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## Lawmakers as Job Buyers

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## LAWMAKERS AS JOB BUYERS

By Edward W. De Barbieri\*

*In 2013, Washington State authorized the largest state tax incentive for private industry in U.S. history. It is not remarkable for a state legislature to use tax benefits to retain a major employer—in this case, the global aerospace manufacturer Boeing. Laws across all states and thousands of cities routinely incentivize companies such as Amazon to relocate or remain in particular areas. Notably, however, Washington did not recover any of the subsidies it authorized despite Boeing’s significant post-incentive workforce reductions.*

*This story leads to several important questions: (1) How effective are state and local legislatures at influencing business-location decisions?; (2) Do such incentive programs actually achieve their goals of increasing and maintaining jobs?; (3) Is the public protected from imprudent spending? This Article looks specifically at the role of state and local governments in encouraging businesses to locate in their jurisdictions. In such cases, state and local lawmakers act as buyers of jobs.*

*This Article argues for a two-step proposal to limit subnational government actions to incentivize business-location decisions. The first step involves a bidding process where companies are awarded incentives based on the lowest subsidy dollar amount required to create or retain a job of a certain quality or pay rate. The second step involves defining job metrics based on certain preconditions and recapturing incentives should a company fail to maintain or achieve a defined number of job and qualities inherent in each job. This two-step proposal has regulatory benefits and it mollifies the political concern for jurisdictions to appear competitive and the need for public financial protection.*

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\* Associate Professor of Law; Albany Law School. For comments and suggestions about earlier drafts, as well as discussions about the ideas that led to this project, thank you to Andy Ayers, Ray Brescia, Matt Bruckner, Sheryll Cashin, Christine Chung, Scott Cummings, Nestor Davidson, Keith Hirokawa, John Lovett, Alicia Ouellette, Eric Posner, Rosemary Queenan, David Reiss, Pat Reyhan, Richard Schragger, Kate Seely-Kirk, Christian Sundquist and the participants of the University of Massachusetts School of Law faculty workshop series, and the Association for Law, Property, and Society Tenth Annual Meeting at Syracuse University College of Law. Thank you to Ben Bucinell, Patrick Cutty, and Anthony Tojek for excellent research assistance, and to the Albany Law School Dean’s Summer Research Grant for financial support.

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## INTRODUCTION

In 2013, the Washington State legislature adopted the largest state tax incentive program for private industry in U.S. history.<sup>1</sup> The governor's office estimated that the almost \$9 billion in tax incentives, in this case for aerospace manufacturers, would yield \$21 billion in economic activity.<sup>2</sup> Only a few years after the incentives were adopted, however, Boeing, the largest aerospace company in the world and the state's largest employer, reduced its workforce in the state by 17,466 workers.<sup>3</sup>

The governor and legislators from both political parties sought to compel Boeing to return a portion of the tax incentives after the company reduced its workforce.<sup>4</sup> Yet, without statutory employment targets, lawmakers were unable to claw back the subsidies.<sup>5</sup> In the end, the legal process to incentivize a company to remain and expand its workforce caused a significant loss in employment to tens of thousands of families.<sup>6</sup> Several years later, it is clear

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1. In this instance, legislators in Washington State acted to keep a new plant set to manufacture Boeing's new aircraft, the 777X, from relocating outside the state. To do that, Washington extended tax incentives, set to expire in 2024, through 2040. Specifically, the legislature added the following text to state tax laws:

It is the legislature's specific public policy objective to maintain and grow Washington's aerospace industry workforce. To help achieve this public policy objective, it is the legislature's intent to conditionally extend aerospace industry tax preferences until July 1, 2040, in recognition of intent by the state's aerospace industry sector to maintain and grow its workforce within the state.

S. 5952, 63d Leg., 3d Spec. Sess. § 1(3) (Wash. 2013) (enacted). This subsidy program tops the list of the largest state and local subsidy programs to private industrial company developments, excluding sports stadiums and other major entertainment projects. PHILIP MATTERA ET AL., GOOD JOBS FIRST, MEGADEALS: THE LARGEST ECONOMIC DEVELOPMENT SUBSIDY PACKAGES EVER AWARDED BY STATE AND LOCAL GOVERNMENTS IN THE UNITED STATES 6 (2013), [www.goodjobsfirst.org/sites/default/files/docs/pdf/megadeals\\_report.pdf](http://www.goodjobsfirst.org/sites/default/files/docs/pdf/megadeals_report.pdf) [<https://perma.cc/E244-9T6R>].

2. The specific tax incentive program was valued at \$8.7 billion and estimated to result in \$21 billion in economic activity over sixteen years. Andrew Garber, *Legislature Approves Tax Breaks to Secure Boeing 777X*, SEATTLE TIMES (Nov. 9, 2013, 7:04 PM), <https://www.seattletimes.com/seattle-news/legislature-approves-tax-breaks-to-secure-boeing-777x/> [<https://perma.cc/9PBK-U2GD>]. The political reality underlying the incentive extension is clear: as one strategist put it, "governors [who] deliver Boeing jobs win reelection. Period." Reid Wilson, *Boeing Machinists Agree to 777X Contract on Narrow Vote*, WASH. POST (Jan. 4, 2014), <https://www.washingtonpost.com/blogs/govbeat/wp/2014/01/04/boeing-machinists-agree-to-777x-contract-on-narrow-vote/> [<https://perma.cc/33UJ-YW36>].

3. Boeing now reports 17,466 fewer workers in Washington State from a high of 83,295 when the tax plan was approved to 65,829 in 2018. See *General Information: Employment Data*, BOEING, <https://www.boeing.com/company/general-info/index.page#/employment-data> [<https://perma.cc/G744-AHW6>] (last visited Aug. 22, 2019); Alwyn Scott, *Washington Lawmakers Nix Bill Linking Tax Breaks to Boeing Jobs*, REUTERS (Feb. 5, 2016, 4:55 PM), <https://reut.rs/2OxdrG1> [<https://perma.cc/C6N4-64WX>].

4. The bill's original text only allowed Washington State to recapture the incentives "[i]f a significant commercial airplane manufacturing program is not sited in the state of Washington . . ." See Wash. S. 5952 § 2(1).

5. Reductions in total workforce or jobs numbers were not considered in the bill language. See *id.*

6. The unfortunate reality is that the Boeing 777X plant was built but the labor will largely be robotic. Dominic Gates, *At Boeing's 777X Wing Factory, Robots Get Big Jobs*, SEATTLE TIMES (Nov. 26, 2016, 6:00 AM), <https://www.seattletimes.com/business/boeing->

that the bill failed as measured against the incentive package's stated intent to "maintain and grow jobs in the aerospace industry in Washington state."<sup>7</sup>

This vignette is but one instance of state lawmakers using tax incentives to attempt to buy jobs.<sup>8</sup> Amazon's public competition to locate its second headquarters and its decision to pull out of a proposed location in New York City<sup>9</sup> are widely reported examples of this frequent phenomenon. Often, efforts to create new jobs result in relocating jobs from a neighboring state or defensive spending to prevent interstate job competition.<sup>10</sup> Current estimates of state and local business incentive spending range up to \$80.4 billion per year.<sup>11</sup> One dataset lists almost 400 commercial and industrial real estate projects that each received over \$50 million in state or local subsidies since approximately 1980.<sup>12</sup> State and local government debt has ballooned alongside this increased spending. Excluding employee retirement funds, state and local government debt has swollen from \$21 billion in 1950 to over \$3 trillion today.<sup>13</sup>

Two common tools used by state and local government to spur economic development activity are job-creation tax credits and property tax abatements.<sup>14</sup> Governments use these tools, along with bond issuances and even local land-use approvals, to induce companies to create jobs and invest

aerospace/at-boeings-777x-wing-factory-robots-get-big-jobs/ [https://perma.cc/WAD8-P6YF].

7. See Wash. S. 5952 pmbl.; see also *General Information: Employment Data*, *supra* note 3; Scott, *supra* note 3.

8. The federal government is largely agnostic about state and local government subsidies to private companies competing with companies from neighboring states. State *ex rel.* Ohio Cty. Comm'n v. Samol, 275 S.E.2d 2, 5 (W. Va. 1980) (Neely, C.J., concurring) (discussing existing federal tax law as "an invitation to states to subsidize their own citizens competing with the citizens of other states"). Commentators have observed that such subsidy programs amount to elected officials buying jobs. Editorial, *Amazon's Golden Fleecing*, WALL ST. J. (Nov. 14, 2018, 6:33 PM), <https://www.wsj.com/articles/amazons-golden-fleecing-1542230916> [https://perma.cc/5YU4-YDUR] ("The worst actors here are the politicians who pose as job creators but are essentially job buyers.").

9. J. David Goodman, *Amazon Pulls Out of Planned New York City Headquarters*, N.Y. TIMES (Feb. 14, 2019), <https://www.nytimes.com/2019/02/14/nyregion/amazon-hq2-queens.html> [https://perma.cc/3ZKE-ZKDY].

10. *Episode 699: Why Did the Job Cross the Road?*, NPR: PLANET MONEY (May 4, 2016, 10:42 PM), <https://www.npr.org/sections/money/2016/05/04/476799218/episode-699-why-did-the-job-cross-the-road> [https://perma.cc/9ZBC-RANY] (investigating the phenomenon of cross border job poaching in Kansas City, Missouri and Kansas City, Kansas).

11. Louise Story et al., *Explore the Data*, N.Y. TIMES (2016), <http://archive.nytimes.com/www.nytimes.com/interactive/2012/12/01/us/government-incentives.html#home> [https://perma.cc/A8ZA-ZQ8R].

12. See generally MATTERA ET AL., *supra* note 1.

13. *State and Local Governments, Excluding Retirement Funds; Debt Securities and Loans; Liability Level*, FRED, <https://fred.stlouisfed.org/series/SLGSDODNS> [https://perma.cc/Z4U6-Y2J6] (last updated June 6, 2019).

14. TIMOTHY J. BARTIK, W. E. UPJOHN INST. FOR EMP'T RESEARCH, A NEW PANEL DATABASE ON BUSINESS INCENTIVES FOR ECONOMIC DEVELOPMENT OFFERED BY STATE AND LOCAL GOVERNMENTS IN THE UNITED STATES 1 (2017).

capital.<sup>15</sup> Job creation and capital investment through building construction and equipment installation grow state and local government tax bases.<sup>16</sup>

The political benefits to providing major employers with financial subsidies are clear.<sup>17</sup> Elected officials act within their authority to halt job losses when faced with a plant closure and the prospect of constituents losing their employment.<sup>18</sup> Similarly, to appear competitive, elected officials enact legislation to lure new jobs by attracting businesses to grow or diversify a state's economy.<sup>19</sup> Both Texas and Florida, for example, authorize their governors to close deals with companies seeking to relocate to another state.<sup>20</sup> Politically, these programs shield legislators when a group of workers faces job cuts or a community lobbies to incentivize an employer to relocate from outside the state.<sup>21</sup>

Economic development activity by state and local government has serious risks. Governments risk bankruptcy should incentives become too costly. In a recent example, incentives to automakers in Michigan brought about a significant state fiscal crisis.<sup>22</sup> In other cases, governments may be financially liable if a development deal falls through. New York State spent massive amounts of public money through its failed Empire Zone Program for projects that were either never built or did little, if anything, to grow the

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15. See *infra* Part I.A.

16. C. Tyler Mulligan, *Economic Development Incentives and North Carolina Local Governments: A Framework for Analysis*, 91 N.C. L. REV. 2021, 2024 (2013) (discussing local government cash grants to private companies to grow tax base).

17. For an excellent discussion about how those companies and individuals with political power benefit their own financial interests, see BRINK LINDSEY & STEVEN M. TELES, *THE CAPTURED ECONOMY: HOW THE POWERFUL ENRICH THEMSELVES, SLOW DOWN GROWTH, AND INCREASE INEQUALITY* 12–13, 28–31, 153 (2017) (“[P]olitical power consists of the ability to win distributional struggles over fixed resources.”).

18. See, e.g., Wilson, *supra* note 2 (regarding Governor Jay Inslee's apparent political calculation to keep Boeing jobs in Washington State as a means of ensuring constituent support).

19. For example, 238 cities pitched proposals to attract Amazon's second headquarters, each with their own local incentives to appear competitive. Amazon News (@amazonnews), TWITTER (Oct. 23, 2017, 7:41 AM), <https://twitter.com/amazonnews/status/922473078805762048> [<https://perma.cc/6G4Z-QUEY>].

20. The Texas Legislature created the Texas Enterprise Fund to allow the governor to negotiate directly with businesses on awarding job-creation tax credits. The law requires an award agreement that includes the number of jobs that will be created and a deadline for the creation of the jobs. It also requires repayment if the jobs are not created by the appropriate deadline. TEX. GOV'T CODE ANN. § 481.078 (West 2019). Florida's Quick Action Closing Fund is similar. However, the bill's text includes criteria for making an award. Specifically, the economic benefit must be 5:1 (five dollars of benefit for every dollar of incentive) and jobs must pay at least 125 percent of the average private sector wage in the state or area. FLA. STAT. § 288.1088 (2018).

21. Legislatures are politically insulated because, at least in these two states, it is the governor's office that bears responsibility should a particular deal fall through.

22. Michigan was forced to negotiate a cap on tax incentives with the “Big Three” automakers following a strain on the state's \$10 billion general fund and a \$325 million midyear budget cut. See Chad Livengood et al., *Value of GM's State Tax Credits Remain Secret*, DET. NEWS (Dec. 15, 2015, 10:19 AM), <https://www.detroitnews.com/story/news/politics/2015/12/15/general-motors-mega/77352724/> [<https://perma.cc/6PW4-UPV8>].

economy.<sup>23</sup> In 2009, St. Louis, Missouri transferred building rights for 1500 acres of land to one developer for a project expected to develop the tax base. But thus far it has only resulted in a single gas station and grocery store.<sup>24</sup>

Areas that devote significant public resources to business location incentives often struggle with other public investments such as school funding.<sup>25</sup> Michigan, while a leader in public spending for business location incentives, lags in school-spending growth.<sup>26</sup> Predominantly African American school districts such as those in Detroit and Flint suffer from conscious decision-making that separates opportunity based on geography.<sup>27</sup>

Legal constraints originally emerged to protect the public and governments against the catastrophes associated with economic development activity gone awry. The public purpose doctrine—the principle that public funds should not go to private parties without a public purpose—emerged in the mid-1800s following public investments in speculative railroad construction.<sup>28</sup> Around

23. Tim Knauss, *Empire Zones, NY's Failed Aid to Companies, Still Costing Taxpayers: \$3 Billion Plus*, SYRACUSE.COM (Aug. 9, 2017, 10:13 AM), [https://www.syracuse.com/state/index.ssf/2017/08/empire\\_zones\\_nys\\_failed\\_aid\\_to\\_companies\\_keep\\_costing\\_taxpayer\\_s\\_3\\_billion\\_plus.html](https://www.syracuse.com/state/index.ssf/2017/08/empire_zones_nys_failed_aid_to_companies_keep_costing_taxpayer_s_3_billion_plus.html) [<https://perma.cc/P48P-8TUN>] (“I’ve never done a study on Empire Zones . . . I would say the empirical evidence . . . suggests that what we were doing, we should not be doing,” said the current head of New York State’s economic development agency.)

24. Jacob Barker, *St. Louis Wants to Cut Ties with Northside Developer Paul McKee*, ST. LOUIS POST-DISPATCH (June 13, 2018), [https://www.stltoday.com/business/local/st-louis-wants-to-cut-ties-with-northside-developer-paul/article\\_88ba714f-10be-5665-be8a-e3df35f5e341.html](https://www.stltoday.com/business/local/st-louis-wants-to-cut-ties-with-northside-developer-paul/article_88ba714f-10be-5665-be8a-e3df35f5e341.html) [<https://perma.cc/2CSG-7A3C>]; David Nicklaus, *With Northside Stalled, It's Time to Rethink City's Development Approach*, ST. LOUIS POST-DISPATCH (July 1, 2018), [https://www.stltoday.com/business/columns/david-nicklaus/with-northside-stalled-it-s-time-to-rethink-city-s/article\\_51c04811-0979-58da-9586-e5c82fd674a1.html](https://www.stltoday.com/business/columns/david-nicklaus/with-northside-stalled-it-s-time-to-rethink-city-s/article_51c04811-0979-58da-9586-e5c82fd674a1.html) [<https://perma.cc/6T7Z-GNVZ>].

25. Michigan, for instance, ranked last among states in total education revenue growth from 1995 to 2015. DAVID ARSEN ET AL., MICHIGAN SCHOOL FINANCE AT THE CROSSROADS: A QUARTER CENTURY OF STATE CONTROL 1, 7 (2019), <http://education.msu.edu/ed-policy-phd/pdf/Michigan-School-Finance-at-the-Crossroads-A-Quarter-Center-of-State-Control.pdf> [<https://perma.cc/6VSN-AN8M>].

26. *Id.* at 1.

