
Economic Recovery Grant Program

CHAPTER 2

The Economic Recovery Grant program is the state's main program for job creation and retention. The program originated in 1984, following the recession of the early 1980s, and it operates in tandem with a similar federal program, the Small Cities Community Development Block Grant (CDBG). Both programs are administered by the Department of Trade and Economic Development (DTED) and are referred to collectively as the "Economic Recovery Fund." Since 1984, the two programs have loaned or provided grants of more than \$100 million to over 400 companies.

The Economic Recovery Grant program is the state's main program for job creation.

In this chapter we address the following questions:

- **Are the current criteria for reviewing and awarding grants under the Economic Recovery Grant program adequate? Does DTED attempt to determine what level of financial support is necessary for projects to proceed? How does the staff determine whether the project should receive a loan or a grant?**
- **How have program funds been used? What types of projects have been funded?**
- **What is the track record of the Economic Recovery Fund in creating and retaining jobs?**
- **What wages have been paid by the jobs created?**

We used a variety of methods to answer these questions. We interviewed department staff and other economic development professionals around the state. We also reviewed and collected data from the department's files for all projects funded between 1991 and 1995.¹ In addition, we interviewed 40 executives from companies that were assisted by loans or grants and verified companies' job creation claims by checking data on employment and wages as reported on companies' unemployment tax returns.

¹ An index of the projects is included as Appendix A.

PROGRAM DESCRIPTION

The Economic Recovery Fund finances "activities designed to create new employment, maintain existing employment, increase the local tax base, or otherwise increase economic activity in a community."² According to state rules, 51 percent of the jobs created must be filled by or made available to low or moderate income people.³ Businesses do not apply for assistance directly to the state; rather, local units of government apply to the state on the businesses' behalf. The maximum amount of money that may be awarded to any local government is \$500,000 per year. The state can provide assistance in the form of a grant, loan, or forgivable loan. A forgivable or deferred loan has a term and interest rate but the state waives principal and interest payments if the company meets its job creation and retention goals.⁴

The state has awarded over \$100 million through the Economic Recovery Fund since 1984.

Table 2.1 shows that state appropriations for the Economic Recovery Grant program for fiscal years 1984 through 1996 exceeded \$68 million. The state also spent \$35 million in federal funds for the Small Cities CDBG program since 1984.⁵

The Business Development and Finance Unit in the Department of Trade and Economic Development administers the Economic Recovery Fund. The unit consists of a supervisor and five senior loan officers and has a budget of about \$535,000 per year. The unit reviews grant and loan applications and oversees projects for which the department has awarded grants.⁶ DTED's organization chart is presented in Figure 2.1.

Although DTED administers both the federal and state programs under state rules, there are some important differences in how the two funds are administered. For example, all local units of government and recognized Indian tribal governments may apply for state funds, but cities and counties that receive CDBG funds directly from the federal government and Indian tribal governments are not eligible for federal funds through the Small Cities program. Also, federally funded construction projects are subject to labor and environmental standards that state pro-

2 This is the definition of economic development projects in *Minn. Rules*, Ch. 4300.0100, Subp. 6.

3 "Low and moderate income" means income which does not exceed 80 percent of the median income for the area, with adjustments made for smaller and larger families. *Minn. Rules*, Ch. 4300.0100, Subp. 13. The state median household income was \$33,682 in 1993; 80 percent of \$33,682 is \$26,946. (Median income is adjusted using the Consumer Price Index for All Urban Consumers (CPI-U). Source: U.S. Census, Current Population Reports, P60-188.)

4 For example, a business might receive a \$500,000 forgivable loan for the creation of 75 jobs that would allow half of the loan to be "forgiven" if the jobs are maintained for 5 years and the other half to be "forgiven" if the jobs are maintained for 10 years. Sometimes the state requires the business to repay the first \$100,000 to the local unit of government to capitalize a local revolving loan fund.

5 The 15 percent set aside for economic development grants is set by state rule *Minn. Rules*, Ch. 4300.2000, Subp. 2). The rest of the CDBG funding is allocated between single purpose and comprehensive grants. The Department of Trade and Economic Development is proposing to modify the rules to allow the commissioner to change the proportion of funding among the three types of grants if there is a shortage of fundable applications in any area.

6 An additional position is vacant, and a supervisor, who has other responsibilities, spends time working on the program.

Table 2.1: Economic Recovery Fund, 1984-1996

State Appropriations: FY 1984-1996		Federal Community Development Block Grant Funds: ^a FY 1984-1995	
FY 1984-1985	\$6,000,000	FY 1984	\$3,188,424
1986-1987	11,329,400	1985	3,190,482
1988-1989	11,329,400	1986	2,210,727
1990-1991	11,328,000	1987	2,663,193
1992-1993	11,034,000	1988	2,569,113
1994-1995	11,034,000	1989	2,224,120
1996	<u>6,017,000</u>	1990	2,172,183
		1991	2,910,447
		1992	3,171,404
		1993	3,294,852
		1994	3,655,443
		1995	<u>3,827,874</u>
TOTAL	\$68,071,800		\$35,078,262

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Department of Trade and Economic Development.

^aFederal fiscal year.

The 1995 Legislature modified the program.

jects are not required to meet. Finally, if federal funds finance a project, the local unit of government keeps the full amount of the grant upon repayment by the business. When a company repays a loan of state funds, the local government keeps only the first \$100,000 and the balance is repaid to the state. The local government uses the funds it retains from loan repayments to capitalize a local revolving loan fund. Repayments for state loans greater than \$100,000 are deposited in the state's General Fund.

