value of all incentives provided by the Commonwealth, including any grants" under the program.
[66] Va. Code § 2.1-548.43:3(E) & (F).
[67] The definition of capital investment is the same as that used in the Investment Performance Grant Subfund. *See* Footnote 60.
[68] Va. Code § 2.1-548.43:4(A).
[69] Va. Code § 2.1-548.43:4(B).
[70] Va. Code § 2.1-548.43:4(D).

In applying for a grant from either subfund, a manufacturer must provide evidence that the requirements of the statute are met, including the amount of capital investment and the number of new jobs created as a result of the capital investment. The statute also requires VEDP to verify that the conditions for approval of a grant have been satisfied.[71]

The statute provides for VEDP to establish guidelines that must be approved by the House Appropriations and Senate Finance Committees, but that are notably exempt from the requirements of the Administrative Process Act, Article 2, section 9-6.14:7.1 et seq.[72] The guidelines were issued on July 18, 2000. While there is no statutory or regulatory restriction on how VIP funds may be used, according to the guidelines, the funds are envisioned to be used to increase production capacity, utilize state-of-the-art technology, and modernize assembly processes.[73] Nothing in the statute prevents their use for land acquisition.

The statute requires reports to the House Appropriations and Senate Finance Committees within thirty days of each calendar quarter. Reports must include the name of the eligible manufacturer, the product it manufactures, the locality of the manufacturing facility, the amount of the grant, the number of new jobs created, the amount of capital investment, and the timetable for completion of the investment and new jobs created.[74]

In March and April 2000, the first four VIP grants were announced. A total of $1,800,000 was awarded to create 524 new jobs and to preserve 400 jobs in four different counties.[75] The exact use of these grants was not disclosed and was simply listed as "expansion."

Year	Total VIP Investment	Number of Grants	Average Grant	Number of Jobs Saved or Created	VIP Investment per Job
2000	$1,800,000	4	$450,000	924	$1,948

C. Virginia Small Business Financing Authority (VSBFA) Economic Development Programs

The VSBFA administers several economic development programs. The VSBFA was established in 1984 under the Virginia Small Business Financing Act.[76] The provisions of the Administrative Process Act do not apply to VSBFA.[77] The purpose of the VSBFA is to provide financial assistance to small businesses through loans, guarantees, insurance and other assistance. Although VSBFA administers numerous small business assistance programs, including an Environmental Compliance Assistance Fund and an Industrial Development Bond

[71] Va. Code § 2.1-548.43:5(A).
[72] Va. Code § 2.1-548.43:3(D).
[73] VEDP, *Virginia Investment Partnership Guidelines*, July 2000, 1.
[74] Va. Code § 2.1-548.43:5(D).
[75] *Report on Business Incentives: 1999-2000*, 11.
[76] *See* Va. Code §§ 9-197 - 9-235.
[77] Va. Code § 9-208.

Program, this report only focuses on the grant and loan programs it administers for purposes of supporting Virginia businesses and attracting new businesses.

Virginia Capital Access Program (VCAP).[78] VCAP provides access to capital for Virginia businesses by encouraging banks to make loans that they would not otherwise make due to a borrower's profile. The program establishes a loan loss reserve at each participating bank, which is funded by enrollment premiums paid by the borrower and VSBFA. To take part in the program, a business must file a loan application with a bank participating in the program. If the financing request does not meet the bank's normal underwriting guidelines, the bank will determine if the proposed loan transaction would be acceptable if the loan were enrolled in VCAP.[79] If the bank approves financing for enrollment in VCAP, the bank then determines the premium amount to be paid by the borrower based on the bank's perceived level of risk. Premiums usually range between three and seven percent of the loan amount and are non-refundable. VSBFA then matches the premium amount and both premiums are contributed to a loan loss reserve fund established for the benefit of the bank.[80] In the 2000 Session, the General Assembly increased the maximum amount of funds that can be used to match any loan from 7 percent to 14 percent of the principal amount of the loan.[81] If the borrower defaults on the loan, the bank can utilize funds in the reserve to offset losses.[82]