27. RICHARD SCHRAGGER, CITY POWER: URBAN GOVERNANCE IN A GLOBAL AGE 243 (2016).

28. The legal academic scholarship on the public purpose doctrine begins with a focus on government’s inability to levy taxes but for public purposes. Francis W. Bird, *The Evolution of Due Process of Law in the Decisions of the United States Supreme Court*, 13 COLUM. L. REV. 37, 43 (1913) (“[T]he fundamental law restrains a state legislature from authorizing the issuance of bonds in aid of a private purpose.”); Breck P. McAllister, *Public Purpose in Taxation*, 18 CALIF. L. REV. 137, 137 (1930) (“It was to curb governmental expenditures that the doctrine of public purpose was first used in state court . . . .”); Howard Lee McBain, *Taxation for a Private Purpose*, 29 POL. SCI. Q. 185, 185 (1914) (discussing the maxim that public authorities may not levy taxes for private purposes). More recently, scholarship has focused on the expanding importance of subsidizing economic development by government. See generally Martin E. Gold, *Economic Development Projects: A Perspective*, 19 URB. LAW. 193 (1987) (discussing different state and local governments’ economic development projects and the legal constraints they face, most notably from the public purpose doctrine and state constitutional prohibitions); Martin E. Gold & Lynne B. Sagalyn, *The Use and Abuse of Blight in Eminent Domain*, 38 FORDHAM URB. L.J. 1119 (2011) (focusing on the role of “blight” in state and local government condemning property through eminent domain for economic development purposes after *Kelo v. City of New London*, 545 U.S. 469 (2005)).

that time, many states and the U.S. Supreme Court drastically limited state- and local-government wealth redistribution to private companies both through public purpose doctrine litigation and state constitutional amendments prohibiting such actions.<sup>29</sup>

Today, state- and city-government spending on economic development activity is enormous.<sup>30</sup> Courts barely constrain payments for such programs.<sup>31</sup> One recent study of litigation brought between 1994 and 2014 indicates that, in almost all cases, courts would not limit government outlays based on public purpose claims or related state constitutional prohibitions.<sup>32</sup>

Scholars who have studied government support for private economic development activity have proposed reforms. Substantive proposals have ranged from a focus on how projects impact communities<sup>33</sup> to compelling courts to use agency law instead of contract law principles in evaluating public purpose cases.<sup>34</sup> Scholars have suggested procedural reforms too. One procedural proposal would give state attorneys general more oversight over investigating subsidy programs.<sup>35</sup> Another procedural proposal argues for only allocating public funds for economic development activities through nonprofit corporations.<sup>36</sup>

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29. State and local spending was never banned completely. For instance, a leading mid-1800s case held that public support for private railroads *could* serve a public purpose. *Sharpless v. Mayor of Phila.*, 21 Pa. 147, 169 (1853) (“A railroad is a public highway for the public benefit . . .”). Other aid schemes to private companies were less favored by courts. The first U.S. Supreme Court case to discuss the public purpose requirement in the government’s economic development activities was decided in 1874. *See generally* *Loan Ass’n v. Topeka*, 87 U.S. (20 Wall.) 655 (1874) (holding that a city bond to be paid to a private ironworks company for bridge building was an *illegal* payment to a private corporation).

30. *See* Story et al., *supra* note 11. There is no single definition of the term “city.” It is used interchangeably throughout this Article with the term “local” to encompass substate government, including, for instance, county, city, town, or other political subdivision.

31. Richard Briffault, *The Disfavored Constitution: State Fiscal Limits and State Constitutional Law*, 34 RUTGERS L.J. 907, 945 (2003) (“[T]he public purpose requirement as a constraint on legislative action is a dead letter today.”).

32. *See generally* Brian Libgober, *The Death of Public Purpose (and How to Prevent It)* (Harvard Univ. John M. Olin Ctr. for Law, Econ. & Bus., Discussion Paper No. 63, 2016), [http://www.law.harvard.edu/programs/olin\\_center/fellows\\_papers/pdf/Libgober\\_63.pdf](http://www.law.harvard.edu/programs/olin_center/fellows_papers/pdf/Libgober_63.pdf) [<https://perma.cc/T7PS-BUMN>] (discussing a correlation, though not causation, between the decrease in the filing of public purpose doctrine cases and an increase in state and local government debt).

33. Comment, *The “Public Purpose” of Municipal Financing for Industrial Development*, 70 YALE L.J. 789, 802 (1961) (arguing that courts ought to consider safety precautions, plans for disposal of industrial waste, transportation congestion, impact on public services, housing, and psychological tensions when considering the effects of a government financed industrial facility). “The argument for finding a public purpose becomes weaker if, for example, no provisions have been made for increased traffic, housing needs, sewerage disposal or health requirements.” *Id.*

34. *See* Libgober, *supra* note 32, at 5.

35. *See, e.g.*, Daniel J. Munoz, *AG to Probe \$11 Billion in NJ Tax Breaks*, NJBIZ (Jan. 14, 2019, 3:57 PM), <https://njbiz.com/ag-to-probe-11-billion-in-nj-tax-breaks/> [<https://perma.cc/CP5K-S848>] (describing a recent example of the attorney general’s investigation of state economic development subsidies).

36. *See* Dale F. Rubin, *The Public Pays, The Corporation Profits: The Emasculation of the Public Purpose Doctrine and a Not-for-Profit Solution*, 28 U. RICH. L. REV. 1311, 1313



Against all of this background rests the theory behind how subnational governments interact with, and encourage, private business investment.<sup>37</sup> While often overlooked, states and cities play important administrative and regulatory functions in shaping business-location decisions.<sup>38</sup> A significant critique, however, is that governmental incentives to influence private business location selection are much more specious than most anticipate.<sup>39</sup>

The simplest and most elegant solution to constraining subnational economic development spending is to limit such spending only to the types of public-works projects that are traditionally the sole realm of state and local government.<sup>40</sup> Such a limitation, however, is unlikely to be acceptable given that economic development spending is currently viewed permissively.<sup>41</sup> An intermediate step that both protects the public fisc and allows states and cities to spend money on economic development is a process with both procedural and substantive checks.

First, states and cities ought to consider a reverse auction approach to rationalize the subsidy-allocation process.<sup>42</sup> A reverse auction allows a seller to sell a predetermined amount of goods or services for the lowest price buyers are willing to pay for everything on sale. For example, Google used

(1994) (“[A]n examination of the historical development of the Public Purpose Doctrine establishes that the proliferation of . . . public subsidies . . . is unconstitutional.”).

37. See, e.g., Timothy J. Bartik, *Business Location Decisions in the United States: Estimates of the Effects of Unionization, Taxes, and Other Characteristics of States*, 3 J. BUS. & ECON. STAT. 14, 14–21 (1985).

38. See Richard C. Schragger, *Mobile Capital, Local Economic Regulation, and the Democratic City*, 123 HARV. L. REV. 482, 484 (2009) (“[C]ities have recently engaged in a flurry of efforts to redistribute capital, place conditions on it, or limit its entry.”).

39. SCHRAGGER, *supra* note 27, at 2 (“But how much of a city’s economic health is or can be attributed to the decisions made by city leaders is quite uncertain.”); Richard C. Schragger, *Rethinking the Theory and Practice of Local Economic Development*, 77 U. CHI. L. REV. 311, 313 (2009) (“[W]e do not have a consensus account of how cities form, develop, and grow or decline. Thus, any claim that one policy or another will generate local economic growth should be made with a great deal of skepticism.”).

40. Public works include infrastructure, such as roads, bridges, water and sewer facilities, and the like.

41. See Gold & Sagalyn, *supra* note 28, at 159. Courts have long deferred to legislatures in interpreting the meaning of a public purpose. *Kalkowski v. Neb. Nat’l Trails Museum Found., Inc.*, 826 N.W.2d 589, 598 (Neb. Ct. App. 2013) (“[I]t is for the Legislature to decide in the first instance what is and what is not a public purpose, for the purposes of expenditure of public funds . . .”). Encouraging economic and industrial growth through indirect activities like marketing and advertising expenditures is a public purpose. *Id.*

42. The government uses auctions to sell goods or services that it otherwise would need to set a price for. See ERIC A. POSNER & E. GLEN WEYL, *RADICAL MARKETS: UPROOTING CAPITALISM AND DEMOCRACY FOR A JUST SOCIETY* 50 (2018). Online advertising providers, like Google’s AdSense, use auctions to determine what ads will appear to a given user. *About the Ad Auction*, GOOGLE: ADSENSE HELP, <https://support.google.com/adsense/answer/160525?hl=en> [<https://perma.cc/J3TE-ATBM>] (last visited Aug. 22, 2019). Online reverse auctions are commonplace in industrial procurement both for government and most major industries. Sandy D. Jap, *The Impact of Online Reverse Auction Design on Buyer-Supplier Relationships*, 71 J. MARKETING, Jan. 2007, at 146, 146. Jap notes the importance of buyers in designing reverse auctions to maintain relationships with suppliers. *Id.*

a reverse auction in its initial public stock offering.<sup>43</sup> The initial price for a single share was set at the lowest price that all shares would be sold following a bidding process.<sup>44</sup> Frequent flyers on commercial airlines are familiar with efforts to engage passengers on an oversold flight to fly at a later date in exchange for vouchers towards future travel using a reverse auction.<sup>45</sup>

Here, the reverse auction process is similar. State or local government economic development agencies would announce a reverse auction proposal process.<sup>46</sup> Private employers are invited to bid on public incentives, such as job-creation tax credits. Employers bid on the dollar amount of job-creation tax credits that they would require to create full-time, or full-time-equivalent,<sup>47</sup> positions. The reviewing economic development agency would consult the bid list and award subsidies for the lowest amount of subsidy-per-job created until all of the budgeted subsidy funds are spent. Agencies could consider additional metrics, such as industry sector, amount of compensation per employee, and a residency requirement for the employees.

Second, recapture mechanisms linked to specific job numbers (retained or created) ought to be included in the contracts awarded through the bid process. This way, governments can precondition the release of funds based on specific, targeted, and predetermined metrics, and they can claw back funds spent on companies that accept subsidies but let workers go anyway. Governmental subsidy administrators may use clawback provisions to deter company flight based on particular community economic needs.<sup>48</sup>

There are potential benefits to involving state and local government in the economic development process using these two steps. Beyond ensuring public law norms, like openness, transparency, and accountability, the “publicization” of economic development activity allows for subnational governments to effect policy priorities. States and cities already exert regulatory control when contracting for construction services, by, for

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43. Ann E. Sherman, *Global Trends in IPO Methods: Book Building Versus Auctions with Endogenous Entry*, 78 J. FIN. ECON. 615, 616 (2005).

44. *Id.* at 629–30.

45. The Hub Team, *Introducing New Customer Options for Flexible Travel Plans*, UNITED (Nov. 7, 2017), <https://hub.united.com/united-new-customer-travel-options-2507483285.html> [<https://perma.cc/4CHM-LXLX>].

46. Government purchasing is typically regulated by state procurement laws. *See, e.g.*, N.Y. STATE FIN. LAW § 163 (McKinney 2019). Such laws often detail how bidding shall occur and under what circumstances—such as in a state of emergency, when such bidding processes may be suspended.

47. Individual agencies have the flexibility to craft their specific programs to reflect either full-time positions or several part-time positions combined to equal a full-time equivalency.

48. A recent academic work in political science and economics also suggests clawing back business location incentives for noncompliance as at least part of the solution to curbing abuse in such incentives. NATHAN M. JENSEN & EDMUND J. MALESKY, INCENTIVES TO PANDER: HOW POLITICIANS USE CORPORATE WELFARE FOR POLITICAL GAIN 201 (2018) (“Clawbacks can thus police fraud or legitimate poor performance of investments, but they do not address that many incentive dollars are duplicative, wasted on firms that would have come anyway.”). Currently, community benefit agreements and other regulatory tools allow communities or governments to negotiate and contract for such specific economic benefit terms with private companies. *See, e.g.*, Edward W. De Barbieri, *Do Community Benefits Agreements Benefit Communities?*, 37 CARDOZO L. REV. 1773, 1776 (2016).

example, requiring a percentage of companies to be owned by women, racial groups traditionally excluded from business ownership, or disabled veterans.<sup>49</sup>

State agency bidding for economic development is not uncommon. Tax credits to spur the creation of affordable housing—low-income housing tax credits (LIHTCs)—are issued by state agencies through an allocation process that is a form of bidding.<sup>50</sup> State housing agencies develop Qualified Allocation Plans to distribute LIHTCs.<sup>51</sup> The LIHTC program itself is facing a crisis since private developers created over 80 percent of affordable housing units—units which will revert to private ownership following the expiration of the tax credits and possibly lead to increased evictions for low-income renters.<sup>52</sup>

A two-step reverse auction and clawback proposal could permit small employers to band together and make collective proposals for jobs and commercial real estate subsidies. Typically excluded from the largest subsidy projects, many small, start-up businesses are kept out of the economic development subsidy market. The proposed two-step approach invites smaller firms to work together to grow and collectively hire more workers.<sup>53</sup>

This Article starts out by analyzing the ways in which state and local officials use law to act as job buyers, often to the detriment of the public. Part I begins by discussing current legal tools available to states and cities to subsidize economic development. Next, Part I discusses competition and other political arguments advanced to support public wealth redistribution to private companies. Finally, this Part addresses the fiscal risks of unconstrained economic development spending. Part II then discusses current doctrinal and constitutional constraints on economic development spending, the ineffectiveness of the same, and existing scholarly substantive and procedural suggestions to constrain such spending.

This Article then analyzes avenues for legislatures and courts to constrain redistribution of public funds to private companies. Part III introduces two primary steps that elected officials should consider—and the judiciary ought to focus on—in reviewing such activities. The first step involves encouraging the use of reverse auctions to ensure that states and cities use the

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49. See, e.g., N.Y. EXEC. LAW § 313 (McKinney 2019).

50. Brandon M. Weiss, *Locating Affordable Housing*, 70 HASTINGS L.J. 215, 221 (2018).

51. I.R.C. § 42(m)(1)(A)(i) (2012) (“[S]uch amount was allocated pursuant to a qualified allocation plan of the housing credit agency which is approved by the governmental unit . . . of which such agency is a part.”).

52. Brandon M. Weiss, *Residual Value Capture in Subsidized Housing*, 10 HARV. L. & POL’Y REV. 521, 545 (2016).

53. While the two-step approach described here is novel, state and local governmental support for small firm job buying is not. New York State, for instance, replaced its failed Empire Zone program, see *infra* note 120, with a program designed specifically to incubate start-ups. *New York State Certified Business Incubators and Innovation Hot Spots*, N.Y. ST.: EMPIRE ST. DEV., <https://esd.ny.gov/certified-business-incubator> [<https://perma.cc/7TBJ-T7L2>] (last visited Aug. 22, 2019). The author directs a pro bono legal services program that partners with one of these incubators.

least amount of subsidy possible when buying jobs. The second step involves substantive analysis to ensure that laws provide clawback mechanisms tied to the actual number of jobs created or retained. Part IV applies the two-step proposal to existing programs used in Washington, Texas, and Florida.

The relationship between subnational governments and private businesses should be reassessed. Legal scholars ought to be skeptical of such governments setting industrial policy.<sup>54</sup> Because economic development programs do not appear to be going anywhere anytime soon, in the interim, alternatives to the status quo should be considered.

States and cities should have companies bid for subsidies.<sup>55</sup> A bidding process with definable job goals ensures that proposed economic development activity best meets the public purpose as outlined by the legislature, interpreted by the agency reviewing the bids, and, ultimately, reviewed by the courts.<sup>56</sup> The two-step reverse auction and clawback proposal argued for here is simpler, easier, and results in a more efficient redistribution of scarce public funds for needed economic development.<sup>57</sup>

## I. ECONOMIC DEVELOPMENT LAW: SUBSIDY TOOLS AND RISKS

### A. Taxes, Bonds, and Local Land Use

To create an effective reverse-auction and recapture process for economic development subsidies, governments must change their current method of financing job-buying. There are a number of tools available to states and cities to engage in economic development activity. These tools largely involve authorization via state legislation.<sup>58</sup> Taxation and bond issuances are the most common tools for revenue generation.<sup>59</sup> At the local level, land-use

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54. For a broader discussion about scholarly skepticism of cities setting industrial policy, see generally SCHRAGGER, *supra* note 27.

55. There have been other market-based proposals in the realm of urban economic development. See, e.g., Michael Heller & Rick Hills, *Land Assembly Districts*, 121 HARV. L. REV. 1465, 1468 (2008) (proposing a legal system for owners in a neighborhood to collectively decide whether the land should be assembled for development into a larger parcel).

56. By analogy, this process would work similarly to the way that projects are reviewed for environmental impact. The state or local government follows development guidelines in an environmental impact statement. Public hearings occur and written comments are accepted. As long as the state or local government agency follows the guidelines, a court will likely uphold the environmental impact statement process. See generally *Ordonez v. City of New York*, No. 450100/2018, 2018 N.Y. Misc. LEXIS 3002 (N.Y. Sup. Ct. July 11, 2018).

57. An empirical proposal of this sort is not alone in its effort to reform an otherwise wasteful political process. Scholars have argued that court analysis of gerrymandering cases would benefit from an *efficiency gap* analysis where courts look to see how many votes for either political party are wasted in a given district. See, e.g., Nicolas O. Stephanopoulos & Eric M. McGhee, *Partisan Gerrymandering and the Efficiency Gap*, 82 U. CHI. L. REV. 831, 834 (2015).