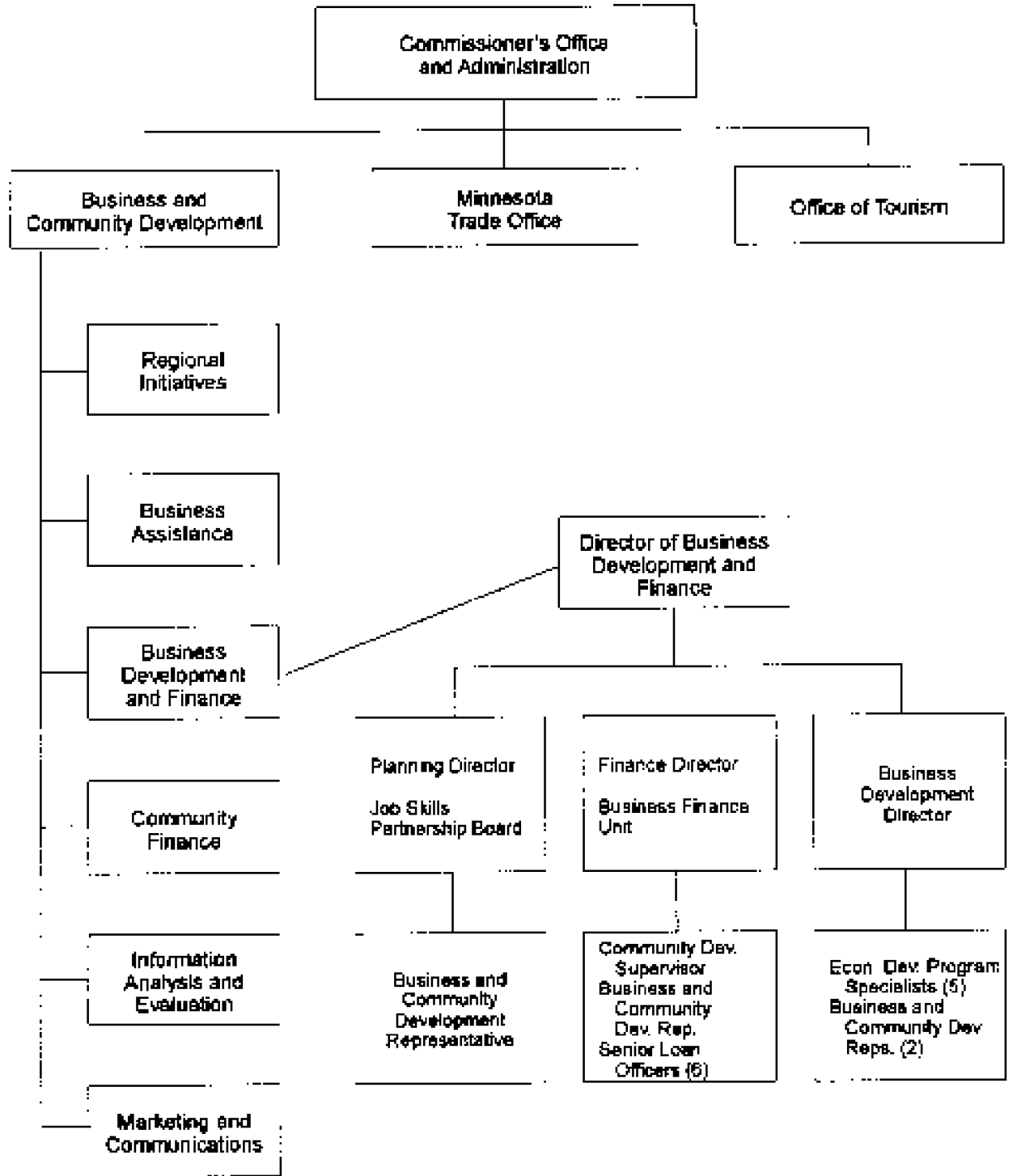
As we discuss later in this chapter, the 1995 Legislature modified the Economic Recovery Grant program in two important respects: first, it stipulated that projects cannot be funded if the only rationale is to attract an out-of-state business or to keep an in-state business from leaving the state unless there is evidence of excessive infrastructure costs or insufficient funding from other sources.⁷ Second, it required state and local government agencies that provide economic development assistance through grants or loans in excess of \$25,000 or tax increment financing to establish wage level and job creation goals and to report the results for each business assisted. Businesses that do not meet their job or wage goals are required to repay the assistance.⁸

It is not clear how this latter law will work in practice. For example, if a firm received a loan from the state and did not meet its job goals it is unclear what action DTED could take. However, the department already has implemented some procedures that might be able to accommodate the requirements of this law. DTED has

⁷ *Minn. Laws* (1995), Ch. 224, Section 55.

⁸ *Minn. Laws* (1995), Ch. 224, Section 58.

Figure 2.1: Department of Trade and Economic Development Organization Chart, July 1995



Source: Department of Trade and Economic Development.

DTED requires companies to report on job creation, wages, and benefits.

included provisions in recent grants and forgivable loans to recapture state assistance if job goals specified in the loan or grant agreements are not met.⁹ Since 1993, the department has required local units of government to provide wage and benefit information for the jobs created. DTED includes the job projections in the loan or grant agreement, but, until recently, has not included the projected wages. In 1995 the department started to include the wage goals in the grant or loan agreement and it will have to develop a process for monitoring whether wage as well as job creation goals are met.

GRANT CRITERIA AND APPROVAL PROCESS

Application Process

The Department of Trade and Economic Development uses a single application process, consisting of two parts, for several of its programs. The Part I application asks for information about a community's need for assistance and the project(s) for which the community is seeking funding, including cost estimates and potential impact. A contract manager reviews the application and refers it to the most appropriate department program. When a Part I application is referred to the Business Development and Finance Unit and the project appears to be one that will meet eligibility requirements for the Economic Recovery or Small Cities program, a loan officer contacts the applicant about completing a Part II application.