Funds borrowed under the program can be used for working capital, expansion, equipment and most business needs.[83] Land acquisition is not prohibited under the program. Both for-profits and non-profits that are authorized to conduct business in Virginia are eligible. Loans are capped at $250,000 per borrower.[84]

According to information provided by VSBFA, in FY 1999, the program helped fund 26 projects with a total of $806,337 and created 82 jobs. The average loan was $31,012. In FY 2000, the program assisted 72 businesses with a total of $3,128,388 and created 79 jobs. The average loan in 2000 was $43,449.[85]

Loan Guaranty Program. The Loan Guaranty Program assists small businesses in obtaining short term financing needed to improve and expand their operations, thereby creating new job opportunities. The Guaranty Program benefits the participating bank by reducing credit and exposure risk. The business benefits by receiving financing it would not otherwise be able to obtain. No specific statutory language exists for the implementation of this program, but rather

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[78] This program is termed the Virginia Small Business Growth Fund in the statute (Va. Code § 9-228.8), but VEDP calls the program VCAP.
[79] Virginia Small Business Financing Authority (VSBFA), *Virginia Capital Access Program*, 2000.
[80] *Id.* at 1.
[81] House Bill 1048, 2000.
[82] VSBFA, *Virginia Capital Access Program*, 1.
[83] *Id.*
[84] *Id.*
[85] VSBFA data were acquired through interviews with staff from the Financial Services Division of the Virginia Department of Business Assistance.

the provisions creating the VSBFA grant VSBFA broad authority to make loans to lenders who make loans to eligible small businesses.[86]

Businesses apply directly to a bank for financing. The bank then determines if a government guarantee is needed. If so, the bank and the applicant fill out applications and provide accompanying materials. Applications are reviewed by VSBFA staff and recommendations are made to the Board of Directors for consideration at their monthly board meetings.[87] Although there is no specific job creation requirement, VSBFA considers the economic impact and job creation from the financing, in addition to assessing the company's ability to repay the loan.[88]

The maximum guarantee under the program is $300,000 or 75 percent of the loan amount, whichever is less.[89] Businesses operating in Virginia that meet at least one of the criteria for a "small business" are eligible. Criteria include: $10 million or less in annual revenues over each of the last three years; a net worth of $2 million or less; or fewer than 250 employees.[90] Fees for this program include an application fee, which varies from $100 to $250 dollars depending on the amount of the loan request, and an annual guarantee fee of 1.5% of the guarantee amount.[91]

Loans can be used for lines of credit to finance inventory and accounts receivable and for short term credit loans to finance permanent working capital or fixed asset purchases, such as office equipment.[92] The acquisition of real property is not prohibited. The program cannot be used to refinance or restructure bank debt, eliminate a bank's requirement for collateral or the principal's personal guaranty, or to compensate for a fundamental business weakness.[93]

According to data provided by VSBFA, in FY 1999, the program provided four businesses with loans averaging $562,500 and helped create 140 jobs. The total loan amount for this time period was $2,250,000. In FY 2000, the program provided 13 loans, totaling $3,755,000 and averaging $288,846, and helped create 110 jobs.[94]

Economic Development Revolving Loan Fund. The Economic Development Revolving Loan Fund is designed to fill the financing gap between private debt financing and private equity.[95] Funds are provided for fixed asset financing to new and expanding industries that are creating new jobs and saving at risk jobs in Virginia.[96] The Economic Revolving Loan Fund is

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[86] Va. Code § 9-217.
[87] VSBFA, *Loan Guaranty Program*, 2000.
[88] *Id.*
[89] *Id.*
[90] *Id.*
[91] *Id.*
[92] *Id.*
[93] *Id.*
[94] *See* Footnote 85.
[95] Va. Code § 59.1-284.2.
[96] VSBFA, *Economic Redevelopment Revolving Loan Fund*, 2000.

regulated and partially funded by the U.S. Commerce Department's Economic Development Administration (EDA).