58. S. 5952, 63d Leg., 3d Spec. Sess. § 1 (Wash. 2013) (enacted); Gold, *supra* note 28, at 207.

59. Richard Briffault has pointed out how state constitutions contain the primary fiscal constraints for state and local governments. Briffault, *supra* note 31, at 908 (“[S]tate constitutions accord extensive consideration to state and local spending, borrowing, and taxing.”).

approvals are common to induce companies to relocate, remain, and expand operations in specific communities. Governments can spend by doing everything from the direct purchase of private corporation shares<sup>60</sup> to the construction of commercial property, which then gets leased to private interests.<sup>61</sup>

### 1. Taxation: Tax Exemption, Job-Creation Tax Credits, and Property Tax Abatements

States and cities frequently grant tax exemptions to spur private economic development. As discussed above, in 2013, the Washington State legislature extended aerospace tax preferences and expanded exemption of sales and use taxes for new plants manufacturing aerospace-related products.<sup>62</sup> The tax exemption was extended specifically on the condition that Boeing build a new manufacturing line—though not necessarily hire or retain a certain number of workers.<sup>63</sup>

Job-creation tax credits, on the other hand, are tax benefits directly connected to creating jobs and increasing payroll.<sup>64</sup> New York State's jobs tax credit program, called the Excelsior Jobs Program, conditions the issuance of credits based on the amount of funds companies plan to invest, as well as the particular type of industry in which the company operates.<sup>65</sup> Amazon was expected to receive \$1.2 billion in Excelsior Jobs Program tax credits for its new headquarters in Long Island City, New York.<sup>66</sup>

Cities frequently exempt local property taxes to encourage business relocation and commercial real estate development.<sup>67</sup> The Excelsior Jobs

60. *See* *Sharpless v. Mayor of Phila.*, 21 Pa. 147, 173, 175 (1853) (upholding the purchase by a city of shares in a railroad corporation).

61. Briffault, *supra* note 31, at 919–20 (“[S]tate or local government enters into an arrangement with a private firm or public authority bond issuer to lease the bond-financed facility for a period of time, with the government’s lease payments covering the annual debt service.”).

62. *See* Wash. S. 5952 § 1. The legislative findings of such an act of the legislature will prove important. Here, the legislature found, for example, “that the people of Washington have benefited enormously from the presence of the aerospace industry in Washington state. The legislature further finds that the industry continues to provide good wages and benefits for the thousands of engineers, mechanics, and support staff working directly in the industry throughout the state.” *Id.*

63. *See id.*

64. *See generally* BARTIK, *supra* note 14.

65. Scientific research and development, software development, and financial services are some of the strategic industries, but so are agriculture, manufacturing, and distribution. *Excelsior Jobs Program*, N.Y. ST.: EMPIRE ST. DEV., <https://cdn.esd.ny.gov/businessprograms/data/excelsior/excelsiorjobsprogramoverview.pdf> [<https://perma.cc/A24D-L886>] (last visited Aug. 22, 2019).

66. Letter from Howard Zemsky, President & Chief Exec. Officer, Empire State Dev., to Holly Sullivan, Head of WW Econ. Dev., Amazon.com Servs., Inc. (Nov. 12, 2018), <https://d39w7f4ix9f5s9.cloudfront.net/4d/db/a54a9d6c4312bb171598d0b2134c/new-york-agreement.pdf> [<https://perma.cc/JRE2-2ML9>].

67. Two examples in New York City from 2013 involved the Hudson Yards development on Manhattan’s West Side and the Willets Point development in Queens. *Hudson Yards, Willets Point Receive Tax Breaks*, CRAIN’S N.Y. BUS. (Dec. 9, 2013, 11:00 PM),

Program, for instance, includes funds for local property tax exemptions in addition to jobs tax credits.<sup>68</sup> Property tax exemptions often accompany discretionary land use approvals, which are addressed in greater detail below. Of note here, none of the types of exemptions mentioned above are auctioned off.<sup>69</sup> Instead, they are generally used to influence company location decisions. The exemption programs are the result of specific legislation authorized by state or local legislatures.

## 2. Bonding: General Obligation Bonds, Revenue Bonds, and Private Activity Bonds

States and cities authorize the issuance of bonds to fund development and support activities like private economic development.<sup>70</sup> The Internal Revenue Code (the “Code”) classifies state- and local-government bonds as either governmental bonds or private activity bonds.<sup>71</sup> Generally, private activity bonds are not tax-exempt, like governmental bonds are, unless the activities funded are qualified private activities.<sup>72</sup> Today, the major qualified private activities funded by private activity bonds are facilities built by hospitals, universities, and other private corporations.<sup>73</sup>

The subsidization of private companies includes instances where the state or city government builds a facility and then leases it to a private business. The private business pays rent, taking advantage of the lower interest rate that the government may obtain based on the tax-exempt nature of the bond. In some cases, the lease can be structured as a lease-to-own—whereby the company owns the property after making lease payments for a certain number of years.<sup>74</sup>

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[https://www.crainsnewyork.com/article/20131210/REAL\\_ESTATE/131219984/hudson-yards-willets-point-receive-tax-breaks](https://www.crainsnewyork.com/article/20131210/REAL_ESTATE/131219984/hudson-yards-willets-point-receive-tax-breaks) [<https://perma.cc/CY33-53P6>].

68. See, e.g., *Excelsior Jobs Program*, *supra* note 65.

69. See *id.* at 3 (describing the application process, which does not discuss an auction process—rather, applicants complete funding applications that may, if approved, lead to certificates allowing selected applicants to claim tax credits).

70. Borrowing is typically subject to allowable debt limits. For an in-depth, critical analysis of how states and local governments limit their borrowing, see generally Nadav Shoked, *Debt Limits’ End*, 102 IOWA L. REV. 1239 (2017).

71. See I.R.C. § 103 (2012). From a terminology perspective, “private activity bonds” were formerly known as “industrial development bonds”—a change that has created some problems. ROBERT S. AMDURSKY ET AL., *MUNICIPAL DEBT FINANCE LAW: THEORY AND PRACTICE* 498 (2d ed. 2013).

72. See I.R.C. § 141 (2012). In 1968, Congress continued the exemption of interest earned on “industrial development bonds” but set limits on the amount and purpose. ROBERT A. FIPPINGER, *THE SECURITIES LAW OF PUBLIC FINANCE* 47 (2d ed. 1998).

73. Martin Z. Braun & Sahil Kapur, *Congress’s Tax Bill Keeps Subsidies for Private Activity Bonds*, BLOOMBERG (Dec. 15, 2017, 5:15 PM), <https://www.bloomberg.com/news/articles/2017-12-15/congress-s-tax-bill-keeps-subsidies-for-private-activity-bonds> [<https://perma.cc/H6UE-552V>].

74. See, e.g., *Bd. of Dirs. of Indus. Dev. Bd. v. All Taxpayers*, 938 So. 2d 11, 26 (La. 2006).

While the Code sets caps on the amount of nonexempt private activity bonds,<sup>75</sup> leaseback or lease-and-sale arrangements allow governments to avoid the strict caps. Some argue that states and cities are smart to engage in creative transactions that permit support for private businesses when such activity would otherwise be prevented.<sup>76</sup> Courts struggle to set the outer limits of industrial support by subnational government.<sup>77</sup> While auctions are common tools for subnational governments to use in the disposition of property, they are not commonly used to influence business-location decisions.

Some state finance laws limit local government from taking on debt that exceeds the useful life of a capital project.<sup>78</sup> Robert S. Amdursky, Clayton P. Gillette, and G. Allen Bass point out that the effect of such regimes is twofold: first, it allows the municipality to require future users to pay their share of the costs of a capital project; second, it limits the ability of a current generation to require a future generation to pay for a project from which it derives no benefit.<sup>79</sup>

### 3. Auctions and Local Land Use

Local land use law mechanisms are additional economic development tools available to local governments to incentivize private economic development.<sup>80</sup> Currently, market-based principles of bidding and auctioning exist within the realm of local land use law. Examples of such market-based tools include tax increment financing districts, transferrable development rights, and even requests for development proposals, among others.

When county or city governments issue tax-exempt development bonds to condemn and improve land for a new manufacturing facility or corporate headquarters, they need a stream of revenue to pay off the bonds. In many cases, this is accomplished using the additional property tax revenue earned once the development sites are improved.<sup>81</sup> Known as tax-increment financing, the process, which dates back to California in 1952, begins with the city council approving a special tax-increment district and a project

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75. STEVEN MAGUIRE & JOSEPH S. HUGHES, CONG. RESEARCH SERV., RL31457, PRIVATE ACTIVITY BONDS: AN INTRODUCTION 17 (2018).

76. See, e.g., Tom Tew, *Industrial Bond Financing and the Florida Public Purpose Doctrine*, 21 U. MIAMI L. REV. 171, 194 (1966).

77. See generally Comment, *supra* note 33.

78. See AMDURSKY ET AL., *supra* note 71, at 12 (citing N.Y. LOCAL FIN. LAW § 11.00 (McKinney 1988 Supp.)).

79. *Id.*

80. The focus of this background section is on state and local subsidization tools. Additional subsidy tools exist at the federal level. Environmental Protection Agency waivers, for instance, provide additional subsidies to industry to encourage investments in new factories. A recent example is the Foxconn deal in Wisconsin. See Michael Hawthorne, *EPA Chief Pruitt Overrules Staff, Gives Wisconsin's Walker, Foxconn Big Break on Smog*, CHI. TRIB. (May 2, 2018, 6:49 AM), <http://www.chicagotribune.com/news/local/breaking/ct-met-smog-pruitt-foxconn-20180501-story.html> [https://perma.cc/FY59-8XJG].

81. Jerry Frug, *The Geography of Community*, 48 STAN. L. REV. 1047, 1087 (1996).

plan.<sup>82</sup> Following the plan's adoption, the tax base of the special district is frozen—any additional revenue is directed to pay off the bonds issued to fund the development.<sup>83</sup>

The otherwise logical nature of tax-increment financing plans belies their occasional controversial nuances. One botched tax-increment financing project in St. Louis, for instance, placed a plan to redevelop 1500 acres of urban land in limbo. Disagreement over the project has led the city and the developer, as well as the Missouri Attorney General, to court.<sup>84</sup> It is not unsurprising that tax-increment financing schemes can be politically controversial. The political economy of urban areas is often a source of political contention.

Other market-based mechanisms for auction-like bidding include transferable development rights and city issuances of requests for proposals. Transferrable development rights have been used in dense urban areas like New York City's Theater District.<sup>85</sup> Importantly, the transfer of development rights—the ability to take buildable air rights from one property and transfer them to another—has always been seen as a strictly private market.<sup>86</sup> A private market for transferrable development rights is certainly a kindred spirit to an auction for job-creation subsidies; once a government creates the program, transferrable development rights are exchanged in a purely private market without government intervention.

Over recent decades, cities holding large portfolios of vacant properties have turned to selling vacant land to mostly real estate speculators through auctions.<sup>87</sup> In New York City, government officials rarely place any conditions on auctions, which has led landowners to leave land vacant and community groups to oppose the auction process.<sup>88</sup>

Aside from auctions, cities transfer property through open requests for proposals (the "RFP" process). A recent RFP for a mixed-use commercial real estate project in Denver describes two properties that the city purchased

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82. See BERNARD J. FRIEDEN & LYNNE B. SAGALYN, *DOWNTOWN, INC.: HOW AMERICA REBUILDS CITIES* 97 (1989) (discussing the history and process of tax-increment financing processes and planning).

83. *Id.*

84. See generally *Smith v. City of St. Louis*, 395 S.W.3d 20 (Mo. 2013); Jacob Barker, *Paul McKee's Northside Regeneration Accused of Tax Credit Fraud in Lawsuit by Missouri Attorney General*, ST. LOUIS POST-DISPATCH (June 14, 2018), [https://www.stltoday.com/business/local/paul-mckee-s-northside-regeneration-accused-of-tax-credit-fraud/article\\_e067f2a6-18ec-5d5f-8e54-ab7a2f2cba0c.html](https://www.stltoday.com/business/local/paul-mckee-s-northside-regeneration-accused-of-tax-credit-fraud/article_e067f2a6-18ec-5d5f-8e54-ab7a2f2cba0c.html) [<https://perma.cc/K5S9-S552>] (describing attorney general's lawsuit and its potential to terminate the financing agreement).

85. Norman Marcus, *Air Rights in New York City: TDR, Zoning Lot Merger and the Well-Considered Plan*, 50 BROOK. L. REV. 867, 900 (1984) (discussing the designation of a special Theater District that both preserved the unique neighborhood flavor and provided developers with general growth incentives).

86. *Id.* at 903.

87. See, e.g., TOM ANGOTTI, *NEW YORK FOR SALE: COMMUNITY PLANNING CONFRONTS GLOBAL REAL ESTATE* 100 (2008) (discussing the way New York City began disposing of its accumulated vacant properties).

88. *Id.* ("In the throes of the abandonment crisis, communities mobilized to stop the city auctions.").



for affordable housing, among other uses.<sup>89</sup> The RFP process allows governments to solicit interest from developers to construct a particular project.<sup>90</sup> The RFP process is a way for government to access the market when it seeks services at a fair price.<sup>91</sup> Also, the RFP process is a way for government to regulate private market activity—in this example, commercial real estate development—in a way that is consistent with public law norms.<sup>92</sup>

*B. Competitiveness: State and Local Government Arguments for Economic Development Activities*

In the last thirty years, state and local government incentive spending has spiked.<sup>93</sup> A number of states stand out. New York leads at over \$13 billion.<sup>94</sup> Close behind are Washington State at just under \$12 billion, Michigan at just under \$11 billion, and Louisiana at just under \$10 billion.<sup>95</sup>

It is commonplace for businesses to pit states and cities against each other when choosing where to locate a new factory or headquarters.<sup>96</sup> In addition, to retain existing businesses, governors and local executive officials routinely argue that subsidies are needed to keep businesses in a given locale.<sup>97</sup> These subsidies are largely a response to threats from private companies to move their operations elsewhere.<sup>98</sup> Thus, the reasoning goes, jurisdictions need to offer subsidies to remain competitive.<sup>99</sup>

89. DENVER OFFICE OF ECON. DEV., 2018 REQUEST FOR PROPOSALS (RFP) 1 (2018), [https://www.denvergov.org/content/dam/denvergov/Portals/344/documents/RealEstate/rfp/8315/East%20Colfax%20RFP\\_Final\\_8315.pdf](https://www.denvergov.org/content/dam/denvergov/Portals/344/documents/RealEstate/rfp/8315/East%20Colfax%20RFP_Final_8315.pdf) [<https://perma.cc/5JKX-MJ7B>].

90. *Id.*

91. *Id.*

92. *See id.* (proposing that affordable housing be constructed). Fundamentally, land use controls differ from direct economic development support. State or local governments exclusively provide land-use controls. Land is unique. Economic development loans, grants, or other incentives are financial in nature. Developers can choose to take or leave them. *See Vicki Been, Community Benefits Agreements: A New Local Government Tool or Another Variation on the Exactions Theme?*, 77 U. CHI. L. REV. 5, 34 (2010) (noting that when local governments elect to subsidize a project, any developer who opposes the local government's restrictions can simply decline to be involved).

93. *See* BARTIK, *supra* note 14, at 1 (“Business incentives have more than tripled since 1990.”).

94. *See* MATTERA ET AL., *supra* note 1 (estimating the total spending in New York State to be \$13,344,524,119 across 33 projects receiving at least \$50 million in subsidies).

95. *Id.* (estimating the total spending for Washington State to be \$11,944,000,000 across just two projects, for Michigan to be \$10,891,136,000 over 35 projects, and for Louisiana to be \$9,716,976,012 over 26 projects).

96. *See* Amazon News, *supra* note 19 (describing the 238 cities that pitched Amazon incentives to locate new headquarters); *Tesla, Nevada Agree on Finalized Incentive Agreement*, L.V. SUN (Aug. 3, 2015), <https://lasvegassun.com/news/2015/aug/03/tesla-nevada-agree-finalized-incentive-agreement/> [<https://perma.cc/2928-7YLK>].

97. *See* FLA. STAT. § 288.1088 (2018); TEX. GOV'T CODE ANN. § 481.078 (West 2019); *supra* note 20 and accompanying text (describing two such funds in each state respectively).

98. In the Florida and Texas examples, the governors are authorized to use legislative funds only when a company is considering another state in addition to either Florida or Texas. *See* FLA. STAT. § 288.1088 (2018); TEX. GOV'T CODE ANN. § 481.078 (West 2019).

99. *See* FLA. STAT. § 288.1088 (2018) (“The Legislature therefore declares that sufficient resources shall be available to respond to extraordinary economic opportunities and to

Some businesses will pursue subsidies for expansion projects and argue that subsidies are needed to prevent competition from another state.<sup>100</sup> In the case of the aerospace subsidy in Washington State, Boeing threatened relocation to another state to, among other sweeteners, extract union concessions.<sup>101</sup> In another instance, Intel, one of the largest employers in New Mexico, invested \$26 billion in local expansion—financed through the issuance of industrial development bonds.<sup>102</sup> In contrast to the Boeing incentive package, Intel’s arrangement with New Mexico merits additional study. First, Intel is required to disclose how it is meeting the job targets required in the bond issuance.<sup>103</sup> Second, there are clawback provisions that apply if Intel fails to meet its obligations under the bond issuance agreement.<sup>104</sup> This reporting requirement and clawback mechanism are unique among projects of a similar subsidy size.<sup>105</sup>

A number of states, including Texas and Florida, empower their governors to quickly close deals with businesses promising to engage in commercial real estate development in their state. Texas’s governor can access a fund to close deals with companies that threaten to move to another state because of competition.<sup>106</sup> The legislature created and funded the Texas Enterprise Fund in 2003.<sup>107</sup> Through the end of September 2018, the Texas Enterprise Fund offered over \$609 million—and disbursed over \$503 million—in support of a claimed 93,806 direct jobs.<sup>108</sup> Of the amount disbursed, over \$48 million was repaid and almost \$28 million was recovered through a liquidated damages repayment—a clawback.<sup>109</sup>

Florida has adopted a similar approach to Texas. The Florida legislature ratified a Quick Action Closing Fund to give the governor’s office the resources to rapidly close deals.<sup>110</sup> This fund has proven controversial and

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compete effectively for these high-impact business facilities, critical private infrastructure in rural areas, and key businesses in economically distressed urban or rural communities . . .”).