The Part II application seeks more detail about the proposed project, including a more exhaustive community need narrative. At this stage, the applicant describes the project activities, projected number and type of jobs to be created, and budget, including a list of actual or potential sources of funding and sources that have denied requests for funding. The applicant must provide assurance of compliance with state and federal requirements, provide a statement of support from the local unit of government, supply evidence of and minutes from a public hearing about the project, and submit extensive financial information about the company on whose behalf the funds are being requested. The department, community, and business negotiate the terms of the financial assistance.

In 1994, DTED loan officers completed approximately 60 in-person interviews with economic development specialists around the state to collect opinions on the program. Most respondents (60 percent) did not like the single application process. Some felt there should not be a Part I application and others thought the department should eliminate Part II. One applicant commented that the Part I should be a pre-application from the business, another that Part II should be program-specific.

⁹ The department is proposing legislation to formalize this repayment, or so called "clawback" provision.

Despite these complaints, we found nothing inherently wrong with the single application process. It allows DTED to obtain preliminary information about a proposed project and direct it to the most suitable program, with more detailed information submitted only for those projects that may be eligible.

We have some concerns about how companies apply for awards, and about how DTED and the companies negotiate the terms and type of award. The loan officers and the respondents to the in-person interviews also noted some of these concerns. First, we found that:

- **Since the beginning of the program in 1984, some businesses have gotten around the normal application and negotiation processes by directly approaching the Governor or the commissioner or deputy commissioner at DTED.**

The businesses still go through the mechanics of completing an application, but with an understanding of the amount and type of award they will receive assuming the application scores the minimum 400 points. Businesses circumventing the normal application process can create the appearance of political favoritism and prevent the loan officer from having input. A respondent to the department's in-person interviews voiced a related concern: sometimes the loan officer negotiates terms without the community's input. In our view, all participants have an interest in the type and terms of an award and should be included in the bargaining process. We also found:

- **The department does not have written criteria for determining the type of award to offer under different circumstances.**

Other than always funding improvements to public infrastructure (e.g., water and sewer systems or roads) with grants, there are no formal guidelines about what type of award to make. Though there are no official guidelines about when to offer loan forgiveness, a letter in the file of one business indicated that the department offers forgiveness "only in rare circumstances, such as when there is a real threat that the company may relocate all or a portion of its business to another state." The lack of criteria allows the type of award to be a negotiated item. It also may create a perception of preferential treatment for certain businesses, if businesses that do not need financial assistance receive grants and forgivable loans while those that are in greater need receive loans. In our opinion, DTED should adopt minimum standards that businesses must meet in order to receive grants or forgivable loans for purposes other than public infrastructure. The standards should be higher than those for businesses receiving loans, and all businesses should be held to the standards. We recommend that:

- **DTED should establish criteria that projects must meet before they will be considered for a grant or forgivable loan for purposes other than public infrastructure.**

These criteria could be part of the scoring process, and might include factors such as the number and type of jobs created and the wages and benefits provided, and

DTED should adopt clear minimum standards for forgivable loans and grants.

other factors that demonstrate that the projects are valuable to the state. The department notes that it is in the process of revising its scoring system for applications.

Evaluation and Scoring of Projects

Loan officers evaluate Part II applications to see that the proposed projects meet eligibility and financial thresholds. To be eligible, both state and federal projects must benefit low and moderate-income persons and meet two of three state objectives.¹⁰ The state objectives include: (1) creation or retention of permanent private sector jobs, (2) leverage of private investment, and (3) increase to the local tax base.¹¹ To provide a benefit to low and moderate-income (LMI) persons requires that "at least 51 percent of the jobs will be held by, or will be available to low- and moderate-income persons." The department has required that federally funded projects actually create jobs that are "held by" LMI persons, while state projects must only be "made available to" LMI persons. According to the state Economic Development Program Manual, "To make jobs available to LMI persons, the jobs created should not require specialized training other than that which will be provided by the employer."¹²

The department is proposing changes to the rules that would do several things: add a fourth state objective ("improved employment and economic opportunity for Minnesota citizens to create a reasonable standard of living"); eliminate the requirement that applicants for the state program have to meet federal objectives; and allow a varying percentage of federal CDBG funds to be used for economic development.

The loan officers do financial analyses of the companies by reviewing existing debt, credit reports, three years of historical financial statements, two years of projected financial statements, audits, personal financial statements of the owners if a personal guarantee is involved, aging of accounts receivable and payable, cost estimates, and business plans. The project must also meet certain financial thresholds: (1) all other financial sources must have been considered and found inappropriate, unavailable, or insufficient; (2) the business must be committed to completing the project according to the terms of the agreement; (3) letters of commitment must have been received from other financial sources; (4) the cash-flow needs to be sufficient to cover the proposed debt service; and (5) the business to be assisted must have a positive net worth.

¹⁰ Federal Community Development Block Grant money must be used for one of three federal objectives: to provide a benefit to low and moderate income persons, to prevent or eliminate slums or blight, or to alleviate urgent community development needs. In the case of economic development projects, the federal objective met is always to benefit low and moderate income persons. The state program has the same requirements because the Economic Recovery Grant statute requires the program to be administered according to the rules for the federal program.

¹¹ The state has required that the jobs are to be created within two years of the award, that at least one job be created for every \$20,000 of funds awarded, that at least one dollar of private funds be leveraged for every dollar of funding, or that there be a 50 percent increase in the value of the parcel of land that would be assisted.