To qualify for assistance, an applicant must create or save one permanent full-time job within two years of the loan closing for each $10,000 borrowed; provide at least 10 percent of the project costs as cash equity; and provide a first lien on the assets purchased with the loan proceeds.[97] All manufacturing companies or other industries which derive 50 percent or more of their sales outside Virginia are eligible. Local industrial development authorities are also eligible to receive financing to purchase fixed assets to be leased to qualified companies. Companies must meet one of the criteria of a "small business."[98] The maximum loan amount for each project is $1 million dollars. The maximum amount of financing available is the lesser of 40 percent of the total project costs or $10,000 per job to be created or retained.[99] Applications are reviewed by VSBFA staff and recommendations are made to the Board of Directors at the upcoming monthly meeting. Credit decisions are based on the company's credit worthiness, ability to repay the loan, and the collateral offered to secure the loan.[100]

Loan funds can be used for acquiring land and buildings, constructing or improving facilities, and purchasing machinery and equipment. Loans cannot be used for subsidizing a business that is able to obtain financing for the project at reasonable terms from conventional sources, refinancing or restructuring existing bank debt, relocating a business activity from one Virginia jurisdiction to another, compensating for a fundamental business weakness, or for providing working capital.[101]

According to information provided by VSBFA, in FY 1999, the program funded eleven projects with a total of $5,381,200. The average loan was $489,200 and the program created 1,057 jobs. In FY 2000, the program assisted seven businesses with an average loan of $474,971 and a total of $3,324,800 and created 599 jobs.[102]

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[97] However, a subordinate lien position will be accepted if required by the primary lender. *Id.* at 1.

[98] *See* Footnote 90.

[99] VSBFA, *Economic Redevelopment Revolving Loan Fund,* 1.

[100] *Id.*

[101] *Id.*

[102] *See* Footnote 85.

Year	Program	Total VSBFA Investment	Number of Grants	Average Grant	Number of Jobs Created	VSBFA Investment per Job
FY 2000	Economic Development RLF	$3,324,800	7	$474,971	599	$5,551
	Loan Guaranty Program	$3,755,000	13	$288,846	110	$34,136
	VA Capital Access Program	$3,128,388	72	$43,450	79	$39,599
FY 1999	Economic Development RLF	$5,381,200	11	$489,200	1,057	$5,091
	Loan Guaranty Program	$2,250,000	4	$562,500	140	$16,071
	VA Capital Access Program	$806,337	26	$31,013	82	$9,833

D. Governor's Economic Development Grant Fund

The Governor's Economic Development Grant Fund is a new fund created by the 2000 General Assembly to be used by the Governor in making grants to localities in which a State-sponsored economic development project was completed on or after July 1, 1995 and resulted in a demonstrated stress on local infrastructure.[103] State-sponsored economic development projects are manufacturing facilities or other job-creating economic development projects for which the Commonwealth developed and submitted a formal proposal that included an incentive package to a business locating or expanding in an eligible locality.[104] The Fund essentially provides incentives to localities to attract businesses by assisting localities with the costs associated with local infrastructure needs. No grants had been awarded as of December 1, 2000.

The Secretary of Commerce and Trade, contingent upon the Governor's approval, determines the amount of the grants to be distributed to localities. The amount of a grant may not exceed ten percent of the amount appropriated by the General Assembly to the Fund for the fiscal year. Localities may not receive more than $3 million in aggregate grants. The amount of grants in any fiscal year cannot exceed $10 million and the Commonwealth's annual obligation for such grants cannot exceed $1 million annually per locality.[105] Economic Development Grants to eligible localities must be offset by grants or loans awarded from the Governor's Development Opportunity Fund.[106]

Actions of the Secretary relating to the allocation and awarding of grants are exempt from the requirements of the Administrative Process Act, Section 9-6.14:7.1 et seq.[107] The Secretary of Commerce and Trade is required to develop an application process and guidelines

[103] Va. Code § 15.2-946.2.
[104] Va. Code § 15.2-946.1.
[105] Va. Code § 15.2-946.3(B).
[106] Va. Code § 15.2-946.2.
[107] Va. Code § 15.2-946.3(D).

for determining the amount of any grant which an eligible locality may receive. The guidelines are also exempt from the requirements of the Administrative Process Act but must be reviewed before issuance by the Senate Finance and House Appropriations Committees.[108] Initial guidelines were submitted by the Secretary on November 1, 2000, but had not been finalized as of January 2001.