100. This was certainly the case with the Boeing example. *See General Information: Employment Data*, *supra* note 3.

101. *See* Scott, *supra* note 3.

102. Rachel Sams, *Intel Rio Rancho Capital Spending Rises as Jobs Decline Appears to Slow*, ALBUQUERQUE BUS. FIRST (Apr. 17, 2018, 5:40 PM), <https://www.bizjournals.com/albuquerque/news/2018/04/17/intel-rio-rancho-capital-spending-rises-as-jobs.html>

[<https://perma.cc/T9A4-L2GU>] (describing Intel’s reporting and compliance with terms agreed to with New Mexico in exchange for jobs subsidies).

103. *Id.*

104. *Id.*

105. The author reviewed the fifty most expensive subsidies in the Good Jobs First database and found that New Mexico was an early adopter of the clawback requirement. *See* MATTERA ET AL., *supra* note 1, at 3.

106. *See* TEX. GOV’T CODE ANN. § 481.078(k) (West 2019); *see also* *Texas Enterprise Fund*, TEX. ECON. DEV., <https://gov.texas.gov/business/page/texas-enterprise-fund> [<https://perma.cc/YZ23-CCVH>] (last visited Aug. 22, 2019).

107. *See* TEX. GOV’T CODE ANN. § 481.078 (West 2019).

108. *Texas Enterprise Fund (TEF) as of September 30, 2018*, TEX. ECON. DEV., [https://gov.texas.gov/uploads/files/business/TEF\\_Listing\\_10-11-18.pdf](https://gov.texas.gov/uploads/files/business/TEF_Listing_10-11-18.pdf) [<https://perma.cc/8BWY-E292>] (last visited Aug. 22, 2019).

109. *Id.*

110. *See* FLA. STAT. § 288.1088 (2018).

several prominent Republican state legislators zeroed it out in recent budget negotiations, calling it “corporate welfare.”<sup>111</sup> Governor Rick Scott, in seeking \$85 million for the fund from the legislature, said, “Florida has to compete with 49 other states and global markets across the world for jobs and I will fight to make sure we have every available tool to remain competitive.”<sup>112</sup> Arguments for the need to subsidize businesses based on competition grounds have a similar, if not stale, odor.

Public outrage about government subsidies for private companies generally falls into one of three categories. One category of outrage stems from companies taking incentives and then cutting jobs and closing plants anyway.<sup>113</sup> This category of outrage is illustrated by workers in the Midwest who are disillusioned by competition from overseas manufacturing.<sup>114</sup> Many of them responded to the economic nationalism message of the 2016 Trump campaign.<sup>115</sup>

A second category is outrage about subsidies attracting new companies from outside a jurisdiction. A third category is general outrage at the idea of the government propping up private companies at all. Outrage in this broad category comes from liberals who would prefer government to invest in public infrastructure projects, education, health care, and more.<sup>116</sup> In addition, outrage in this category comes from conservatives who would prefer government to cut taxes and reduce its size and influence over private

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111. Matt Dixon, *Scott's Divisive Incentive Fund Attracts Big Deals, and Its Share of Critics*, POLITICO (Jan. 6, 2017, 5:31 AM), <https://www.politico.com/states/florida/story/2017/01/scotts-divisive-incentive-fund-attracts-big-deals-and-its-share-of-critics-108509> [<https://perma.cc/R9HS-U6NF>].

112. *Id.*

113. Autoworker outrage in Michigan and other Midwest states is illustrative. The Michigan legislature, for example, has acted to keep and grow jobs in the auto industry and other fields. In particular, Michigan's legislature passed the Michigan Economic Growth Authority Act in 1995 to provide job creation tax incentives to businesses. *See* MICH. COMP. LAWS § 207.801 (1995). Some of the incentives proved too favorable to automakers, like General Motors, which agreed to limit its most recent round of incentives from 2009, but per agreement with the state, failed to disclose the total amount of the incentives. *See* Livengood et al., *supra* note 22.

114. *See* Scott Horsley, *Trump Administration Threatens to Withhold Subsidies from GM*, NPR (Nov. 27, 2018, 3:26 PM), <https://www.npr.org/2018/11/27/671231681/trump-administration-threatens-to-withhold-subsidies-from-gm> [<https://perma.cc/F4TH-6V89>].

115. President Trump's 2016 victory in Pennsylvania can be attributed in part to his margin of victory in Luzerne County, a county that twice went for Obama. In 2016, 60 percent of Trump's 44,000 vote win in Pennsylvania came from Luzerne County (26,000 votes). At the same time, manufacturing jobs in Luzerne County have declined from 42,000 in 1980 to 19,000 now. Shannon M. Monnat & David L. Brown, *More Than A Rural Revolt: Landscapes of Despair and the 2016 Presidential Election*, 55 J. RURAL STUD. 227, 236 (2017).

116. *See, e.g.*, Editorial, *Amazon News Shows How Corporate Incentive Arms Race Is Bad for Delaware: Editorial*, DEL. ONLINE (Nov. 14, 2018, 4:43 PM), <https://www.delawareonline.com/story/opinion/editorials/2018/11/14/amazon-news-shows-problem-incentive-arms-race-editorial/1999842002/> [<https://perma.cc/Y7DS-BUJZ>] (arguing that states should compete for jobs by investing in infrastructure, education, and job training); *see also* Alexandria Ocasio-Cortez (@AOC), TWITTER (Nov. 12, 2018, 11:40 PM), <https://twitter.com/Ocasio2018/status/1062203458227503104> [<https://perma.cc/6WS2-U9EW>] (“We’ve been getting calls and outreach from Queens residents all day about this. The community’s response? Outrage.”).

citizens and the economy.<sup>117</sup> Criticism of the recent Amazon HQ2 and HQ3 selection processes illustrates both the second and third types of outrage from both ends of the political spectrum.<sup>118</sup> Unsurprisingly, Amazon is steeling itself against popular outrage by engaging local lobbyists to protect its promised incentives.<sup>119</sup>

None of the examples or programs mentioned in this section made use of auctions to distribute incentives. The named categories of outrage will be revisited in the context of potential solutions. For now, the focus of the discussion shifts to the potential negative impacts of private economic development activity on state and local budgets.

### C. Fiscal Risks to State and Local Governments Due to Economic Development Activities

A challenge to analyzing the effectiveness of a given program is lack of information. A number of state economic development programs, often led by independent economic development agencies authorized to cut deals, involve a very low degree of transparency.<sup>120</sup> In some instances, economic development programs have caused state revenue crises as the programs were implemented. The Empire Zone program,<sup>121</sup> which lapsed in 2010 in New York State, failed to restart economic activity in rust-belt cities like Buffalo, Rochester, and Syracuse.<sup>122</sup> But there were bright spots in the Empire Zone program, such as a new microchip manufacturing plant in the Saratoga Springs area opened by worldwide semiconductor company Global Foundries.<sup>123</sup>

Yet, data on the Empire Zone program is difficult to obtain.<sup>124</sup> Local governments were given autonomy to draw boundaries of specific zones.<sup>125</sup> New York was not unique in making these types of missteps. However, the

117. See Editorial, *supra* note 8.

118. See Veronique De Ruyg, *Alexandria Ocasio-Cortez Is Right About Amazon's Corporate Welfare*, NAT'L REV. (Nov. 13, 2018, 2:36 PM), <https://www.nationalreview.com/corner/rep-alexandria-ocasio-cortez-is-right-about-amazons-corporate-welfare/> [<https://perma.cc/K4VC-ZPBC>].

119. See Ankita Rao, *Amazon Is Bringing in Elite Lobbyists Amid Seething Rage Over HQ2*, VICE (Dec. 6, 2018, 5:56 PM), [https://www.vice.com/en\\_us/article/nepq7q/amazon-is-bringing-in-elite-lobbyists-amid-seething-rage-over-hq2](https://www.vice.com/en_us/article/nepq7q/amazon-is-bringing-in-elite-lobbyists-amid-seething-rage-over-hq2) [<https://perma.cc/K5Z8-9GPF>].

120. See, e.g., Michigan Economic Growth Authority Act, MICH. COMP. LAWS § 207.801 (2019); S. 1-B, 1999–2000 Leg., Reg. Sess. (N.Y. 1999) (enacted).

121. See N.Y. S. 1-B.

122. See Knauss, *supra* note 23. Notably, the Empire Zone program allowed businesses to take credits over fourteen years, allowed for refundability of those tax credits, and permitted (early on) “shirt changing” where a company could double dip on the credits by changing its corporate names. *Id.* The program also supported retail, an industry that experts argue should not be subsidized. See BARTIK, *supra* note 14, at 13, 50. Law firms took advantage too. See Knauss, *supra* note 23.

123. This plant brought 3000 jobs to New York State's Capital Region at a subsidy of around \$1 billion, around half of which came through Empire Zone tax credits. See Knauss, *supra* note 23.

124. One journalist in Syracuse obtained information following a Freedom of Information Law request. *Id.*

125. *Id.* (discussing how hydro companies paid local governments to draw boundaries).

Empire Zone program brought New York to the top of the standings in terms of state spending on private economic development activity.<sup>126</sup>

In one particularly egregious example, a developer in Syracuse, New York engaged in planning that was “dominated by brainstorming ways to use taxpayers’ money” to expand Destiny USA—a shopping mall.<sup>127</sup> The developer “worked with a philosophy that nothing could get in the project’s way—not laws, financial hurdles or the practical difficulty of building something so big.”<sup>128</sup> Support from local government was all but assured. As a result, the group “never worried about opposition from City Hall . . . [because] the city [w]as desperate for development.”<sup>129</sup>

The most fanciful plans for the Destiny USA project ultimately did not come to fruition.<sup>130</sup> The scope of the project was impractical and otherwise seemingly aimless, other than the fact that it was designed to soak up tax incentives.<sup>131</sup> After building a vastly scaled-down version of what was originally planned, Pyramid, the developer, announced that it would not move forward with the remaining planned development.<sup>132</sup> Yet, the local tax base has not grown since the company still retains decades of local property tax exemptions.<sup>133</sup>

The Destiny USA example teaches three lessons. First, developers frequently view themselves as having leverage over city officials because the declining Rust Belt needs economic development to grow tax revenue. Second, focusing on low-wage sectors, like retail, typically will not be fruitful compared to high-skilled, high-paying sectors of the economy like high-tech services and manufacturing. Third, the law should scrutinize efforts to subsidize private economic development activity undertaken without meaningful review, oversight, transparency, or accountability.<sup>134</sup>

The Michigan Economic Growth Act, which was implemented by the Michigan Economic Development Corporation (MEDC), is also noteworthy for its lack of transparency and fiscal precariousness.<sup>135</sup> The act created the Michigan Economic Growth Authority (MEGA), which oversaw a tax credit program intended to prop up the declining auto manufacturing sector during the Great Recession.<sup>136</sup> In a moment of questionable legislation, the program

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126. See BARTIK, *supra* note 14, at 68.

127. See John O’Brien, *Inside Planning Destiny USA: It Was All About the “Golden Cow” of Tax Breaks*, SYRACUSE.COM (July 1, 2012), [https://www.syracuse.com/news/index.ssf/2012/07/inside\\_planning\\_destiny\\_usa\\_it.html](https://www.syracuse.com/news/index.ssf/2012/07/inside_planning_destiny_usa_it.html) [<https://perma.cc/2TV9-YZTZ>].

128. *Id.*

129. *Id.*

130. Rick Moriarty & Tim Knauss, *Destiny USA’s Untaxed Anti-climax: After 13 Years, It Is What It Is*, SYRACUSE.COM (June 7, 2012), [https://www.syracuse.com/news/index.ssf/2012/06/destiny\\_usas\\_untaxed\\_anti-clim.html](https://www.syracuse.com/news/index.ssf/2012/06/destiny_usas_untaxed_anti-clim.html) [<https://perma.cc/Q7JC-VU3T>].

131. See O’Brien, *supra* note 127.

132. See Moriarty & Knauss, *supra* note 130.

133. *Id.*

134. For a discussion of “opportunity zones,” see *infra* Part IV.D.

135. See MICH. COMP. LAWS § 207.801 (2019).

136. See *id.*; Chad Livengood, *Michigan Pays Price for Auto Investment*, DET. NEWS (Feb. 5, 2015, 12:15 PM), <https://detroitnews.com/story/news/politics/2015/02/05/michigan-tax-credits-car-companies/22908711/> [<https://perma.cc/3NRP-32XA>].

issued *unlimited* tax incentives to the largest auto manufacturers.<sup>137</sup> In one instance, General Motors (GM) only agreed to cap the amount of tax credits it received following a massive impending fiscal crisis.<sup>138</sup> In exchange for not having to disclose the value of the tax credits, GM finally agreed to a cap.<sup>139</sup> Eventually, in July 2014, Michigan reported that GM's tax credits exceeded \$2.1 billion.<sup>140</sup> Ford agreed to cap its tax credits at \$2.3 billion, and Fiat Chrysler agreed to a \$1.7 billion cap.<sup>141</sup>

Since both the Empire Zone and MEGA programs have ended, it is difficult to obtain data about the programs. Focus on newer replacement programs also further obscures the prior programs. This is unfortunate since the original programs themselves were no help to state fiscal budgets. State governments have had difficulty being successful in this area. In most cases, government fails because it is trying to do more than private companies: it seeks to either extend a mature and declining industry or actively launch a new technology sector.<sup>142</sup>

## II. DOCTRINAL AND CONSTITUTIONAL LIMITS HAVE FAILED TO CONSTRAIN JOB-BUYING LAWMAKING

Legal and judicial efforts have failed to check wealth redistribution to private companies. Historically, the shift to industrialization and new developments in technology have led state governments to encourage private enterprise.<sup>143</sup> In the mid-1800s, new infrastructure projects, such as canals, bridges, and railroads, brought about direct government support for companies.<sup>144</sup> When particular enterprises failed—canal corporations went bankrupt or railroad companies collapsed—the public scrutinized government support for private industries.<sup>145</sup> Significantly, the years

137. See Jarrett Skorup, *MEGA Failure: Job Projections from Michigan Tax Credit Program Rarely Came True*, MICH. CAPITOL CONFIDENTIAL (May 15, 2014), <https://www.michigancapitolconfidential.com/MEGA-program-a-complete-failure> [https://perma.cc/6F86-YTDW] (noting that the “original cap on the number of credits issued per year was eliminated”).

138. See Livengood et al., *supra* note 22.

139. See *id.*

140. See Livengood, *supra* note 136 (“Michigan faces years of budget uncertainty because state leaders awarded billions of dollars in tax credits mostly to Detroit’s three automakers to save tens of thousands of manufacturing jobs during the Great Recession . . . . General Motors has been awarded more than \$2.1 billion in refundable tax credits by the Granholm and Snyder administrations—the most of any automaker.”).

141. *Id.*

142. MARIANA MAZZUCATO, *THE ENTREPRENEURIAL STATE: DEBUNKING PUBLIC VS. PRIVATE SECTOR MYTHS* 18 (2015).

143. Ellis Leigh Waldron, *The Public Purpose Doctrine of Taxation* 34 (1952) (unpublished B.A. thesis, University of Washington) (on file with author) (“The tremendous capital demands of canal, road and railroad development were at that time beyond the reach and inclination of private capital reserves. So the state governments assumed the burden.”).

144. *Id.* at 34–35 (noting that in New York, income from fees to use the Erie Canal offset the need for the state to levy taxes to pay for the cost of the canal’s construction).

145. Several factors led to the change in public attitude against government assisting private businesses: (1) high rates of default, (2) a belief that private companies did not need public support, (3) skepticism about government favoring some companies over others, (4)

between the financial crises of 1837 and 1857 were some of the most frenzied in the area of developing the “internal arteries of commerce.”<sup>146</sup> Much of the investment dollars that fueled the construction binge of the time came from foreign European shores.<sup>147</sup>

At the same time, cities and towns were, and continue to be, dependent on private economic development activity.<sup>148</sup> Thus, planning, designing, constructing, and maintaining infrastructure to support private enterprise is closely aligned with the goals of local elected officials and administrative agency staff.<sup>149</sup> The importance of attracting and retaining private businesses is central to the existence of state and local administrative agencies.<sup>150</sup>

Yet, information about state and local incentives to private businesses is very limited.<sup>151</sup> Further, studies suggest that no state tests whether the legislative efforts to create jobs through incentives are working.<sup>152</sup> As a result, it is unclear whether economic growth actually results from economic development activity by government.<sup>153</sup> Nevertheless, lawmakers continue to dole out incentives to private companies.<sup>154</sup> Two primary legal constraints, one doctrinal and one constitutional, have developed to limit government support for economic development activities.

The public purpose doctrine emerged in response to a number of concerns about wasteful government spending. Each of the fifty states has codified the public purpose doctrine by placing limits on direct gifts, loans, or the

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fear of corruption, (5) fear of government’s intervention in free markets, and (6) government not sharing in the profits of private enterprise. Gold, *supra* note 28, at 201.