¹² Economic Development Program, *Program Manual*, (St. Paul: Minnesota Department of Trade and Economic Development, October 1992), 6.

If a project meets the eligibility and financial thresholds, the loan officer evaluates the request for funding based on a 600 point scale: 400 points are based on community need, project impact, and the capacity of the applicant to complete the project; 200 points are based on financial feasibility. An application must score 400 points, with at least half the possible points obtained from each section, to be eligible for funding. Because the loan officers provide technical assistance to the applicants, projects that will not score 400 points do not submit Part II applications. A copy of the scoring sheet is included as Appendix B.

The application provides ample information about the financial health of a company and the soundness of the project. No review process can eliminate all possibility that weak projects will be funded, but as long as the information required by the department is being utilized by loan officers in a thorough and systematic way, we feel that application and review procedures are adequate.

Changes should be made to DTED's scoring system for grant and loan applications.

We noted several aspects of the Economic Development Score Sheet, however, that we think should be eliminated or revised. The current score sheet allows for too much subjective consideration (175 points) under the guise of an objective process. Subjectivity and consideration of individual circumstances are required to maintain flexibility of the program but should not be part of the scoring process.¹³ The scoring sheet also measures some of the same criteria more than once.¹⁴

We also question the appropriateness of the scale used for the demographic criteria (i.e., county unemployment rate, median income, and poverty rate). The department awards all or none of the possible points for each demographic criterion. Communities with demographic characteristics only slightly worse than the state median will score the same as very distressed communities, receiving all of the possible points. At the same time, because the metro area tends to set the state median for the demographic characteristics, it is difficult for metro area applicants to receive any points for demographics. Finally, while median income is used as an indicator of community need, it is not adjusted for the cost of living in the community.

Loan officers score project impact based on the number of jobs the business projects it will create and the amount of dollars requested per job to be created. We see two problems with this. First, DTED does not consider the wages, benefits, or type of jobs created in the scoring system.¹⁵ In our opinion, the scoring system should reflect that jobs providing higher wages and/or employee benefits are "worth more" to the state. Second, it is difficult for small companies, particularly

¹³ For example, a loan officer can check up to twenty items under "community and economic needs" and "beneficial results and tangible effects" and award up to 110 points based on the level of need. It is not clear how many items need to be checked to reflect the different levels of need. On three applications, 60 points (indicating moderate need) were awarded: one application had 6 items checked, one had 10, and one had 12. At the same time, an application with 9 items checked received 80 points (indicating substantial need).

¹⁴ Unemployment, job training for low-income persons, ratio of dollars requested to jobs created, amount of private investment, and increases in the local property tax base are measured more than once.

¹⁵ Loan officers do consider the type and wage level of jobs informally.

in the metro area, to be funded using this scoring system. It is difficult for smaller companies in the metro area to score 400 points because projects creating fewer than five jobs receive no points for job creation (regardless of the dollars requested per job), and because metro area applicants rarely receive points for demographic characteristics.

Some criteria do not differentiate between projects because the scores do not vary much across projects. Examples include: "Increase to the local tax base (in excess of 50 percent)," "Interest rate on grant funds over the term of the loan," and the score assigned under financial feasibility gap.

**Recently
requests have
exceeded
available funds.**

Until 1994, the amount of money available through the Economic Recovery Fund equalled or exceeded requests for funding, however, demand for the funds has increased in the last two years. The department has implemented a "pipeline" list -- projects that will be approved contingent on future appropriations. When there were sufficient funds the scoring system served as a minimum threshold and the department could fund all projects scoring at least 400 points. Since the department cannot fund all projects at the requested amount, the scoring system should mean something. However, the funding received by projects does not appear to bear a relationship to the points a project received. Instead, the department either negotiates with the businesses to determine how much money the business will receive or determines the amount of the award based on how much money remains to be lent.

We recommend:

- **DTED should revise its scoring system for the Economic Recovery Fund.**

In our opinion, the revised scoring sheet should eliminate subjective criteria and criteria that do not differentiate projects and it should consider the job type, wage, and benefit level. The scoring system should also consider demographic factors on some type of relative sliding scale basis.

The department should identify the characteristics of the community and the project that lend themselves to quantification and that are important for differentiating projects funded through this program and include them in a scoring system. The department should count each characteristic only once and should weight each characteristic to reflect its importance relative to others. The scoring system should reflect the value of the project so that projects with more points are understood to be "better" than projects with fewer points, other things being equal. The department also should consider developing different scoring systems for federal-versus state-funded projects. Different minimum point requirements might be appropriate for grants versus loans or infrastructure versus other projects. After projects have been scored, specific subjective criteria that have been determined to be important to the state should be considered, and those criteria, in combination with the projects' score, should be used to determine funding. DTED officials note that they are in the process of revising their application scoring process.

"GAP FINANCING" VERSUS "INCENTIVE FINANCING"

Another important issue is whether the Economic Recovery Grant program should provide assistance only to businesses that can demonstrate financial need, or whether it can be used as an incentive for business without a financial need to remain, relocate, or expand in Minnesota. The former strategy, known as "gap financing," was the clear preference expressed by the Legislature in 1995 when it modified the terms under which grants could be made. The Legislature stipulated that projects were to be evaluated based on the following conditions:

- (1) whether assistance is necessary to provide equity to business owners who do not have the capacity to invest in a project;
- (2) whether there is an inability to secure sufficient financing from other public or private sources at market interest rates or on favorable market terms;
- (3) whether assistance is necessary to attract out-of-state businesses or to retain existing businesses within the state;
- (4) whether there are excessive public infrastructure or improvement costs beyond the means of the affected community and private participants in the project.¹⁶

The statute also requires that the decision cannot be based on clause 3 alone. We believe the Legislature's intent was to target aid to businesses that faced a financing "gap." Indeed, several of DTED's program documents imply that a financial need must exist for projects to receive funding. For example, the Economic Development Program Manual states:

The program is not intended to substitute for conventional business financing or to be used in place of other more specialized state, federal, or local programs that may be better suited to specific project needs. Instead, grants from this program are intended to be used in situations in which a funding "gap" exists, and alternative sources of public and private financing are inadequate or unavailable.¹⁷

There has been a trend to award more grants and forgivable loans.