E. The Virginia Coalfield Economic Development Authority (VCEDA)

The purpose of the VCEDA is to enhance the economic base of certain counties and a city in the coalfields region of Virginia. The counties are Buchanan, Dickenson, Lee, Russell, Scott, Tazewell, and Wise counties, and the city is the City of Norton. The VCEDA was established in 1988, based on the finding by the General Assembly that: "[t]he Economy of Southwest Virginia has not kept pace with that of the rest of the Commonwealth" and the economic problems are "due in large part to its present inability to diversify."[109]

The program provides low interest loans and grants to new or expanding private, for-profit businesses and to industrial development authorities. According to the statute, financial support for industrial development authorities and private enterprises may be used for a wide range of activities, including:

- "purchase of real estate;
- grading of sites;
- construction of flood control dams;
- water, sewer, natural gas and electrical line replacement and extensions;
- construction, rehabilitation, or expansion of buildings;
- construction of parking facilities;
- access road construction and street improvements;
- purchase or lease of machinery and tools;
- construction of improvements outside the Commonwealth if in the Breaks Interstate Park; and
- such other improvements as the Authority deems necessary to accomplish its purpose."[110]

However, by policy, the Authority limits the use of funds by private enterprises to only land, building purchase or construction, and equipment, but allows the industrial development authorities to finance the listed range of uses.[111]

New and expanding industries that are basic employers and will bring new income to the seven county, one city service area are eligible for assistance. Priority is given to loans and grants requiring $10,000 or less for each new basic job created and the average minimum hourly wage should equal or exceed one and one-half times the current federal minimum wage at the time the

[108] Va. Code § 15.2-946.4.
[109] Va. Code § 15.2-6001.
[110] Va. Code § 15.2-6011.
[111] Virginia Coalfield Economic Development Authority (VCEDA), *Project Policies*, Amended 5-18-00.

job was created. Projects providing at least 25 jobs within 12 months of initiation are given priority.[112]

Working capital and refinancing loans are ineligible under the VCEDA.[113] Projects that provide "support employment" are also not eligible for funding. Therefore, facilities which primarily serve the local economy, such as retail and wholesale trade, contract construction, insurance, real estate, and medical services businesses are ineligible.[114] Coal mining production projects and projects involving the relocation of jobs from one county to another within the VCEDA's service area are ineligible for support.[115]

VCEDA is funded by 25% of the gross receipts of the Coal and Gas Road Improvement Fund[116] in each participating jurisdiction, half of one percent of gross receipts of the natural gas severance tax levied after June 30, 1990, and state, coal and private sources of funding.[117] In 1997, the VCEDA fund balance was $12,500,000, and the loans and grants given totaled $3,000,000.[118] In 1998, the fund balance was $14,300,00 and the loans and grants given totaled $3,400,000.[119] In 1999, the fund balance was $15,400,00 and the loans and grants given totaled $2,800,000.[120]

The Authority is governed by a Board made up of 16 members who serve four year terms. The Board is required to submit annual reports of the Authority's activities at the close of the calendar year to the General Assembly, the boards of supervisors of the seven coalfield counties, and the Norton City Council. The reports are required to include a complete operating and financial statement.[121]

Year	Total VCEDA Loan Investment	Number of VCEDA Loans	Average Loan	Total VCEDA Grant Investment	Number of VCEDA Grants	Average Grant
1999	$1,448,061	4	$427,148	$294,102	6	$49,017
1998	$3,125,000	6	$520,833	$270,533	6	$45,089
1997	$2,968,403	6	$494,734	$51,859	2	$25,930

[112] *Id.*
[113] *Id.* at 4.
[114] *Id.* at 3-4.
[115] *Id.* at 2.
[116] The Coal and Gas Road Improvement Fund consists of money collected from a license tax on every person engaging in the business of severing coal or gas from the earth. Va. Code § 58.1-3713.
[117] VCEDA, *Virginia Coalfield Economic Development Authority*.
[118] VCEDA, *Annual Report 1997*, 1997, 3.
[119] VCEDA, *Annual Report 1998*, 1998, 3.
[120] VCEDA, *Annual Report 1999*, 1999, 3.
[121] Va. Code § 15.2-6003.