146. Waldron, *supra* note 143, at 32 (describing significant public infrastructure investment in railroads as “produc[ing] more wealth, more waste, more hope and disillusion than any previous twenty years in the country’s history” (quoting THOMAS C. COCHRAN & WILLIAM MILLER, *THE AGE OF ENTERPRISE* 52 (1942))).

147. *Id.*

148. Mulligan, *supra* note 16, at 2023 (describing local government incentive payments to induce businesses to locate within the granting jurisdiction).

149. State and local officials are also under increasing pressure to maintain business-friendly social and economic policy as a means of encouraging economic development. The recent “Bathroom Bill” in North Carolina allowing LGBT discrimination led to athletic conferences and private companies pressuring the state to change the law. See Richard C. Schragger, *The Attack on American Cities*, 96 TEX. L. REV. 1163, 1229 (2018) (“[The North Carolina bathroom ban] is also an example of how economic development remains a central concern of state and local politicians and an important driver of policy.”).

150. An early example of a state agency charged with economic development is the New York State Urban Development Corporation. Gold, *supra* note 28, at 215. For a discussion of local administrative agencies in modern urban governance, see generally Nestor M. Davidson, *Localist Administrative Law*, 126 YALE L.J. 564 (2017).

151. See BARTIK, *supra* note 14, at 117–18.

152. See BRANDON BROCKMYER ET AL., PEW CTR. ON THE STATES, EVIDENCE COUNTS: EVALUATING STATE TAX INCENTIVES FOR JOBS AND GROWTH 1 (2012) (“[N]o state regularly and rigorously tests whether those investments are working and ensures lawmakers consider this information when deciding whether to use them, how much to spend, and who should get them.”).

153. Richard Schragger makes this point over the course of his recent book, *City Power*. Schragger argues that we ought to be skeptical generally about subnational governments making industrial policy. See generally SCHRAGGER, *supra* note 27.

154. See Story et al., *supra* note 11.

extension of government credit for private interests.<sup>155</sup> Additionally, state constitutional amendments followed the development of the public purpose doctrine.

Yet, courts are unwilling to constrain state and local spending on private businesses. The public purpose doctrine is ineffective as a limit on legislative action.<sup>156</sup> Courts broadly interpret the public purposes of economic development activities to fall within allowable limits.<sup>157</sup> Also, courts read a public purpose exception into constitutional limits on government spending for private enterprise.<sup>158</sup>

*A. Courts Defer to Legislatures in Broadly Interpreting the Public Purposes of Economic Development Activities*

Generally, the government may not use public funds for the benefit of private interests.<sup>159</sup> There must be a public purpose when government allocates public resources. The definition of a public purpose, however, is not well-settled in the law.<sup>160</sup> Courts apply a broad standard: the legislature has broad discretion to determine whether an action constitutes a public purpose.<sup>161</sup> Courts should only restrain “clearly evasive” legislative actions.<sup>162</sup>

As early as the mid-1800s, courts addressed matters involving the authority of cities to levy taxes to pay for state-supported infrastructure projects. One case in the Supreme Court of Appeals of Virginia, *Goddin v. Crump*,<sup>163</sup> involved a tax levied by the city of Richmond to fund the purchase of shares in a state-chartered corporation whose purpose was to connect Richmond to the Ohio River via canal.<sup>164</sup> The court in *Goddin* held that the

155. Rubin, *supra* note 36, at 1313 n.15 (“All fifty states either have amended their constitutions to include the [public purpose] doctrine or the doctrine has received judicial sanction.”).

156. Briffault, *supra* note 31, at 945.

157. Robert S. Amdursky, *The Urban Crisis, Private Enterprise, and State Constitutions: A Plan for Action*, 19 SYRACUSE L. REV. 618, 631 (1968) (“All that is necessary to insure the constitutionality of a particular expenditure is a legislative finding of public purpose confirmed by the state’s highest court.”).

158. *Id.* (“[N]o state decision on ‘public purpose’ has ever been overruled by the Supreme Court.”).

159. See *State ex rel. Ohio Cty. Comm’n v. Samol*, 275 S.E.2d 2, 9 (W. Va. 1980) (Neely, C.J., concurring); Waldron, *supra* note 143, at 1 (“Midway through the nineteenth century, American courts developed the idea that government may tax its people only if such exactions are to finance objects of [public] benefits.”).

160. Rubin, *supra* note 36, at 1313 (arguing that no real limits exist on the government’s power to raise a tax to enrich a private company regardless of whether the current judicial test is to find a public benefit or simply judicial obedience to legislative findings).

161. *Associated Gen. Contractors of S.D., Inc. v. Schreiner*, 492 N.W.2d 916, 923 (S.D. 1992) (“Determining whether a statutory purpose is public or private is pretty much a matter of policy and wisdom for the legislature. In making such a decision it is vested with a large discretion with which courts should not interfere unless its action is clearly evasive.” (quoting *Clem v. City of Yankton*, 160 N.W.2d 125, 131 (S.D. 1968))).

162. *Id.*

163. 35 Va. (8 Leigh) 120 (1837).

164. *Id.* at 133–36.



local ordinance authorizing the city tax collector to seize the property of residents who refused to pay the tax was valid.<sup>165</sup>

A number of other early cases addressed governmental power to delegate the authority to levy taxes for public purposes. *Sharpless v. Mayor of Philadelphia*<sup>166</sup> involved the subscription of railway stock.<sup>167</sup> While the court in *Sharpless* upheld the legislation authorizing the purchase of railroad company shares, Chief Justice Jeremiah S. Black found that if the facts involved a taking of private property for private use, then such a taking would be unconstitutional.<sup>168</sup>

The first appearance of the public purpose doctrine in the U.S. Supreme Court was in *Loan Ass'n v. Topeka*<sup>169</sup> in 1874.<sup>170</sup> In that case, the local government used tax revenue to pay interest on bonds sold to support the development of an ironworks manufacturing company.<sup>171</sup> The intent was to increase bridge construction.<sup>172</sup> A financial company that had bought the bonds sued when the city failed to make interest payments.<sup>173</sup> The Court held the bond issuance impermissible because the city had not established a public purpose in extending the city's credit.<sup>174</sup> The Court's opinion did suggest that expenditures not reliant on levying a tax might be permissible.<sup>175</sup> This distinction places in contrast project revenue bonds, funded through

165. *Id.*

166. 21 Pa. 147 (1853).

167. *See generally id.*

168. *See id.* at 167; Waldron, *supra* note 143, at 90 ("While it would be 'palpably unconstitutional' to take private property for private use, [Justice] Black could discover 'no taking at all' in the present case." (quoting *Sharpless*, 21 Pa. at 167 (opinion of Black, C.J.))).

169. 87 U.S. (20 Wall.) 655 (1874).

170. *Id.* at 664. In Justice Samuel Freeman Miller's opinion:

To lay with one hand the power of the government on the property of the citizen, and with the other to bestow it upon favored individuals to aid private enterprises and build up private fortunes, is nonetheless a robbery because it is done under the forms of law and is called taxation. This is not legislation. It is a decree under legislative forms.

*Id.* Note that Justice Miller's opinion in *Loan Ass'n* was not necessarily motivated by some high-minded concept of free market economics. In the *Slaughterhouse Cases*, 83 U.S. (16 Wall.) 36 (1873) the year before, Justice Miller's majority opinion upheld a Louisiana law that granted a twenty-five-year monopoly to a private business to maintain slaughterhouses in and around New Orleans.

171. *Loan Ass'n*, 87 U.S. (20 Wall.) at 656 ("The bonds on their face purported to be payable to the King Wrought-Iron Bridge Manufacturing and Iron-Works Company, of Topeka, to aid and encourage that company in establishing and operating bridge shops . . .").

172. *Id.* (noting that the intent was "to encourage that company in its design of establishing a manufactory of iron bridges in that city").

173. *Id.* at 656-57 (describing the tax assessed to pay the bonds and the action brought for payment on the bonds).

174. *Id.* at 664.

175. *Id.* at 659 ("If these municipal corporations . . . have a fund or other property out of which they can pay the debts which they contract, without resort to taxation, it may be within the power of the legislature of the State to authorize them to use it in aid of projects strictly private . . .").

project fees, and general obligation bonds, which states may pay for using tax revenue.<sup>176</sup>

State courts, where most litigation related to the public purpose doctrine originates, quickly applied *Loan Ass'n's* limits on taxation for private purposes.<sup>177</sup> However, the public purpose doctrine was never a total limitation on legislative actions.<sup>178</sup> Nevertheless, state and local governments largely avoided the limits set by *Loan Ass'n* with non-tax, alternative financing arrangements.<sup>179</sup> Further, on principle, courts are increasingly restrained in their efforts to invalidate programs approved by legislatures.

Judicial restraint has led to mixed results and no clear rules. Cases involving taxation for the purposes of marketing or promoting agricultural products, for example, are often decided based on how economically important judges determine a particular product to be. Maine's highest court was willing to uphold a potato tax to support farming because potato production is significant to the state's economy.<sup>180</sup> But a similar tax on apples in West Virginia was rejected since apple production is only an incidental part of that state's economy.<sup>181</sup>

State court decisions largely rest on legislative findings associated with the given subsidy program.<sup>182</sup> In *State ex rel. Ohio County Commission v. Samol*,<sup>183</sup> a 1980 case before the Supreme Court of Appeals of West Virginia, for instance, the court relied on legislative findings to uphold a state law authorizing counties and cities to issue bonds for commercial real estate projects.<sup>184</sup> General legislative findings supporting the spending of public

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176. Gold, *supra* note 28, at 204 (distinguishing general obligation bonds that are backed by full faith and credit from project revenue bonds that are not).

177. See, e.g., *Weismer v. Village of Douglas*, 64 N.Y. 91, 103 (1876) (“[T]hese are not the direct and immediate public uses and purpose to which money taken by tax may be directed.”). In another example, in *People v. Westchester County National Bank of Peekskill*, New York's highest court invalidated a county tax used to fund a payment to veterans of the First World War. See 132 N.E. 241, 247 (N.Y. 1921).

178. See Briffault, *supra* note 31, at 912 (“The public purpose requirement was never a complete bar to government financial assistance to the private sector.”).

179. See *supra* Part I.A.

180. See *State v. F. H. Vahlsing, Inc.*, 88 A.2d 144, 150 (Me. 1952) (“[W]e must so hold where the industry for the benefit of which the tax is levied is as important and as basic as is the potato industry to the State of Maine which imposes the tax.”). “What justifies the tax is that the money expended for the promotion of the potato industry is not primarily expended for the benefit of those individuals engaged therein but for the benefit of the people as a whole . . .” *Id.*

181. See *Lingamfelter v. Brown*, 52 S.E.2d 687, 693–94 (W. Va. 1949) (“[T]he growing and moving of commercial apples . . . is not an enterprise or undertaking of such size as to impress it with a public interest. . . . [T]he monetary returns from such business are . . . not sufficient to characterize that business as one of the principal commercial or agricultural enterprises of the State . . .”).

182. See, e.g., *State ex rel. Ohio Cty. Comm'n v. Samol*, 275 S.E.2d 2, 4 (W. Va. 1980).

183. 275 S.E.2d 2 (W. Va. 1980).

184. *Id.* at 4 (“Section 2 thereof declares as a matter of legislative finding that the lack of employment and business opportunities in many areas of this state has created a critically adverse condition; that the development of new commercial, industrial and manufacturing

funds for a private purpose seem sufficient for courts to avoid invalidating a state law.<sup>185</sup>

Analysis of twenty years of case law reveals that state courts are unlikely to find government programs illegal based on the public purpose doctrine.<sup>186</sup> The scholarly discussion about the public purpose doctrine has focused on its toothlessness.<sup>187</sup> However, the common law alone was not the only legal tool used to reign in government spending on economic development activity.

State constitutional amendments followed the development of the public purpose doctrine. Many states in the first half of the 1880s adopted constitutional prohibitions on state support for private companies. In certain instances, state constitutional amendments were designed to limit local government support for railroads.<sup>188</sup>

Scholars argue that such provisions prevent states and cities from engaging in much of the economic development activity that takes place today.<sup>189</sup> Federal courts are reluctant to overturn the decisions of state courts that are political in nature once state court judges have sanctioned state and local legislative activities.<sup>190</sup>

In the background is the broadening of the meaning of public purpose, which was discussed in *Kelo v. City of New London*.<sup>191</sup> Although the backlash to the *Kelo* decision led to state constitutional amendments limiting the ability of states to condemn property through eminent domain,<sup>192</sup> the

plants is essential to relieve such condition . . . ." (quoting *State ex rel. Cty. Court v. Kemp*, 151 S.E.2d 680, 683 (W. Va. 1966))).

185. Note the legislative findings discussed in the Washington State tax preference for the aerospace industry. *See generally* S. 5952, 63d Leg., 3d Spec. Sess. (Wash. 2013) (enacted).

186. *See* Libgober, *supra* note 32, at 23 (arguing that based on case study research from 1994 to 2014 courts are almost guaranteed not to limit a legislative action based on a public purpose challenge).

187. *See, e.g.*, Briffault, *supra* note 31, at 909. As Briffault points out, the lack of enforcement of the public purpose doctrine and its constitutional counterparts demonstrates the difficulties inherent in enforcing state constitutions. *Id.*

188. Gold, *supra* note 28, at 209.

189. *See, e.g.*, Tew, *supra* note 76, at 172.

190. The Guarantee Clause of the Fourth Amendment to the U.S. Constitution states that "The United States shall guarantee to every State . . . a Republican Form of Government . . ." U.S. CONST. amend. IV, § 4. Courts have interpreted the Guarantee Clause to find nonjusticiable issues of a political nature; nonetheless, scholars argue that courts can decide matters falling under the Guarantee Clause. *See, e.g.*, Erwin Chemerinsky, *Cases Under the Guarantee Clause Should Be Justiciable*, 65 COLO. L. REV. 849, 851–52 (1994). In the takings context, Justice Sandra Day O'Connor noted the Court's deference to legislative decisions about what constitutes a public purpose. *See Kelo v. City of New London*, 545 U.S. 469, 499 (2005) (O'Connor, J., dissenting) ("[W]e emphasized the importance of deferring to legislative judgments about public purpose."); *see also* *Berman v. Parker*, 348 U.S. 26, 32 (1954) ("The legislature, not the judiciary, is the main guardian of the public needs to be served by social legislation.").

191. 545 U.S. 469 (2005).

192. *See, e.g.*, Ilya Somin, *The Limits of Backlash: Assessing the Political Response to Kelo*, 93 MINN. L. REV. 2100, 2102 (2009) ("The *Kelo* backlash probably resulted in more new state legislation than any other Supreme Court decision in history.").

often weak enforcement of existing state constitutional prohibitions in support for private companies is perhaps instructive.<sup>193</sup>

The push and pull of constitutional limitation versus deregulation is significant. Proponents of constitutional interpretation through a deregulatory lens view competition among neighboring states as a guiding principle. If, for instance, a number of Southern states permitted local governments to support private manufacturing through the construction of a new plant, then why should Florida not permit it as well?<sup>194</sup>

Judicial interpretation of constitutional limits on subsidies for private industry can be separated from the interpretation of whether there is a public purpose.<sup>195</sup> Step one is to establish a public purpose. Assuming a court can find a public purpose, step two is to evaluate whether the particular bond issue (in the case of industrial development bonds) constitutes the city pledging its credit. If the city is not pledging its credit, for instance in the case of a bond that is a private activity bond as opposed to a general obligation bond, then the activity should not be prohibited by the constitution.<sup>196</sup>

#### *B. Existing Proposals for Substantive and Procedural Constraints*

Scholars have not fully addressed the government's substantive and procedural challenges in constraining economic development activity. Substantively, the public purpose doctrine fails because of judicial inability to craft doctrinal constraints that limit state and local spending.<sup>197</sup> Specifically, the doctrine lacks a clear substantive definition of a public purpose. Much of the public purpose litigation relates to the government's ability to levy taxes to support particular economic activities.<sup>198</sup> Public purpose litigation illustrates the challenges courts have faced in crafting clear doctrinal constraints.

It might seem attractive to entirely outlaw state and local government spending outside of public infrastructure improvement. This is the purest and simplest limit. However, it is unlikely that courts would exert such constraints on their own without some galvanizing facts. The political pressure to redistribute wealth in order to claim credit for attracting and retaining employers is very powerful.<sup>199</sup> As a result, such a total ban seems unlikely in the near term.

Another proposal focuses on analyzing state and local agency professionals under agency law rather than contract law.<sup>200</sup> This forces

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193. See Libgober, *supra* note 32, at 7.

194. See Tew, *supra* note 76, at 174.

195. See *id.* at 173.

196. *Id.*

197. See Rubin, *supra* note 36, at 1346 (“Yet, the significance of [disastrous public aid to railroads] and the evils that gave rise to it have been lost on present judiciaries who find a public purpose in almost any proposed government expenditure.”).

198. See, e.g., Waldron, *supra* note 143, at 1.

199. See JENSEN & MALESKY, *supra* note 48, at 227.

200. See Libgober, *supra* note 32, at 55.

courts to apply an agency standard—which looks at whether the agent acted in the public’s interest—instead of a contractual one.<sup>201</sup> Applying an agency law approach offers a wealth of case law and analysis for courts to draw on in interpreting job-buying cases.<sup>202</sup> Another proposal argues for the increased role of the attorney general in constraining spending by the legislature.<sup>203</sup>

Another argument proposes that Congress should ban state and local incentives to businesses and should impose federal tax on such incentives to discourage them.<sup>204</sup> This proposal, articulated by Arthur Rolnick, is a “stick” approach to limiting spending.<sup>205</sup> Other tax regimes, like the federal, state, and local tools available to preserve affordable housing created through the LIHTC, offer carrots as well.<sup>206</sup> Rolnick’s suggestion to tax private companies for public incentives bears merit. Crafting appropriate language to capture potentially harmful spending would require much care.