However, in our review of projects funded after 1991, we noted many projects where there was no evidence of financial need for the company assisted. Indeed, there has been a trend toward increasing funding for large companies, compared to the early years of the program, as well as an increasing trend toward awarding grants and forgivable loans as opposed to loans.

- **Even though the 1995 Legislature tried to limit "incentive financing," DTED has continued to award a number of "incentive" grants and loans.**

The department has given a liberal reading to clause 2 of the 1995 legislation, interpreting it to mean that a company being offered incentives by other states cannot otherwise secure sufficient financing "on favorable market terms." This interpretation has allowed DTED to make awards to firms that considered relocat-

¹⁶ 1995 Laws of Minnesota, Chapter 224, Section 55.

¹⁷ Economic Development Program, *Program Manual*, (St. Paul: Minnesota Department of Trade and Economic Development, October 1992), 1.

ing parts of their business in other states but were able to fund their project internally or through market financing.

Because of the seeming inconsistency between the statute and DTED's current practice, we recommend:

- **The Legislature should further clarify the goals and purpose of the program and provide clearer direction on whether it wants to allow “incentive financing.”**

The Legislature needs to provide clear direction on the program's purpose.

There are two aspects to this: first, deciding whether “incentive financing” should be included under the program, and, second, if “incentive financing” is permissible, under what rules should it be administered. The Legislature may 1) allow unrestricted incentive financing, 2) allow incentive financing under some circumstances, 3) prohibit “incentive financing” altogether (and strengthen the language in statute), or 4) provide for separate pools of money for the two types of financing, each with its own eligibility criteria.

If “incentive financing” is to be allowed, are there policies that could be adopted that would maximize the benefit to the state? We saw in Chapter 1 that there is general agreement that “incentive financing” does not create greater economic activity on the national level. Economists do agree that in some circumstances the state can play a role in alleviating market failures. There is also agreement that some sorts of state government investments for business make more sense than others. We were particularly impressed by the ideas of Mary Waits and Rick Heffernon:

Incentives for businesses can represent good public policy, but only if they meet certain conditions:

- Incentives should be used to accomplish clearly defined goals based on an overall economic development strategy, not simply to win bidding wars.
- Incentives should be subject to a rigorous cost-benefit analysis in both the short and long term.
- Incentives should be made contractual so that recipient businesses are held accountable for their promises and performances.¹⁸

Waits and Heffernon suggest the following guidelines for a state incentive policy:

- Link incentives to quality jobs and advancement opportunities, not simply numbers of jobs (e.g., company must pay higher than average wages for the industry in the county it is located).
- Encourage recipient companies locating in rural areas to fill a certain percentage of new jobs with local people.

¹⁸ Mary Waits and Rick Heffernon, “Forging Good Policy on Business Incentives,” *Economic Development Review*, Fall 1994, 21.

- Link incentives to company investments in technology and people. (e.g., company must meet a threshold of investments in property and/or worker training).
- Encourage recipient companies to offer health insurance to all employees.
- Insist that recipient companies have strong environmental management and compliance records.
- Target companies that are important to key clusters that provide clear economic benefits.
- Make public investments such as customized job training or infrastructure development the priority offer to companies because these programs will continue to provide community wide benefits even if a company moves or shuts down.
- Minimize the need for special deals by ensuring the state has strong economic foundations (e.g., competitive tax and regulatory policies, advanced infrastructure, educated work force).
- Use tax based incentives (tax breaks) as a last resort, or for purposes of catalyzing business investments in productivity.
- Avoid legislation aimed at specific companies, unless the opportunity is unique. Make new incentive programs broad based in application (i.e., applicable to a broad spectrum of existing and new businesses).
- Analyze the costs and benefits of all incentive packages to ensure the best decision possible. Specify an organization to conduct the analysis and, if possible, an economic model to be used.
- Set performance standards with clawback provisions to hold companies that receive incentive benefits (especially those that are taxed based) accountable for their end of the bargain.

The Legislature might consider restricting "incentive financing" to infrastructure or job training projects.

As we saw earlier, there is a great deal of competition between states for expanding companies. In light of this reality, the Legislature might consider allowing incentive financing in some circumstances, but restricting the funding to infrastructure or job training purposes. In that way, the funding would provide an investment in the state's physical or human capital while providing a less direct subsidy to the benefiting company. This option will probably restrict DTED's ability to assist some businesses in some cases.

A task force in North Carolina developed guidelines that one writer called "the nation's most advanced set of guidelines for awarding location incentives to corporations" that might be instructive for Minnesota.¹⁹ Applications to North Carolina's

¹⁹ Peirce, Neal R., "State of the States: The Gold in Them Thar States," *National Journal*, November 11, 1995, 2820.