According to a VCEDA analysis of its program from 1988 through 1998, 56.0% of VCEDA's approved funding in the ten year period went to new industry. Existing industry received 12.5%. From 1988 through 1998, 10.9% went to infrastructure, 10.4% went to shell buildings, 9.0% went to assist with property acquisition, and 0.9% was approved for studies. Buchanan County received a majority of the approved funding with 40.5% of the funding between 1988 and 1998.[122]

[122] VCEDA, *Annual Report 1998*, 8.

IV. FINDINGS AND RECOMMENDATIONS

A. Findings

1. *Virginia's Economic Incentive Programs Do Not Consider Sustainable Land Use*

Virginia's economic incentive programs are not required to take into account their effects on patterns of growth. Rather, the programs focus on job creation, capital investment by the grant and loan recipients and, in general, on increased long term revenue for the Commonwealth.[123] While these economic incentive programs promote an important economic development agenda, they also may influence growth patterns in many Virginia communities by subsidizing land acquisition, constructing new infrastructure, and establishing business sites without regard to other Virginia goals including efficient land use, housing, and quality of life.

While giving no attention to land use and other spillover effects of business development and location was typical of economic development strategies used by many states in the 1980s and 1990s, this approach neglects key issues relevant in the 2000s. Business attraction and retention strategies depend more heavily now on quality of life issues than they once did. Furthermore, transportation issues matter over the long term as businesses compete for employees and attempt to grow while maintaining supply chains and customer networks.

States that neglect these issues do so at the risk of diminishing the long term value of their investments. Greenfields sites located outside of towns – relying wholly on automobile transportation with surface parking, and without attention to surrounding land uses – run the risk of lacking sufficient amenities in the long run to retain employees and managers. Furthermore, greenfields locations for businesses may also suffer from transportation problems as adjacent uses proliferate and secondary roads are affected. At the same time, development at such sites may contribute to the lack of vitality of town commercial centers, to the lack of occupancy and investment in local housing stock in those centers by potential employees, and to the decay of local tax bases.

This study does not affirmatively find that Virginia's economic incentive programs are producing harm, or that they are doing more harm than good. Indeed, the data that would be needed for such a detailed assessment are not readily available. But this study does find that

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[123] Only one new program, the Urban Public-Private Partnership Redevelopment Fund, considers land use directly by providing incentives to local governments to remediate sites in urban areas. The program is not included in the programs described in Section III because it does not provide grants and loans to businesses. The Fund makes grants and loans to local governments for assembling, planning, clearing and remediating sites, in order to promote such sites to private developers for redevelopment. The Fund was created to "address the serious problem of a lack of developable land in urban areas of the Commonwealth and the high cost of redeveloping such land." Va. Code § 15.2-2415. The establishment of such a fund was recommended by the Commission on the Condition and Future of Virginia's Cities. The Fund is administered by the Department of Housing and Community Development. Va. Code § 15.2-2415. Grants are limited to $500,000. Each grant is conditioned upon a 100 percent match of funds by the local government. Va. Code § 15.2-2417.

Virginia's extensive and highly influential economic incentive programs are being administered *without regard to* these important development factors – factors that should be on the screen of every public official. The result is missed opportunity.

2. *More Data Are Needed to Administer Economic Incentive Programs for Sustainability*

Virginia's economic incentive programs are required to provide data to the General Assembly about the use of state funds. Most of the required information has been provided on a timely basis. The provided information does not, however, contain enough detail on the use of the funds to assess their effect on growth and land use patterns. In addition, there is no assessment of the data under Virginia's statewide goals to protect the environment as anticipated under Article XI, Section 1 of the Virginia Constitution.[124]

The formats used to present information about the implementation of the economic incentive programs also do not help those wishing to gauge the broader effects of the programs, or to assess local impacts of supported projects. Rather, most information is either limited to press release materials about individual projects, or is presented in aggregated financial reports. For example, it is difficult to obtain information about how grants and loans are used with respect to particular facilities and their infrastructure, and whether their uses are affecting land use patterns in Virginia. It is impossible to determine from the documents available the precise location of many of the grant recipients' facilities (beyond the identity of the county or city where the facility is or will be located), and whether any projected new construction and expansion is taking place near existing infrastructure, town centers, housing, or transportation corridors or on rural roads far from most housing, retail, sewer and water service, and other features.