Reforms at the federal level seem necessary given the pervasive nature of state and local spending on private businesses. Any reform effort that does not include federal action is liable to face piecemeal implementation. In Part IV, this Article will revisit federal reforms and detail the next steps in regulating job-buying.

Fundamentally, any reform needs to involve cooperation among state and local lawmakers. On the cooperation theme, David Reiss has suggested that cities sharing similar population sizes should cooperate in agreeing not to compete with one another for particular companies.<sup>207</sup> This proposal is an innovative twist on efforts to stop incentive border wars across state lines. Kansas City is a well-known hot spot in this war.<sup>208</sup> Recently, Missouri adopted legislation that would prevent the issuance of tax incentives to lure companies from adjoining counties in Kansas.<sup>209</sup> On August 13, 2019,

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201. *Id.* at 6.

202. *Id.*

203. Recently, the New Jersey attorney general has announced an investigation into that state’s economic development spending. *See* Munoz, *supra* note 35 (“Attorney General Gurbir Grewal . . . said his office would see if any civil or criminal laws were violated by companies receiving tax breaks and if so, ‘seek the recovery of those funds.’”).

204. Arthur J. Rolnick & Melvin L. Burstein, *Congress Should End the Economic War Among the States*, FED. RES. BANK MINNEAPOLIS (Jan. 1, 1995), <https://www.minneapolisfed.org/publications/annual-reports/congress-should-end-the-economic-war-among-the-states#f3> [<https://perma.cc/W5Q6-WJ4A>].

205. *See id.*

206. *See* Weiss, *supra* note 52, at 562.

207. David Reiss, *The Hunger Games: Amazon Edition*, N.Y.L.J. (Nov. 21, 2018, 2:25 PM), <https://www.law.com/newyorklawjournal/2018/11/21/the-hunger-games-amazon-edition/> [<https://perma.cc/6T97-5AZR>] (“A mutually beneficial and more economically rational approach would be for certain tiers of cities to commit to not compete against each other with direct subsidies to companies seeking to locate a new facility within their borders.”).

208. *See Episode 699: Why Did the Job Cross the Road?*, *supra* note 10.

209. S. 182, 100th Gen. Assemb., 1st Reg. Sess. (Mo. 2019) (enacted); *see also* *Missouri Offers Truce to Kansas in Business Incentive Battle*, AP NEWS (May 17, 2019), <https://www.apnews.com/f275b4faf8dd47df893674a96c584bf3> [<https://perma.cc/EAK5-UQHT>].

Missouri Governor Mike Parson and Kansas Governor Laura Kelly signed an agreement to end the use of tax incentives to attract companies across state boundaries.<sup>210</sup>

Cooperation agreements to limit business incentives might follow the lead of compacts or other collective agreements.<sup>211</sup> For example, states and cities could agree to refrain from issuing business location incentives if a certain threshold of states, cities, or populations opt in.

In 2016, the Louisiana Governor John Bel Edwards shifted veto power over industrial tax exemptions from the state to localities.<sup>212</sup> Once the East Baton Rouge Parish School exercised its newfound power to veto an ExxonMobil project, however, state legislators introduced five bills to strip the local veto right in favor of a state appointed commission.<sup>213</sup> This battle illustrates the tensions present between states and cities in legislating local conduct.

Others have argued for the European Union model that treats business subsidies as export subsidies, which, if beyond a certain size, are deemed illegal.<sup>214</sup> The European Union can force the company to repay subsidies if they exceed the allotted amount.<sup>215</sup>

In addition to the specific targets articulated above, there are guiding principles that state and local elected officials should consider when incentivizing private business. These include: clawbacks (recapturing incentives if businesses fail to fulfill the incentives' requirements); disclosure (outlining what information businesses are required to submit to both justify the subsidy and to support the transfer of the subsidy in practice); and transparency (ensuring that the information disclosed is shared broadly with the public).

One can imagine an economic impact statement being required, much the way an environmental impact statement (EIS) is required for certain types of developments. Typically, an EIS is required when commercial developers seek land use approval or other approval to build from the government. Governments issue handbooks on when EISs are necessary and how to draft them if they are.<sup>216</sup>

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210. See Kevin Hardy, 'Sometimes Common Sense Does Prevail.' *Missouri, Kansas Celebrate End of Border War*, KAN. CITY STAR (Aug. 14, 2019), <https://www.kansascity.com/news/business/article233725152.html> [<https://perma.cc/5BTZ-CUQV>].

211. Fifteen states have adopted legislation for a national popular election of the president. "Agreement Among the States to Elect the President by National Popular Vote," NAT'L POPULAR VOTE (May 1, 2019), <https://www.nationalpopularvote.com/sites/default/files/1-pager-npv-v184-2019-5-1.pdf> [<https://perma.cc/H85Y-QNPG>].

212. Mark Ballard, *Multiple Bills Changing Industrial Tax Breaks Making Their Way Through Legislature*, ADVOCATE (Apr. 30, 2019, 3:36 PM), [https://www.theadvocate.com/baton\\_rouge/news/politics/legislature/article\\_99850102-6b87-11e9-a747-07d24eb0aeed.html](https://www.theadvocate.com/baton_rouge/news/politics/legislature/article_99850102-6b87-11e9-a747-07d24eb0aeed.html) [<https://perma.cc/2TYU-DK4J>].

213. *Id.*

214. See generally Adinda Sinnavee, *How the EU Manages Subsidy Competition*, in REINING IN THE COMPETITION FOR CAPITAL 87 (Ann Markusen ed., 2007).

215. *Id.*

216. See, e.g., DIV. OF ENVTL. PERMITS, N.Y. ST. DEP'T OF ENVTL. CONSERVATION, THE SEQR HANDBOOK: FOURTH EDITION 2019 (2019) (draft), [https://www.dec.ny.gov/docs/permits\\_ej\\_operations\\_pdf/dseqrhandbook.pdf](https://www.dec.ny.gov/docs/permits_ej_operations_pdf/dseqrhandbook.pdf) [<https://perma.cc/8HNF-9TUE>]. For a

Recently, cities and counties have required community impact reports before proposed development projects are approved.<sup>217</sup> Typical community impact report ordinances are triggered by developments above a certain square footage threshold.<sup>218</sup> Community impact reports require a developer to disclose financial information related to the development.<sup>219</sup> Typical requirements include the financial effect of the development on the city's potential revenue, the number of jobs created by the project, and its impact on affordable housing.<sup>220</sup>

Market-based critics of a community economic impact statement will likely be wary of additional regulation of development. They also will point out that such regulation will simply drive development across a local border to a neighboring town. These are valid criticisms. Therefore, such regulation would be more effective if imposed on a county- or state-wide basis. That would require all developers in a county or state to follow the same rules.

On the disclosure front, a community economic impact statement would focus attention on the specific information that would (1) justify the public investment and (2) ensure that the public was protected through updates.

From a transparency perspective, there is a lack of public information about private economic development activity supported by state and local governments. Timothy J. Bartik and others have called for additional research and study of the available data.<sup>221</sup> Some datasets, like the Good Jobs First "megadeals" dataset<sup>222</sup> and a similar one focused on New York,<sup>223</sup> are recent attempts to aggregate and report the amount and breadth of these subsidies. In the rush to keep states and cities competitive, government programs may obfuscate the subsidy process.<sup>224</sup> Efforts need to be taken to include transparency in all efforts to support private economic development activity.

Dale F. Rubin has argued that the solution is to have a nonprofit organization dole out economic development subsidies.<sup>225</sup> Since nonprofits are mission-based organizations, they are more likely to guarantee a public purpose.<sup>226</sup> The trouble with this proposal is that it has been used in some cases and the nonprofit model has not changed how states and cities subsidize private actors. The MEDC, for instance, is a Michigan nonprofit that has

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discussion of the environmental impact review process, see generally *Ordonez v. City of New York*, No. 450100/2018, 2018 N.Y. Misc. LEXIS 3002 (N.Y. Sup. Ct. July 11, 2018).

217. *See id.* (citing a 2001 Evanston, Wyoming resolution).

218. *See, e.g.*, Petaluma City Council Res. 2008-189 N.C.S. (Cal. 2008) (enacted).

219. *See id.*

220. *See id.*

221. *See* BARTIK, *supra* note 14, at 117–18.

222. *See generally* MATTERA ET AL., *supra* note 1.

223. Masako Melissa Hirsch et al., *New York State Subsidy Tracker: Tracking the State's Growing Portfolio of Business Subsidies*, PROPUBLICA (Mar. 27, 2017), <https://projects.propublica.org/subsidies> [<https://perma.cc/Y4WS-GAEK>].

224. *See supra* Part I.B.

225. Rubin, *supra* note 36, at 1340–41.

226. *See id.*

authority from the state legislature to subsidize private businesses.<sup>227</sup> The MEDC's nonprofit status has not stopped the state from incentivizing private businesses at its fiscal peril.<sup>228</sup>

This Article rejects the notion that substantive judicial interpretation of public purpose can constrain state and city legislatures. The doctrinal and constitutional inquiries are simply too muddled. Further, such substantive decisions should not necessarily be left to the courts. Legislators, as representatives accountable to the people, ought to have some flexibility to determine what is in the interest of the public. However, that flexibility is not absolute. It should not devolve into folly. State courts, in particular, ought to play a role in reviewing failed efforts to grow and maintain jobs, such as in the case of the Washington State tax incentive program for the aerospace industry, as well as others.

### III. A TWO-STEP REVERSE AUCTION AND CLAWBACK PROPOSAL

If lawmakers are buying jobs, then they should follow certain norms in government purchasing. This Part draws from this scholarly conversation about government contracting to explore how government can distribute economic development subsidies more fairly. It presents a novel two-step reverse auction and clawback solution for economic development activity procurement that builds on public law principles like transparency, openness, and accountability.

This Part draws on existing legal academic literature on government contracting. Specifically, it places economic development activity squarely within government contracting practices. Economic development activity contracting is a more troublesome type of contracting because it requires the government to seek private actors to do something for third parties—in this case, hire them.

#### *A. Two-Step Proposal to Ensure Fair Distribution of Public Funds*

##### 1. Where Does the Money Come From?: Revenue vs. General Obligation

Today, most economic development activity occurs through government-issued revenue bonds as opposed to general obligation bonds.<sup>229</sup> Interest and principal payments on revenue bonds are paid through a stream of revenue, like lease payments, fees, hotel taxes, or similar items. A private entity, rather than the state or locality, is the obligor of the debt.

The federal government supports revenue bonds in a number of ways. Notably, the interest on revenue bonds is tax-exempt. Thus, when a state or local government sells revenue bonds on the financial markets, the government passes the tax exemption through to the debt holder, such as the

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227. See Michigan Economic Growth Authority Act, MICH. COMP. LAWS § 207.801 (2019).

228. See Livengood et al., *supra* note 22.

229. See *supra* Part I.



company or developer receiving the proceeds of the bond, and ultimately to investors.

Congress limits how much tax-exempt debt can be issued for private activities as well as the types of projects that can access exempt debt.<sup>230</sup> Certain types of projects have no limit to the amount of debt that can be issued. These types include airports, docks and wharves, government-owned solid waste disposal facilities, and qualified veterans' mortgages.<sup>231</sup> On the other hand, debt issued for qualified tax-exempt organizations, such as hospitals, is capped.<sup>232</sup> In fact, over 65 percent of private activity bonds in 2015 went to constructing hospital facilities and other properties owned by tax-exempt entities—this amounted to over \$67 billion.<sup>233</sup>

It is also important to know that for capped projects, states were limited in 2018 to \$37.5 billion in debt.<sup>234</sup> For large states like California, Texas, Florida, and New York, this worked out to \$4.2 billion, \$3 billion, \$2.2 billion, and \$2.1 billion respectively.<sup>235</sup>

Here, a state or local legislature could budget a particular amount of private activity bond proceeds for capped and uncapped activities for private economic development. Legislatures could publish a budgeted amount of funds to inform companies that they can bid to access them.

## 2. Step One: The Reverse Auction

Instead of assuming that business location incentives are legitimate, we ought to first question why and under what circumstances such incentives ought to be extended to private companies. Economists might argue that such incentives should be extended only during periods of economic downturn, and they should be broadly available to private companies rather than tailored to particular industries. Moreover, given the Amazon example, there are frequent auctions from competing jurisdictions to lure the same companies.

In spite of fiscal crises,<sup>236</sup> some academic economic research indicates that location-based incentives are useful to attract businesses.<sup>237</sup> However, the cost of attracting new businesses or jobs can be great. One study estimated the cost of attracting a new business to a federal “empowerment zone” at around \$19 million per business.<sup>238</sup> While state and local lawmakers may want to create new businesses, they should want to do so in the least costly

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230. See MAGUIRE & HUGHES, *supra* note 75, at 2.

231. *Id.* at 11.

232. *Id.* at 14.

233. *Id.* at 14–15 (The sum of the percentage of qualified hospital facilities and qualified section 501(c)(3) non-hospitals exceeded 65 percent in 2015.).

234. *Id.* at 12.

235. *Id.* at 17–18.

236. See *supra* Part I.C.

237. See Andrew Hanson & Shawn Rohlin, *Do Location-Based Tax Incentives Attract New Business Establishments?*, 51 J. REGIONAL SCI. 427, 429 (2011).

238. *Id.* at 428.

way possible. To do this, officials must focus on auction design, monitoring, and review.

Already, the government uses auctions to sell goods and services that it otherwise would need to set a price for.<sup>239</sup> Auctioning is frequently used in the private sector too. For example, online advertising providers host auctions to determine what ads will appear to a given user.<sup>240</sup> The reverse auction, conceptually, is closely aligned with the notion of an auction. Instead of the award going to the highest bidder, in a reverse auction, it goes to the lowest.

Readers who have recently flown on a commercial airline will likely be familiar with the reverse auction process. On flights with oversold seats, airlines will ask passengers, frequently at a check-in kiosk or via an app, to bid on a voucher for future air travel. In November 2017, United Airlines announced that customers could select a compensation bid amount and be placed on a list of potential volunteers willing to give up their seats. The airline advised customers that, if needed, it would select volunteers to be compensated starting with the lowest bidding customers.<sup>241</sup> The advisory highlighted ways that customers can bid for compensation to fly at a later date.<sup>242</sup>

The academic literature on reverse auctions focuses largely, and unsurprisingly, on procurement and marketing.<sup>243</sup> Sandy D. Jap concentrates on the importance of maintaining relationships in online reverse auctions in the procurement context.<sup>244</sup> From an efficiency perspective, Jap discusses the ability of an online reverse auction to reduce weeks of bidding and document processing to a process that can occur in the span of hours.<sup>245</sup>

A reverse auction is a mechanism for arriving at the lowest price buyers are willing to pay, rather than the greatest as in a traditional auction, for a fixed amount of goods or services. In an attempt to resist convention, Google used a reverse auction in its initial public stock offering.<sup>246</sup> The initial price for a single share was set at the lowest price that all shares would be sold following a bidding process.<sup>247</sup>

Given a reverse auction's potential advantages, states and cities ought to consider how such an approach may rationalize the subsidy allocation process when attempting to influence business-location decisions.

A state or local agency could implement a reverse auction following the legislature's and executive's budget allocation. The agency would issue a public notice of available funding. There would be a deadline for companies

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239. See POSNER & WEYL, *supra* note 42, at 50.

240. See, e.g., *About the Ad Auction*, *supra* note 42.

241. See The Hub Team, *supra* note 45.

242. *Id.*

243. See, e.g., Jap, *supra* note 42, at 146.

244. *Id.*

245. See Sandy D. Jap, *Online Reverse Auctions: Issues, Themes, and Prospects for the Future*, 30 J. ACAD. MARKETING SCI. 506, 509 (2002).

246. See Sherman, *supra* note 43, at 629–30.

247. *Id.*

to inform the agency of plans to use the subsidy and a disclosure of how much subsidy would be needed per job, either created or retained. Upon allocating all of the budget, the agency would award the lowest amount of subsidy per job.

Elected representatives would still largely decide the first principles regarding why and whether business incentives should be offered. Through this public process, elected officials would be able to hold hearings, consider different perspectives, and decide which metrics would be most important. For instance, lawmakers might enact a state residency requirement for any new jobs.<sup>248</sup>

On the other hand, lawmakers might be concerned that new jobs will go to workers already employed, and this might cause them to leave their current jobs in search of some other factor, such as better pay, work conditions, or commutes. This could lead lawmakers to avoid a state residency requirement. Whatever the particular metrics or values, having the reverse auction design begin at the lawmaking step has the political appeal of involving some expression of state or local values, however they are expressed.

Also, the lawmaking process allows additional metrics and expert perspectives to be included in the auction design process. Several metrics are articulated in the literature about business location incentives. They include: (1) frontloading subsidies in the early years after a business location decision, (2) including services like job training in addition to money, (3) making the subsidies non-refundable (i.e., the state or locality does not need to pay out the subsidy in cash), and (4) favoring high-skilled industries over retail.<sup>249</sup>

Assuming a legislative body decides that it is legitimate to fund business incentives for a particular industry—perhaps health care or technology given geographic proximity to hospitals and schools—and a set allocation of funds, it is still necessary to examine how large companies would be able to game the system in deciding between multiple jurisdictions. For companies bidding in multiple jurisdictions, business incentives simply reduce taxes on larger employers while existing businesses pay at a higher tax level. Solutions to addressing this problem could lie in the collective agreements discussed in Part II.B. For instance, states and cities of a certain size could agree not to compete with each other for large employers of a certain size.