Industrial Recruitment Competitive Fund, which provides "incentive financing" to businesses, are scored on four main dimensions: job quality, industry quality, economic impact, and local impact. The task force identified three aspects of job quality: the wage the firm will be paying relative to the average manufacturing wage in North Carolina; a measure of job stability of the firm's industry; and a measure of job safety of the firm's industry. The task force also developed measures of industry quality intended to reflect the use of technology and the productivity of the firm's industry. The economic impact is measured by the number of jobs, the number of spin off jobs, and the spin off earnings. Local impact is measured by wages and the county unemployment rate compared to the state average. All criteria are scored on a scale and each criterion is weighted to reflect its importance to the state. In addition, companies are judged on environmental impact and financial stability.

North Carolina recognizes that no rating system can account for all contingencies and also identified four factors that could result in special consideration: (1) the area the firm would expand in has experienced a sudden and severe economic dislocation; (2) the firm will create an unusually high number of jobs; (3) the firm agrees to negotiate special hiring arrangements for low income people; or (4) the firm will bring an exceptional technology or is a recognized industry leader.

ECONOMIC RECOVERY FUND ACTIVITY: FISCAL YEARS 1991 THROUGH 1995

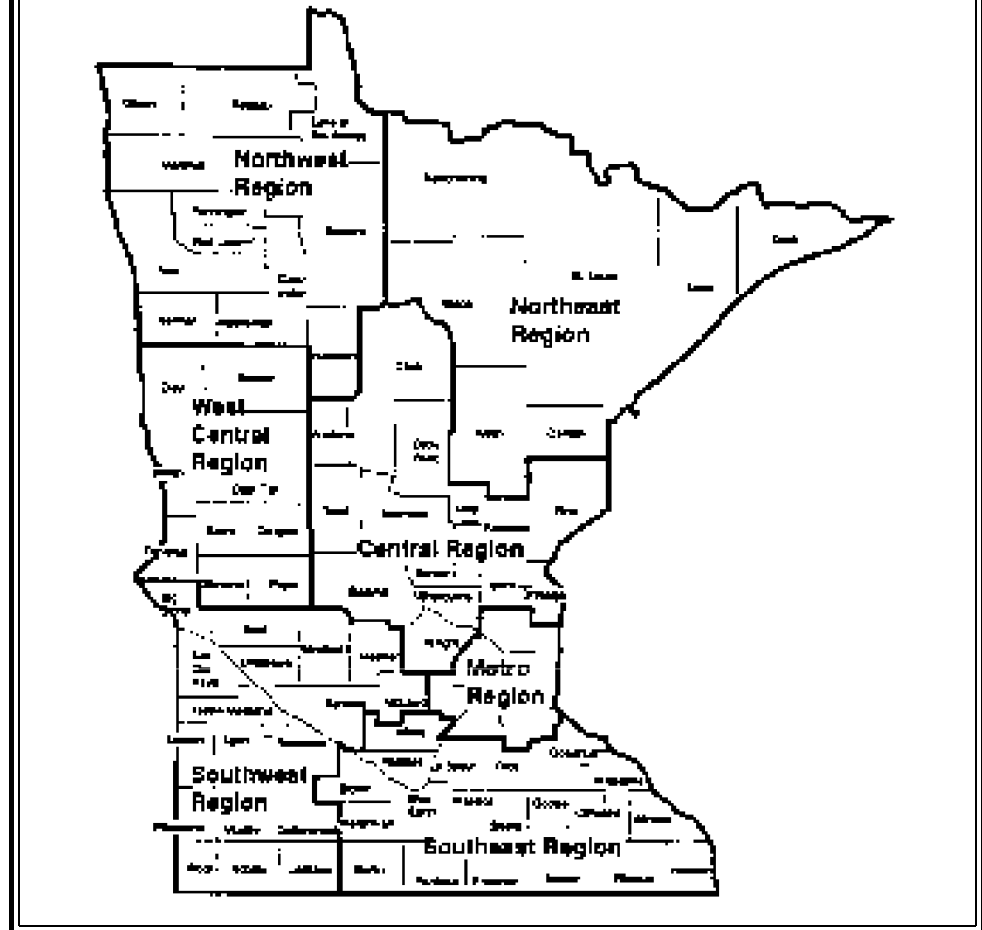
We reviewed grants and loans made to businesses through the Economic Recovery Grant and Small Cities programs in fiscal years 1991 through 1995. During this time, the Department of Trade and Economic Development approved 185 projects for funding.²⁰ Nine of the projects were never funded either because they never occurred or because the company chose not to draw down the loan funds they were awarded. Thirteen companies received more than one grant or loan during the five year period. The 176 projects which were funded helped 158 companies.

Figure 2.2 shows the department's seven economic development regions. Seven cities and four counties are ineligible to receive federal money through the Small Cities program because they receive Community Development Block Grant funds directly from the federal government.²¹ Therefore, we looked at the distribution of funds among the regions as a whole and by their source: federal or state.²² As Table 2.2 shows,

²⁰ In the discussion of the Economic Recovery Grant program, "projects" will refer to the incidence of a business receiving money through a local unit of government. A local unit of government may receive one grant that funds two projects. The instance of a company receiving more than one infusion of money through this program, even for the same purpose (such as receiving a loan from the city and one from the county for one expansion), will be counted as multiple "projects."

²¹ The cities are St. Cloud, Duluth, Rochester, Moorhead, St. Paul, Minneapolis, and Bloomington. The counties are Hennepin, Ramsey, Anoka, and Dakota.

²² The figures do not reflect the federal funds that cities and counties receive directly.

Figure 2.2: DTED Economic Development Regions

- **Regions outside the Twin Cities metro area received 85 percent of the grant and loan funds.**

We also looked at the distribution of program dollars among industries. Table 2.3 shows that manufacturing companies received 80 percent of the funds awarded between fiscal years 1991 and 1995.