The necessary data would not be difficult to obtain and compile, were the General Assembly or Governor to request it. Indeed, to the extent that economic incentive programs do not already do so, application and proposal packages could be redesigned specifically to seek this information from applicants and their communities.

Even the detailed information that is currently collected could be organized in a manner that would make it possible to assess the effect of Virginia's economic development programs on land use and sustainable growth. For example, Geographic Information Systems could be used in combination with the site plan information required from applicants to produce alternative projections of growth patterns. The data could be used to identify the location of likely housing increases and to assist in determining necessary ancillary development. This type of compilation would require further work by the Commonwealth's economic development agencies, but chiefly in presenting information already available in a different form.

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[124] "To the end that the people have clean air, pure water, and the use and enjoyment for recreation of adequate public lands, waters, and other natural resources, it shall be the policy of the Commonwealth to conserve, develop, and utilize its natural resources, its public lands, and its historical sites and buildings. Further, it shall be the Commonwealth's policy to protect its atmosphere, lands, and waters from pollution, impairment, or destruction, for the benefit, enjoyment, and general welfare of the people of the Commonwealth." Va. Const. Art. XI, § 1.

B. Recommendations

1. *Consider Growth Impacts in Administering Existing Economic Incentive Programs*

Current economic incentive programs should take into account land use impacts in allocating these important funds. This could be done in several ways: (1) by giving preference to proposals that take sustainable land use and development into account, (2) by requiring sustainable land use as an element of these programs, (3) by disclosing impacts and potential impacts and advantages, or (4) by determining the amount of funding based in part on sustainable development criteria.

Considering such factors as the effect of grants and other subsidies on infrastructure needs, land use, and other growth-related impacts does not mean that the programs' economic development goals need to be compromised. In fact, healthy economic development over the long run could be fostered by more thoughtful allocation of economic incentive funds to produce economic growth in locations that are designed to maximize benefits to the surrounding communities.

In addition, current modes of business location and expansion can cause adverse effects on adjacent jurisdictions even while benefitting the target community. Similarly, a project may be quite beneficial in statewide terms for job creation, but impose local burdens on housing, schools, and local services. Under current grant and loan fund programs there is no requirement that these effects be assessed or provided for, with the exception of the Governor's Economic Development Grant Fund, which provides an after-the-fact remedy for some communities.

Furthermore, taking sustainability into account in allocating economic incentive funds does not mean that these programs would be limited to supporting development only in urban portions of metropolitan areas. Economic incentive programs are important in sustaining Virginia's small towns and rural economies as well. In Southside Virginia and the coalfield counties, for example, economic incentives are crucial to economic growth. But the job growth should also help maintain the local tax base, the existing infrastructure (including schools, fire and police services), and the agricultural and forest base of the area. Supporting business parks on miscellaneous parcels of land is generally far less desirable than restoring employment on local Main Streets and on larger parcels adjacent to towns where the spillover benefits can be maximized. It is possible for Virginia's economic incentive programs to foster business locations and expansions that are within town centers or that are in selected parts of rural areas suitable for sustainable development.

a. Adopt Sustainable Criteria

The following approaches may be used to integrate sustainable land use into the Commonwealth's existing economic incentive programs. They may be used separately or in

combination. Some may require legislation while others may be implemented through executive or administrative changes.

(1) The governor and other program administrators could give a specific *preference* to funding projects that meet certain requirements. If these preferences are articulated, then companies and communities will tailor their future proposals accordingly. In the same way that proposals now must demonstrate job creation or retention benefits, proposals might be required to show positive effects on local community tax bases, use and reuse of existing infrastructure, and avoidance of sprawl effects. This approach would not deny funding to qualified projects that create jobs and meet the other objectives currently specified, but it would clearly establish goals and incentives for projects to do more than just the minimum in order to obtain funding.