Another challenge is the competition within a jurisdiction to redistribute economic development funds from very productive areas to less productive ones. For example, the rise of highly successful metropolitan regions in some cases has led to demands from areas with lower productivity for more government funding.<sup>250</sup> In such cases, states may work to more evenly

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248. For an example of such a state residency requirement, see the case of Intel in New Mexico. *See Sams, supra* note 102.

249. *See infra* Part III.A.5.

250. Michael Cox, *The Rise of Populism and the Crisis of Globalisation: Brexit, Trump, and Beyond*, 28 IRISH STUD. INT'L AFF. 9, 9–17 (2017); Richard C. Schragger, *Federalism*,

disperse capital. To make a reverse auction business-incentive scheme politically acceptable to lawmakers from less economically productive areas, a compensation scheme or a community benefits agreement approach could be implemented to balance out the demands to redistribute scarce economic development funds.

Payments to towns and landowners in exchange for accepting undesirable land uses are not unprecedented. New York's largest landfills, for instance, are located in the Finger Lakes region of New York.<sup>251</sup> Through a host of community benefits agreements pertaining to one landfill in Seneca Falls, the town receives 5.5 percent of the landfill's revenue.<sup>252</sup> Paying less developed parts of a state in exchange for permitting a state to engage in a reverse auction for business incentives would make such a program palatable statewide.

### 3. Step Two: The Clawback Provision

Next, once all available subsidies are allocated, the agency would contract with the successful bidders. This is where recapture mechanisms linked to a specific number of created or retained jobs would be included in the awarded contracts. This allows governments to claw back funds spent on companies that accept subsidies but still reduce their workforces. Governmental subsidy administrators may deter company flight based on particular community economic needs.

If businesses fail to successfully do what they say they will do, the contractual remedy will be available to claw back incentives and cancel contracts.<sup>253</sup> States and cities have used clawbacks effectively to recapture incentive payments when companies do not deliver the jobs numbers that they promise.<sup>254</sup> In exchange for government subsidies, Intel regularly reports its progress in hiring and retaining workers to the New Mexico government.<sup>255</sup> Under a clawback regime, the business must repay some of the original incentive if it shuts or lets employees go during a specific

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*Metropolitanism, and the Problem of States*, 105 VA. L. REV. (forthcoming 2019) (manuscript at 7), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3384084](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3384084) [<https://perma.cc/SYM3-UCDT>].

251. Steve Orr, *Investigation: NYC Dumping More Garbage Than Ever in Finger Lakes Area*, DEMOCRAT & CHRON. (July 6, 2018, 1:34 PM), <https://www.democratandchronicle.com/story/news/2018/07/06/finger-lakes-landfills-booming-monroe-ontario-and-seneca-counties-residents-angry/754940002/> [<https://perma.cc/KE99-Z5AK>].

252. David L. Shaw, *Current Landfill Benefit Agreement Explained*, FINGER LAKES TIMES (July 24, 2016), [https://www.fltimes.com/news/current-landfill-benefit-agreement-explained/article\\_22aa5a44-5142-11e6-b320-7f9175b863fd.html](https://www.fltimes.com/news/current-landfill-benefit-agreement-explained/article_22aa5a44-5142-11e6-b320-7f9175b863fd.html) [<https://perma.cc/NP29-7GNF>].

253. BARTIK, *supra* note 14, at 83.

254. The Intel incentive project is an example of this. *See, e.g.*, Sams, *supra* note 102.

255. *Id.*

timeframe.<sup>256</sup> The contract phase is an opportunity for agencies to influence private companies through public law norms.<sup>257</sup>

#### 4. Oversight: Role of the Public

Once contracts are in place, monitoring is primarily up to the agencies. Agencies tasked with monitoring economic development programs face challenges in ensuring that programs function.<sup>258</sup> Typically, agencies that are spread thin lack the resources for monitoring. Legislatures and executives would need to consider the monitoring responsibilities of agencies when allocating funds for incentive programs. The public could assist with the monitoring process.

The intended beneficiaries of economic development incentive programs are constituent workers who risk losing their current jobs and those who may be hired in the future. If constituents are included in the monitoring process through a private right of action, the monitoring agency can share the burden of oversight. The contract drafting process can include a third-party beneficiary provision allowing administrative challenges if the company fails to deliver on its contractual obligations.

#### 5. Additional Concerns: Setting Further Metrics

Beyond the two-step proposal, there are additional concerns that agencies ought to consider when subsidizing private economic development. Once the legislature allocates funds, the government, through the legislature or a state or local administrative agency, sets metrics. The metrics determine how and upon what conditions the bidding company will receive subsidies. Now, as shown through the Washington State aerospace subsidy example and others, the task of setting metrics for economic development is not easy. Further, because economic development activities are not well studied, it can be challenging to set meaningful metrics.

Currently, metrics for economic development programs focus on somewhat obvious numbers, like the number of full-time equivalent jobs created or retained, the investment in capital equipment or real property, and the spending on local infrastructure. In some cases, such as Washington State's, the focus on keeping a particular production program failed to keep and grow jobs due to the inclusion of robot manufacturing.<sup>259</sup> There are several additional metrics to consider when evaluating whether a program is likely to be successful.

Economic data indicates that economic subsidies are most effective when implemented in particular ways. These include: (1) when subsidies are front-

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256. BARTIK, *supra* note 14, at 83.

257. See Jody Freeman, *The Contracting State*, 28 FLA. ST. U. L. REV. 155, 156 (2000).

258. See, e.g., PHILIP JAMES DEGNAN, OFFICE OF THE STATE COMPTROLLER, NEW JERSEY ECONOMIC DEVELOPMENT AUTHORITY: A PERFORMANCE AUDIT OF SELECTED STATE TAX INCENTIVE PROGRAMS 9 (2019), [https://nj.gov/comptroller/news/docs/eda\\_final\\_report.pdf](https://nj.gov/comptroller/news/docs/eda_final_report.pdf) [<https://perma.cc/Z3QP-DEXE>].

259. See *supra* note 6.

loaded in the first couple years after a move or expansion; (2) when subsidies are focused on certain high-skilled positions (subsidies targeting job expansion in low-wage industries like retail tend to be less effective); (3) when tax credits are nonrefundable and unlimited in terms of budget allocation; and (4) when subsidies are geared towards services like customized job training rather than cash.<sup>260</sup> As Bartik points out, the lack of data available to study private economic development makes disclosure requirements in law even more critical.<sup>261</sup>

*a. Front-Load Subsidies in Early Years*

When designing metrics for the type of subsidy to offer a private business, state and local agencies and legislatures should front-load the subsidy in the first few years of a business's relocation or expansion. The reasons for front-loading incentives are easy to understand. Businesses assign a discount rate to future years' incentives.<sup>262</sup> Incentives offered in the first year, or the first five years, are worth much more than those offered in future years.<sup>263</sup>

A bright spot is that the data indicates that, as of 2015, front-loading is already happening.<sup>264</sup> Moving forward, states and cities should set metrics that focus on the incentive's first, or first five, years. These first five years are most important for businesses in assessing where to move or keep jobs. Incentives offered seven to ten years into the future tend not to impact business decision-making.<sup>265</sup> Plus, incentives extended into the future can be very costly to the government and public.

*b. High-Skilled vs. Retail Jobs*

A significant criticism of government incentives to private businesses is that the inducements further low-wage, low-skill, part-time employment.<sup>266</sup> Recent scholarship touts programs that place focus on career-oriented jobs in manufacturing and other skilled sectors.<sup>267</sup> Luckily, the data suggests that the incentive programs of states and cities are focused more on manufacturing and other skilled areas of work, including technology.<sup>268</sup>

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260. BARTIK, *supra* note 14, at 117.

261. *Id.* at 7.

262. *Id.* at 83.

263. When building a new facility, for instance, a sales tax exemption on the materials and equipment used to construct and fit out that factory is very valuable. *Id.* As Bartik points out, "it seems doubtful that the property tax abatement provided in year 11 will do much to drive business location decisions. Yet long-term property tax abatements may lead to future fiscal problems for local schools and governments." *Id.*

264. *Id.* at 81.

265. *Id.*

266. *See generally* MATTERA ET AL., *supra* note 1.

267. *See, e.g.*, BRUCE KATZ & JEREMY NOWAK, THE NEW LOCALISM: HOW CITIES CAN THRIVE IN THE AGE OF POPULISM 63 (2017) (highlighting the development of a robotics industry centered around local institutions of higher education).

268. *See* BARTIK, *supra* note 14, at 6.

There are two ways to ensure that incentives produce growth across an economy. The first is to define the industries that can use the incentive program.<sup>269</sup> The second is to assign a multiplier to the jobs produced or retained by the incentive.<sup>270</sup>

Congress specifies industries and projects through the private activity bond program.<sup>271</sup> This approach has given Congress tools to respond to natural disasters and economic collapse.<sup>272</sup> Such a response could be adopted in the proposed bidding program and allow for legislatures to prioritize certain projects based on responses to current needs.

Using economic multipliers seems attractive. Both the Texas and Florida deal-closing funds require an economic multiplier of 6:1 and 5:1 respectively.<sup>273</sup> The theory underlying this policy is that an economic multiplier accounts for the recycling of dollars within a community.<sup>274</sup> Simply put, it is difficult to manage this. It largely will be up to agencies reviewing bids to ensure that the economic multiples are delivered.

*c. Make Tax Subsidies Nonrefundable and  
Set Caps on Amount of Incentive*

Currently, many tax-incentive programs are uncapped. A related issue is that subsidies are frequently refundable.<sup>275</sup> Bartik observes that incentives are refundable to businesses too frequently, meaning that the state or city has to pay the business cash.<sup>276</sup>

For example, in the case of the Tesla Gigafactory project, Tesla receives refundable tax credits.<sup>277</sup> If Tesla were to apply for a tax refund, the state would pay the credits, valued at \$1.4 billion, in cash.<sup>278</sup> This payment, which would further deplete public coffers, would do nothing to address the affordable housing crisis and overcrowded schools in Nevada.<sup>279</sup> Without eliminating the refundability of tax incentives, and setting a reasonable cap on the total amount of subsidy, the public is not protected.

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269. *See id.* at 117.

270. *See, e.g.*, FLA. STAT. § 228.1088 (2018); TEX. GOV'T CODE ANN. § 481.078 (West 2019).

271. *See generally* FIPPINGER, *supra* note 72.

272. *See* MAGUIRE & HUGHES, *supra* note 75, at 9.

273. *See* FLA. STAT. § 228.1088 (2018); TEX. GOV'T CODE ANN. § 481.078 (West 2019).

274. *See, e.g.*, Press Release, Greg Abbott, Tex. Governor, Governor Abbott Announces New Infosys Limited Expansion in Richardson (Nov. 13, 2018), <https://gov.texas.gov/news/post/governor-abbott-announces-new-infosys-limited-expansion-in-richardson> [<https://perma.cc/C8AQ-QT3Q>].

275. *See* BARTIK, *supra* note 14, at 117. Specific examples discussed above include the MEGA program in Michigan and the New York Empire Zone program, among others. *See supra* notes 23, 113.

276. BARTIK, *supra* note 14, at 117.

277. *See Tesla, Nevada Agree on Finalized Incentive Agreement*, *supra* note 96.

278. Rory Carroll, *All Humanity Has Left the Area: Paying for Tesla's Gigafactory*, *GUARDIAN* (July 3, 2018, 6:00 AM), <https://www.theguardian.com/cities/2018/jul/03/all-humanity-has-left-the-area-the-cities-paying-for-tesla-gigafactory> [<https://perma.cc/VGQ5-88PD>].

279. *Id.*

As a threshold matter, a bidding program imposes a cap by allocating only a limited amount of funds. The refund matter can be addressed through drafting the incentive program. Thus, these two issues can be addressed.

*d. Include Services like Job Training in Addition to Cash*

While the data is not conclusive, states spend very little on job training programs.<sup>280</sup> Some data suggests that services like job training can be more cost-effective than cash incentives to businesses.<sup>281</sup> Job training may not be effective in addressing the displacement of existing small businesses.<sup>282</sup> Some states like New York<sup>283</sup> and Maine<sup>284</sup> are taking steps to either pay for higher education or cover the cost of student loan debt, thus easing some pain points related to financing an education. But it is likely that more can be done.

*B. The “Publicization” of Private Economic Development*

Lawmakers using legislation to increase economic development activity do not always clearly further public goals and purposes. This creates both challenges and opportunities.<sup>285</sup> As Jody Freeman suggests, there are public

280. BARTIK, *supra* note 14, at 117.

281. See generally Harry J. Holzer et al., *Are Training Subsidies for Firms Effective?: The Michigan Experience*, 46 *INDUST. & LAB. REL. REV.* 625 (1993); Kevin Hollenbeck, *Is There a Role for Public Support of Incumbent Worker On-the-Job Training?* (Upjohn Inst., Working Paper No. 08-138, 2008), [https://research.upjohn.org/cgi/viewcontent.cgi?article=1155&context=up\\_workingpapers](https://research.upjohn.org/cgi/viewcontent.cgi?article=1155&context=up_workingpapers) [<https://perma.cc/F23D-J4BM>]; William H. Hoyt et al., *Business Incentives and Employment: What Incentives Work and Where?* (Inst. for Federalism & Intergovernmental Relations, Working Paper No. 2009-02, 2008).

282. *Mayor Bloomberg and Deputy Mayor Lieber Announce New Partnerships to Provide Advanced Auto-Related Training Programs at No Cost to Willets Point Workforce*, NYC.GOV (Nov. 1, 2008), <https://www1.nyc.gov/office-of-the-mayor/news/430-08/mayor-bloomberg-deputy-mayor-lieber-new-partnerships-provide-advanced-auto-related> [<https://perma.cc/V2WJ-8WD5>].

283. *Tuition-Free Degree Program: The Excelsior Scholarship*, N.Y. ST., <https://www.ny.gov/programs/tuition-free-degree-program-excelsior-scholarship> [<https://perma.cc/WRR3-382K>] (last visited Aug. 22, 2019).

284. *The Opportunity Maine Tax Credit Reimburses Student Loan Payments for College Graduates Who Live and Work in Maine*, LIVE & WORK IN ME., <https://www.liveandworkinmaine.com/opportunity-maine/> [<https://perma.cc/4KM8-KMNP>] (last visited Aug. 22, 2019).

285. To be clear, government has a variety of mechanisms available to it to buy or create jobs. Government can hire workers to perform a variety of tasks. Historically, this was the course taken by the FDR administration during the Depression. See, e.g., Patrick Kline & Enrico Moretti, *Local Economic Development, Agglomeration Economies, and the Big Push: 100 Years of Evidence from the Tennessee Valley Authority*, 129 *Q.J. ECON.* 275 (2014); *A History of Innovation*, N.Y. ST.: N.Y. POWER AUTHORITY, <https://www.nypa.gov/about/timeline> [<https://perma.cc/85W8-NW3F>] (last visited Aug. 22, 2019). Government works projects, such as the St. Lawrence-Franklin D. Roosevelt Power Project on the border of Canada and New York State and the Wilson Dam in the Tennessee Valley were job creation programs.



law tools available, such as budgeting, regulating, and contracting, to bring private actors under the frame of public law norms.<sup>286</sup>

There are several reasons for lawmakers, public policy advocates, and legal scholars to focus on the publicization of private economic development activity. The government's current doctrinal and constitutional constraints on private economic development activity are wholly inadequate to constrain spending in this area.<sup>287</sup> A lack of constraints on government spending for private economic development activity is correlated with higher state and local debt.<sup>288</sup>

Freeman identifies three factors that should be considered when deciding on whether a function should involve publicization<sup>289</sup>: "(1) the relative precision with which a service can be specified and the extent of the provider's discretion, (2) the potential impact on the consumer, and (3) the government's motivation for privatization."<sup>290</sup> Arguments for services being publicized are strongest where "services are highly contentious, value-laden, and hard to specify, and when providers enjoy significant discretion; when services affect vulnerable populations with few exit options and little political clout; and/or when the motivation for privatization is explicitly ideological or clearly corrupt."<sup>291</sup>

The case for the publicization of private economic development activity is strong. First, as demonstrated in the examples above, private economic development activity is very difficult to specify with particularity, and companies have sole discretion in most cases about how to develop their businesses, including the decision to leave after receiving public funds.<sup>292</sup> Second, workers and their families are increasingly immobile, while companies and their capital are very mobile.<sup>293</sup> Workers are vulnerable and, especially in postindustrial urban and rural areas, have few job alternatives.<sup>294</sup> Third, political self-preservation typically motivates public support of private economic development activity.<sup>295</sup> This motivation alone is suspect.

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286. Jody Freeman, *Extending Public Law Norms Through Privatization*, 116 HARV. L. REV. 1285, 1285 (2003).

287. *See supra* Part II.

288. *See* Libgober, *supra* note 32, at 5.

289. *See* Freeman, *supra* note 286, at 1291.

290. *Id.*

291. *Id.*

292. *See* Scott, *supra* note 3 (describing the Boeing tax subsidy example where the company took significant subsidies to construct a new facility and still cut almost 17,500 jobs in Washington State).

293. *See* Schragger, *supra* note 38, at 495.