Some Legislators indicated that the Economic Recovery Grant program originally was intended to help smaller businesses that might have difficulty obtaining financing in the private sector. Table 2.4 shows the distribution of establishments and funding by the size of the establishment as measured by the number of employees.²³ We looked at both the number and size of awards because smaller

²³ The U.S. Census Bureau defines an establishment as a location of doing business. One firm may have more than one establishment. Throughout this discussion, "establishment," "business," and "company" are used interchangeably to indicate a location of doing business. "Firm" is used to indicate organizations with multiple locations of doing business.

Table 2.2: Economic Recovery Fund, FY 1991-95, Distribution of Funds by Region

<u>Region</u>	<u>Number of Projects</u>	<u>Percent of Projects</u>	<u>State Funded</u>	<u>Federal Funded</u>	<u>Amount of Grants and Loans</u>	<u>Percent of Dollars</u>	<u>Percent of 1990 Population</u>
Central	39	22.2%	\$7,263,750	\$2,954,814 ^a	\$10,218,564	24.4%	11.5%
Metro	24	13.6	5,791,261	500,000 ^b	6,291,261	15.0	52.3
Northeast	15	8.5	4,378,420	100,000 ^c	4,478,420	10.7	7.1
Northwest	12	6.8	2,229,490	1,415,000	3,644,490	8.7	3.6
Southeast	40	22.7	3,907,434	4,704,739 ^d	8,612,173	20.5	14.5
Southwest	27	15.3	3,464,000	2,048,000	5,512,000	13.2	6.5
West Central	19	10.8	2,409,000	750,000 ^e	3,159,000	7.5	4.5
Total	176		\$29,443,355	\$12,472,553	\$41,915,908		

Note: "Economic Recovery Fund" refers to both the state and federal funded programs. The population figures are included only to give an idea of the size of the region.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development reports. Population source: U.S. Census Bureau data as reported in Economic Resource Group, *1992 Economic Report to the Governor* (St. Paul: Author), 26-27.

^aSt. Cloud is ineligible to receive federal funds through this program.

^bSt. Paul, Minneapolis, Bloomington, Hennepin County, Ramsey County, Anoka County, and Dakota County are ineligible to receive federal funds through this program.

^cDuluth is ineligible to receive federal funds through this program.

^dRochester is ineligible to receive federal funds through this program.

^eMoorhead is ineligible to receive federal funds through this program.

Table 2.3: Economic Recovery Fund, FY 1991-95, Distribution of Funds by Industry Type

<u>Industry</u>	<u>Number of Projects</u>	<u>Percent of Projects</u>	<u>State Funded</u>	<u>Federal Funded</u>	<u>Amount of Grants and Loans</u>	<u>Percent of Dollars</u>	<u>Percent of Minnesota Establishments</u> ¹
Agriculture, Forestry, Fishing	2	1.2%	\$ 60,000	\$ 77,739	\$ 137,739	0.3%	2.1%
Manufacturing	132	79.0	22,698,189	9,668,814	32,367,003	80.2	6.5
Wholesale and Retail Trade	12	7.2	2,090,000	1,000,000	3,090,000	7.7	31.7
Finance, Insurance, Real Estate	8	4.8	1,746,256	0	1,746,256	4.3	9.5
Services	13	7.8	2,073,910	940,000	3,013,910	7.5	34.2
Total ²	167		\$28,668,355	\$11,686,553	\$40,354,908		

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Sources: Program Evaluation Division analysis of Department of Trade and Economic Development files. Establishment data from Department of Trade and Economic Development, *Business Tracking System Quarter Report* (September 1995). Data are from 4th Quarter, 1994, and were not adjusted for late or missing employer reports.

¹Percents do not add to 100 percent because not all industry groups received assistance through the Economic Recovery Fund.

²The total number of grants and loans and the total dollars do not match previous tables because nine projects were missing Standard Industrial Classification codes.

Table 2.4: Economic Recovery Fund, FY 1991-95, Distribution of Funds by Establishment Size and Location

Establishment ¹ Size	Number of Projects ²	Percent of Projects	Amount of Grants and Loans ²	Percent of State Dollars	Percent of Federal Dollars	Percent of 1993 Establishments In The State
NON-METRO						
0 to 4 employees ³	33	19.0%	\$7,262,324	19.2%	13.4%	25.8%
5 to 9	7	4.0	843,000	2.5	0.9	8.4
10 to 19	10	5.7	997,339	3.2	0.6	5.0
20 to 49	26	14.9	5,298,000	15.1	7.2	2.8
50 to 99	22	12.6	4,429,490	8.9	14.7	0.8
100 to 249	19	10.9	6,878,000	15.4	19.1	0.6
250 to 499	20	11.5	5,881,074	9.3	24.7	0.2
500 to 999	5	2.9	1,323,920	2.8	4.0	0.1
1,000+	8	4.6	2,515,000	3.8	11.3	0.0
Total	150	86.2%	\$35,428,147	80.1%	96.0%	43.7%
METRO						
0 to 4 employees ³	2	1.1%	\$750,000	2.6	0.0%	30.5%
5 to 9	1	0.6	500,000	1.7	0.0	10.1
10 to 19	3	1.7	455,000	1.6	0.0	6.9
20 to 49	4	2.3	610,000	2.1	0.0	5.1
50 to 99	2	1.1	445,513	1.5	0.0	1.8
100 to 249	8	4.6	2,180,748	5.8	4.0	1.2
250 to 499	1	0.6	100,000	0.3	0.0	0.3
500 to 999	1	0.6	500,000	1.7	0.0	0.1
1,000+	2	1.1	750,000	2.6	0.0	0.1
Total	24	13.8%	\$6,291,261	19.9%	4.0%	56.3%
Total	174	100.0%	\$41,719,408	100.0%	100.0%	100.0%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Sources: Program Evaluation Division analysis of Department of Trade and Economic Development files. Establishment numbers from: U. S. Bureau of the Census, County Business Patterns 1993 - Minnesota, CBP-93-25.