(2) A second, more aggressive, approach would be to *require* projects to demonstrate these sustainability benefits as a condition of receiving grant or loan funding – in the same way that a proposal must now demonstrate economic or job growth benefits. Adoption of this proposal would make the fulfillment of sustainability criteria a mandatory, integral part of these economic incentive programs, on the same footing as requirements for job creation or net economic benefit to the Commonwealth.

(3) A third approach, which could possibly be implemented by administrative action, would be to require project applicants to *disclose* the anticipated external costs and benefits of their activity with regard to sustainable development concerns. The applications for assistance would inquire about these factors. While this relatively modest reform would not add new requirements or create a preference for funding one or another proposal based on these factors, nevertheless it would serve as an incentive for project proponents to design their projects in ways that improve sustainability.

(4) Another approach would determine the *amount* of funding based in part on whether factors that would foster sustainable growth are part of the project. Indeed, variations on this approach could allow different grant or loan funding levels based on a point system or sliding scale reflecting the extent to which these other factors were part of the project.

Any of these approaches would help integrate two key Virginia goals: economic development and sustainable land use. Any of them would improve the current Virginia incentive system, which now treats sustainability issues as irrelevant for funding purposes. As discussed earlier, various versions of these approaches are in use in other states, including states that compete with Virginia in attracting businesses. In Maryland, for example, the Priority Funding Areas legislation specifically restricts the use of economic development incentive programs except in priority funding areas.[125] Additionally, some of the regulations implementing Maryland's economic development incentive programs specifically contain limiting provisions to only allow funding in priority funding areas.[126] In New Jersey, businesses are required to create

[125] Md. Code Ann. § 5-7B-04.

[126] Md. Code Ann. § 7-314(a), Md. Regs. Code tit. 24, § 05.21.04, Md. Regs. Code tit. 24, § 05.22.04, Md. Regs. Code tit. 24, § 05.23.05.

fewer jobs in designated development areas in order to qualify for some incentive programs than if the businesses are located elsewhere, thus providing an additional incentive for businesses locating in economic development areas.[127] And in Tennessee, legislation has tied the creation of local growth plans to the granting of certain economic development incentives aimed at local governments. The legislation provides an additional 5 points on a scale of 100 points, or a comparable percentage increase on evaluation forms, for certain grant and loan programs for counties and municipalities that have an approved growth plan in place by July 1, 2001.[128]

b. Use a Public Process to Identify the Factors

The sustainable growth factors to be used in Virginia's incentive programs could be developed through a public process that would obtain input from a variety of stakeholders. To date, there has been minimal public involvement in developing program guidelines. Indeed, several programs' legislative authorities specifically provide that agencies can forego public notice and comment processes on their economic incentive program guidelines and policies.[129]

Virginia could make a substantial contribution to its competitiveness and to corporate perception of Virginia as a cutting-edge "new economy" state by using a public process to identify key factors for the management of impacts on land use. The factors could be adopted as part of incentive program guidelines or to help inform legislative changes to the programs.

New considerations that might be identified through such a public process might include the following:

- whether the project is built around a transportation corridor and contributes to the utility of that corridor, rather than requiring construction of entirely new transportation infrastructure;
- whether the project is an infill development that utilizes current infrastructure;
- whether the project reuses and rehabilitates old buildings;
- whether the project is near to or provides connections to public transportation or alternative modes of transportation, including location near affordable housing;
- whether the project provides for traffic control measures and takes into account traffic patterns in a manner that preserves the community as much as possible, particularly in older towns;
- whether the project involves the cleanup and reuse of a brownfields site;
- whether the project maximizes the retention of open space, agriculture, forest land, and other natural resources and amenities.[130]

Another set of guidelines that could inform a public process for developing sustainable development factors to consider in implementing Virginia's incentive programs are those that are