294. *Id.* at 494.

295. *See generally* Monnat & Brown, *supra* note 115.

## IV. APPLYING THE TWO-STEP PROPOSAL

A. *The Washington State Example Revisited*

The failure of the Washington State aerospace subsidy extension was largely because the statutory metrics focused on the development of a new airplane wing manufacturing line.<sup>296</sup> The number of jobs for human workers was not included in the statute.<sup>297</sup> Boeing could keep the tax credit because it constructed the wing manufacturing plant.<sup>298</sup> However, Boeing reduced its workforce in Washington State by developing robotics and scaling back workers on other manufacturing lines.

How would the proposed two-step bidding process address the Washington State failure? It would do so in three ways. First, through the budgeting process, legislators would have a public opportunity to debate the amount of funds that should be set aside for private companies. Second, through the setting of metrics, legislators, the executive branch, and constituents could address the issue of maintaining jobs and not just new real property investment. Finally, through the contracting process, the agency charged with selection and monitoring could ensure that the company was competitive in its incentives proposal. Through budgeting, regulation, and contracting, public law norms could improve the incentive allocation process.

A company as large and important as Boeing would certainly have influence at each stage. However, the procedural bidding process would shed light on a currently opaque subsidization process. For instance, information about the actual benefits of the Boeing tax deal was not evident until the company was required to report its 2015 tax savings.<sup>299</sup> The current process did not even set jobs targets.<sup>300</sup> It is possible that other employers could have made better use of the public funds—whether they be new employers from out of state, neighboring tech employers in Seattle, or small businesses.<sup>301</sup>

There would be a public conversation about the amount of the subsidy extended in a bidding process. The Washington State aerospace subsidy is the largest state transfer to private industry in U.S. history.<sup>302</sup> A bidding process, in which other companies would have had the chance to meet or beat Boeing's hiring plans, would have improved an otherwise broken process.

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296. See S. 5952, 63d Leg., 3d Spec. Sess. § 1(3) (Wash. 2013) (enacted).

297. *Id.*

298. See Gates, *supra* note 6.

299. Jim Brunner, *For First Time, Boeing Reveals State Tax Breaks: \$305 Million in 2015*, SEATTLE TIMES (Apr. 29, 2016), <https://www.seattletimes.com/seattle-news/politics/boeing-saved-305-million-last-year-from-state-tax-breaks/> [<https://perma.cc/W3GK-BEGV>].

300. See Wash. S. 5952 § 1(3).

301. Small businesses typically do not get the same attention and financial support from state and local government—but they create most of the new jobs. *Frequently Asked Questions*, U.S. SMALL BUS. ADMIN. OFF. ADVOC. (June 2016), [https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016\\_WEB.pdf](https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf) [<https://perma.cc/NTK9-R84U>].

302. See MATTERA ET AL., *supra* note 1, at 19.

The agency required to oversee the economic development could share its monitoring obligations by including a private right of action to third-party beneficiaries. It is true that there were challenges to the Boeing subsidy, but the challenges were not in state court and not based on the company's failure to meet its obligations under contract.<sup>303</sup> As demonstrated above, court challenges based on public purpose doctrine are unlikely to be successful.<sup>304</sup> But a group of intended beneficiaries bringing a claim based on contract law is another story. Individual workers, groups of workers, or unions representing workers could have brought a contract law claim when Boeing reduced jobs following its receipt of subsidy dollars.<sup>305</sup>

### B. Florida and Texas

A bidding regime would slightly alter deal-closing funds in Florida, Texas, and other states that have similar programs. The main change under the bidding regime is that states like Florida and Texas would accept company bids rather than approach the companies directly. The state legislature would still approve an annual (or biennial) budget for the program. The governor's office, or monitoring agency, would still set regulation through use of metrics. This is currently done through an enabling statute. Individual company contracts and monitoring would continue with a few changes. States could compare information about subsidies extended on a per job basis. Small- and medium-sized companies could compete more easily with larger employers when seeking government funds.

Table 1, below, compares the Washington State aerospace extension, the Florida Quick Action Closing Fund, the Texas Enterprise Fund, and the two-step company bidding proposal.

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303. The World Trade Organization (WTO) found the tax breaks illegal. *Boeing Illegally Given \$5.7 Billion in Tax Breaks by Washington State, WTO Rules*, L.A. TIMES (Nov. 28, 2016, 9:00 AM), <https://www.latimes.com/business/la-fi-boeing-wto-20161128-story.html> [<https://perma.cc/7FY2-3XSV>]. However, the WTO ruling was overturned on appeal. Tim Hopher & Tom Miles, *WTO Reverses Boeing 777X Tax Credit Ruling in Blow to EU*, REUTERS (Sept. 4, 2017, 10:13 AM), <https://www.reuters.com/article/us-wto-aircraft/wto-reverses-boeing-777x-tax-credit-ruling-in-blow-to-eu-idUSKCN1BF1PC> [<https://perma.cc/NRD5-CS8Z>].

304. See generally Briffault, *supra* note 31.

305. In the Boeing example, machinists narrowly agreed to a new contract around the 777X following the passage of the tax deal. See Wilson, *supra* note 2.

Table 1: WA,<sup>306</sup> FL,<sup>307</sup> and TX<sup>308</sup> Compared to Two-Step Company Bidding Proposal

	WA	FL	TX	Two-Step Proposal
<b>Amount</b>	\$9 billion	\$225.5 million	\$516 million	Set by state or local legislature
<b>Metrics</b>	New facility	5:1	6:1	Multiplier, jobs, and other metrics
<b>Target</b>	Aerospace sector	Companies planning to relocate	Companies planning to relocate	Set by legislature or agency
<b>Oversight</b>	Boeing must site aerospace manufacturing program in state to keep receiving funds	Companies must meet job targets to keep receiving funds	Companies must meet job targets to keep receiving funds	Company reporting and subject to claw back if jobs targets not met

### C. Capture, Gaming, and Other Arguments Against the Proposal

Any administrative process is subject to capture by regulators, especially one involving public spending for private business development. Of course, companies will make efforts to game the system by using metrics to win bids. There are a number of ways to guard against this.

The two-step bid proposal itself works to break down the capture process: if companies are not made offers by the government but are instead required to bid, then the process will likely be more efficient from the start. Companies seeking to bid can also influence the metric setting, or regulation, and the contracting parts of the process. However, there are checks throughout the bidding process with public processes at each step, public norms of accountability, transparency, and rationality, as well as the principle of due process.

Certain requirements ought to limit gaming, which would lower its likelihood. For instance, a company must demonstrate that it is considering a location in another jurisdiction to bid on the available funds.

Another way to address the issue of gaming is through blind bidding. By blind bidding, companies would bid for the least amount of government

306. See S. 5952, 63d Leg., 3d Spec. Sess. (Wash. 2013) (enacted). See generally MATTERA ET AL., *supra* note 1.

307. See FLA. STAT. § 288.1088 (2018); Dixon, *supra* note 111.

308. See TEX. GOV'T CODE ANN. § 481.078 (West 2019); *Texas Enterprise Fund (TEF) as of June 30, 2019*, TEX. ECON. DEV., [https://gov.texas.gov/uploads/files/business/TEF\\_Listing\\_as\\_of\\_6.30.19.pdf](https://gov.texas.gov/uploads/files/business/TEF_Listing_as_of_6.30.19.pdf) [<https://perma.cc/X58J-58GV>] (last visited Aug. 22, 2019).

subsidy per job without disclosing the company name.<sup>309</sup> Such a program embraces what Mariana Mazzucato has described as government support for business; the state stepping in with needed investment the private sector will not provide.<sup>310</sup> While some large employers might make themselves known by certain types of proposals, as is likely with any public process, all qualifying projects could be entered into a lottery and selected at random.

It is unlikely that this process would entirely eliminate public outrage towards employers that accept subsidies and then leave. However, a bidding mechanism with an opportunity to address recapture of a subsidy for company nonperformance affords a clear opportunity for the government and community to address outrage around employers fleeing after receiving subsidies.

There is a chance that critics still will cry foul about a process involving government agencies where the names of bidders are disclosed. Two solutions to this problem stick out: first, names of bidders could be sealed; and second, once eligible bids are assessed, subsidies could be allocated at random based on funds available.

#### D. Federal Reforms, Next Steps

The focus of some reform suggestions center on efforts at the federal level.<sup>311</sup> While they are important, and certainly could go a long way to improving the efforts states and cities make to encourage local private economic development, they are outside the scope of this Article.

Furthermore, if anything, the floodgates are wide open for federal-level regulation. With the Treasury's recent proposed regulations of the Opportunity Zone program,<sup>312</sup> investors will be able to avoid capital gains on real estate invested for at least ten years in a specific area.<sup>313</sup> Maps of the Opportunity Zones have already been drawn.<sup>314</sup> One report has suggested

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309. By analogy the process would work like a company's initial public offering. See Sherman, *supra* note 43, at 629–30.

310. Mariana Mazzucato, *The Innovative State: Governments Should Make Markets, Not Just Fix Them*, FOREIGN AFF., Jan./Feb. 2015, at 61, 61.

311. Bipartisan efforts already have been made to curb the rampant subsidization of sports and entertainment stadiums and arenas through tax-exempt bond financing. See, e.g., Press Release, Cory Booker, U.S. Senator, Booker, Lankford Introduce Bipartisan Bill to End Federal Subsidies for Sports Stadiums (June 13, 2017), [https://www.booker.senate.gov/?p=press\\_release&id=612](https://www.booker.senate.gov/?p=press_release&id=612) [<https://perma.cc/8GY4-AHK7>]. Previously, the White House had zeroed out the budget for public financing for sports and entertainment facilities in the 2017 budget. DEP'T OF THE TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2017 REVENUE PROPOSALS 83 (2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf> [<https://perma.cc/S4HV-BMYJ>].

312. Investing in Qualified Opportunity Funds, 83 Fed. Reg. 54,279 (proposed Oct. 29, 2018) (to be codified at 26 C.F.R. pt. 1).

313. Micah W. Bloomfield et al., *Stroock's Take on the New 'Qualified Opportunity Zone' Guidance*, STROOCK (Oct. 19, 2018), <https://www.stroock.com/publications/stroocks-take-on-the-new-qualified-opportunity-zone-guidance> [<https://perma.cc/D6JT-8XS2>].

314. CDFI FUND, [https://www.cdfifund.gov/preparation/?config=config\\_nmtc.xml](https://www.cdfifund.gov/preparation/?config=config_nmtc.xml) [<https://perma.cc/DRH8-8CJE>] (last visited Aug. 22, 2019) (showing a national map of the qualified opportunity zone borders).

that the Treasury do the following to implement the Opportunity Zone tax credits appropriately, including: (1) target the right places using better data; (2) use appropriate financing, monitoring compliance, and mandating transparency; (3) guard against federal subsidy abuse; and (4) evaluate the program to ensure it achieves its goals.<sup>315</sup>

The author remains skeptical about the likelihood that state or federal courts will reinterpret the substance of the public purpose doctrine or the state constitutional prohibitions on gifts, loans, or extension of the government's credit for private business.<sup>316</sup> The Supreme Court took steps to further the public's understanding of what constitutes "public use,"<sup>317</sup> which is related to public purpose. Whether or not that will shift with the reconfiguration of the Court to a solid five conservative vote majority remains to be seen.

Were courts to adopt a more robust analysis of what constitutes a public purpose, there are some guides. There are a number of factors that courts can use to assess whether a project fits within a public purpose: (1) safety precautions of the project; (2) waste disposal plans; (3) traffic; (4) burden of increased population on existing government services; (5) availability of housing; and (6) psychological tensions caused by the project.<sup>318</sup> With the possible exception of the sixth factor, most of these factors certainly fit within a specific analysis that a court could engage in at a fact-finding stage to assess whether a public purpose exists. The difficulty, however, is perhaps in courts' reluctance to legislate. Courts tend to defer to legislatures, especially on social laws.<sup>319</sup> In other words, courts rely on the legislative check to curb such oversubsidization.

In a related area, courts are reluctant to overturn state and local government efforts to regulate development because of gentrification claims. One recent opinion on this topic, issued by a court in New York State, highlights this issue. In *Ordonez v. City of New York*,<sup>320</sup> a state court judge combined two separate challenges to zoning approvals brought by longtime residents of rent regulated housing in East Harlem and Brooklyn.<sup>321</sup> In both instances, residents challenged the city's analysis of the socioeconomic impact of zoning approvals on longtime, low-income renters.<sup>322</sup> In each case, city

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315. HILARY GELFOND & ADAM LOONEY, BROOKINGS INST., LEARNING FROM OPPORTUNITY ZONES: HOW TO IMPROVE PLACE-BASED POLICIES 1 (2018), [https://www.brookings.edu/wp-content/uploads/2018/10/Looney\\_Opportunity-Zones\\_final.pdf](https://www.brookings.edu/wp-content/uploads/2018/10/Looney_Opportunity-Zones_final.pdf) [<https://perma.cc/DNM9-Y4AV>].

316. See *supra* Part II.A.

317. See *Kelo v. City of New London*, 545 U.S. 469, 494 (2005) (O'Connor, J., dissenting) ("Under the banner of economic development, all private property is now vulnerable to being taken and transferred to another private owner, so long as it might be upgraded—*i.e.*, given to an owner who will use it in a way that the legislature deems more beneficial to the public—in the process.").

318. Comment, *supra* note 33, at 802.

319. See, e.g., *Berman v. Parker*, 348 U.S. 26, 32 (1954).

320. No. 450100/2018, 2018 N.Y. Misc. LEXIS 2911 (N.Y. Sup. Ct. July 11, 2018).

321. See generally *id.*

322. *Id.* at \*13.

officials followed environmental assessments guidelines in analyzing how zoning decisions would impact the various areas.<sup>323</sup>

Since the city followed the guidelines, the court would not overturn the city's final approval of each zoning application based on claims that new development would have significant harms on longtime residents.<sup>324</sup> Such a decision reveals the challenges that gentrification places on residents and the reality that state courts are likely to uphold state and local government agencies' decisions.

#### CONCLUSION

Courts and lawmakers have much to grapple with in constraining government support for private economic development activity. Studies demonstrate that the public purpose doctrine and state constitutional prohibitions are wholly inadequate at limiting the ability of state and local legislators to buy jobs for their constituents. This Article proposes an auction-based approach to rationalize the job-generation process.

Under this Article's proposed two-step auction process, disruptions to communities are likely. Few legal remedies are available to longtime residents at risk of displacement. But as areas grow and develop, there are perhaps opportunities for middle class families to return to areas, like urban cores, that they have fled. And revitalized job opportunities may allow poor families—especially in African American communities—to move into the middle class.

In light of this Article's discussion about state and local officials spending public funds to retain and attract employment, one wonders about the future of work and the government's role in transferring funds to workers. There are issues related to how governments ensure that workers have money to consume while also ensuring a healthy, dignified, and productive society. In engaging in job buying, lawmakers have adopted a supply-side, neoliberal belief that it is better to spend public funds to attempt to attract high paying jobs than to use public resources to expand direct payments to workers through social or economic programs.

More fundamentally, there is the question of what types of jobs governments can attract and how private sector employment will develop. A shift to a service-based economy and the robotization of certain manufacturing or dangerous work will continue to mean that the work that families relied on for generations will no longer exist. Workers must confront that reality. Governments already deal with displaced factories, the closure of which eliminates property tax, sales tax, and income tax revenue. Additional direct and indirect economic benefits occur through the injection of payroll into a local economy and the multiplier effect that occurs when workers eat at restaurants, shop at grocery stores, buy or rent homes, and consume local goods and services.

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323. *Id.* at \*12.

324. *Id.* at \*79.

The public policy imperative for lawmakers to buy jobs is unlikely to change. The force and power of constituents' need for work and income is so strong. Because it is unlikely that spending on private economic development will subside on its own, a legal constraint is necessary to check lawmakers. Because it has proven too difficult to substantively constrain spending, a procedural check is the more obvious solution. This Article has presented a two-step proposal. The first step involves a reverse-auction process to ensure the least amount of public subsidy is used per job. The second step is a clawback provision that allows the public to recapture subsidies should agreed-upon job targets not be achieved.

Some observers may argue that an auction approach unnecessarily complicates a simple negotiation process for businesses and governments to reach agreement on subsidy terms. A bid process, some may think, could chill private sector participation in job creation through new commercial real estate development. Even simpler, a jurisdiction that adopts such a process could drive businesses across city or state lines into an area with fewer regulations.

This criticism is certainly a fair one to consider. Government is frequently characterized—often deservedly—for moving too slow for the pace of business. However, in the reverse-auction scenario posed by this Article, the idea is to accomplish the dual goals of government inducing businesses to hire workers, grow operations, and spend money on office and plant facilities, while also checking potential overspending of scarce public funds.

A related criticism is that the possible programs legislated in the reverse-auction process could limit innovation. If the goal is to get companies to increase their innovativeness, having the strictures of government-imposed metrics could be too limiting. In the Boeing example, perhaps developing robot technology for airplane wing or fuselage manufacturing actually improves the process. A reformed, more restrictive bidding process could unnecessarily limit companies' ability to develop new manufacturing techniques and processes.

The answer likely lies somewhere in between. Lawmakers must consider what the government's role is in developing industry such that constituent employment remains fruitful and robust. Exploring the values involved in work—both financial and, in some cases, moral—ought to occur through debate among elected representatives. Courts likely are better left to determine the satisfactory compliance with procedural requirements than in making substantive decisions about how and when lawmakers can use public money to buy jobs.