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[127] N.J. Stat.§ 34:1B-127.
[128] Tenn. Code Ann. § 6-58-109.
[129] Virginia Investment Partnership Grant Fund (Va. Code § 2.1-548.43:3), Governor's Economic Development Grant Fund (Va. Code § 15.2-946.4), and Virginia Small Business Financing Act (Va. Code § 9-208).
[130] *See generally*, ELI/SELC, *Smart Growth in the Southeast* (1999).

endorsed by the National Governors' Association. The governors recommended ten strategies for "better land use." These could be incorporated into existing state incentive programs designed to serve economic development and sustainability goals, and also could be used as a checklist for the General Assembly in adding criteria for new incentive programs. The ten (10) strategies are: (1) mix land uses; (2) take advantage of existing community assets; (3) create a range of housing opportunities and choices; (4) foster "walkable," close-knit neighborhoods; (5) promote distinctive, attractive communities with a strong sense of place, including the rehabilitation and use of historic buildings; (6) preserve open space, farmland, natural beauty, and critical environmental areas; (7) strengthen and encourage growth in existing communities; (8) provide a variety of transportation choices; (9) make development decisions predictable, fair, and cost-effective; and (10) encourage citizen and stakeholder participation in development decisions.[131]

Regardless of whether established factors, such as those identified in the National Governors' Association strategy, are used as a guide or new factors are developed, the public, the business community, and local government officials should be given an opportunity to help select the factors, in addition to statewide economic development and job growth, that are considered in making Virginia's economic incentive programs the best in the nation.

2. *Establish New Economic Incentive Funds Focused on Sustainable Development*

In addition to adding new assessment criteria to current economic incentive programs, new programs could be developed that are specifically aimed at fostering sustainable economic development. Such economic development programs could provide incentives to companies to locate in Virginia, and for Virginia businesses to expand, in a manner that is consistent with principles of sustainable development. Factors for determining sustainability could, as discussed above, be developed through a public process. In the alternative, Virginia could use factors that are generally recognized as indicators of sustainability.

The bipartisan National Governors' Association in 1999 adopted a formal resolution entitled "Principles for Better Land Use."[132] The resolution notes that "Governors nationwide are realizing that, at times, government policies – even well-meaning policies – have stimulated and perpetuated the patterns of growth that many states and local government are now trying to address." The governors' resolution goes on to say:

> Public officials at the state and local levels are becoming increasingly aware of the impact that public expenditures can have on growth and the *need for a more balanced approach to providing financial support for development*. In hindsight, it appears that financial assistance has been provided without adequate consideration of the

[131] National Governors' Association, NGA Policy NR-13 (1999-2001).
[132] *Id.*

long-term effects on farmland, ranches, forests, or other natural resources of economic, recreational, or aesthetic value.[133]

Drawing on these observations, it may be highly desirable to establish any new economic development funds and incentives with express provisions for sustainability in development. This would not require reworking existing funds, but would recognize that when the General Assembly enacts new legislation it should take care to incorporate the land use and development lessons of the preceding decades.

The establishment of new programs that take land use and development patterns into account is not only sound economic policy, but it also comports with Virginia's commitments under the year 2000 Chesapeake Bay Agreement. In that agreement, the Commonwealth recognized that "future development will be sustainable only if we protect our natural and rural resource land, limit impervious surfaces and concentrate new growth in existing population centers or suitable areas served by appropriate infrastructure."[134] Virginia committed to create "tax incentives" to encourage investments "consistent with sound growth management principles," and to promote redevelopment and remove barriers to investment in underutilized urban, suburban and rural communities.[135] Consistent with these approaches, Virginia should also assure that its direct subsidies and business incentive funds support sustainable use of land throughout the Commonwealth.

C. Conclusion

Although additional research is needed to understand how current incentive programs influence land use and how they may be able to take into account sustainable growth patterns, it is clear that a significant opportunity is being missed. In 1999 alone, the programs examined in this report provided nearly $30 million in grants and loans to attract and retain job-creating businesses in Virginia. In the future, some or all of these funds have the potential to contribute further to the sustainability of the Commonwealth's communities and its environment.

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[133] *Id.*
[134] Chesapeake 2000 (June 28, 2000).
[135] *Id.*