¹Establishments are locations of doing business. One firm may have more than one establishment. Retail establishments are excluded from these figures. For businesses receiving financial assistance, "establishment size" is the number of full-time equivalent employees at application reported by the business.

²Total numbers of awards and dollars do not match those on previous tables because two companies did not report size at application.

³"0 to 4 employees" includes start-up businesses receiving financial assistance from the state. The census figures are for establishments with one to four employees.

businesses might receive a large number of awards that are, on average, smaller.²⁴

We found:

- **Establishments with fewer than 100 employees received about 58 percent of state grant and loan funds, but they represent about 97**

²⁴ There are two possible problems with the data. First, the U.S. Census Bureau reports the distribution of establishments by the number of employees, not full-time equivalent employees. Applicants are supposed to report jobs to DTED in full-time equivalencies. Therefore, the number of employees at businesses receiving assistance may be larger than the U.S. Census Bureau establishments of the same size. Second, we recorded the number of employees at the business location on subsidiary requesting assistance at the time of application, unless only total firm or parent company employment was available on the application. The number of employees at the business location indicates establishment size and is more comparable to the U.S. Census Bureau data. However, total firm employment may be a more accurate indication of borrowing strength.

percent of all firms in the state. The disproportion was even greater in the metro area.

Larger establishments received disproportionately more grants and loans. Establishments with 500 or more employees, while accounting for less than one-half a percent of establishments in the state, received 12 percent of dollars awarded. Larger companies with more than 500 employees, however, make up almost 25 percent of non-retail employment. This pattern also may be in part a function of the inability of small firms to create a large number of jobs or to leverage private investment. Also, Twin City metro area applicants, particularly small firms, have difficulty qualifying for the program. Another possible explanation is that small businesses in the non-metro area might approach the Challenge Grant program instead of the Economic Recovery Fund.²⁵ In fact, one loan officer told us that he avoids loans to smaller businesses and encourages them to apply for financial assistance to the Challenge Grant program, that is designed to help businesses with smaller capital needs.

Larger establishments received disproportionately more grants and loans.

Table 2.5 shows the type of award used to distribute almost \$42 million in fiscal years 1991 through 1995. Businesses received over half of the assistance in the form of loans. However, the department awarded over \$14 million in awards that will not be repaid if job creation goals are met and maintained. Most of these awards were grants, which the department usually reserves for public infrastructure projects. The metro region received 15 percent of program funds, but 23 percent of forgivable loan dollars and 20 percent of granted funds.

Table 2.5: Economic Recovery Fund, FY 1991-95, Distribution of Funds by Type of Award

Type of Award	Number Awarded	Dollars Awarded	Average Award
Loan	119	\$24,470,419	\$205,634
Forgivable Loan	11	4,250,000	386,364
Grant	37	9,808,489	265,094
Other ¹	9	3,387,000	376,333
Total	176	\$41,915,908	\$238,159

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development files.

¹"Other" includes awards that are some combination of grants, loans, and forgivable loans.

Table 2.6 shows that companies with 100 or more employees received 88 percent of the dollars distributed through forgivable loans and 61 percent of the grants. Companies with fewer than 100 employees received 60 percent of loaned dollars and 78 percent of funds distributed through awards that were some combination of grants, loans, and forgivable loans.

²⁵ We discuss the Challenge Grant program in Chapter 4.

Table 2.6: Economic Recovery Fund, FY1991-95, Type of Award by Establishment Size

Establishment Size	Award Type							
	Loan ¹		Forgivable Loan		Grant		Other ²	
	#	Dollars	#	Dollars	#	Dollars	#	Dollars
0 to 4 employees ³	26	\$4,920,400	1	\$500,000	6	\$1,591,924	2	\$1,000,000
5 to 9	5	343,000	0	0	1	500,000	2	500,000
10 to 19	10	979,000	0	0	3	473,339	0	0
20 to 49	23	3,968,000	0	0	5	970,000	2	970,000
50 to 99	21	4,452,263	0	0	2	255,740	1	167,000
100 to 249	20	6,321,256	3	1,500,000	4	1,237,492	0	0
250 to 499	10	2,790,000	0	0	10	2,691,074	1	500,000
500 to 999	1	400,000	2	750,000	3	673,920	0	0
1,000+	1	100,000	5	1,500,000	3	1,415,000	1	250,000
Total	117	\$24,273,919	11	\$4,250,000	37	\$9,808,489	9	\$3,387,000
Under 100 employees	72.6%	60.4%	9.1%	11.8%	45.9%	38.7%	77.8%	77.9%
100 or more employees	27.4	39.6	90.9	88.2	54.1	61.3	22.2	22.1
Under 250 employees	89.7%	86.4%	36.4%	47.1%	56.8%	51.3%	77.8%	77.9%
250 or more employees	10.3	13.6	63.6	52.9	43.2	48.7	22.2	22.1

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development files.

¹Totals do not equal totals on previous tables because two firms did not report number of employees at application.

²"Other" includes awards that are some combination of loans, grants, and forgivable loans.

³"0 to 4 employees" includes start-up businesses receiving financial assistance from the state.

Table 2.7 shows businesses most often used Economic Recovery funds for machinery and equipment, construction and renovation, or infrastructure. DTED always funds public infrastructure projects such as roads or sewer systems with grants, but has sometimes awarded grants to finance other parts of a project such as working capital and employee training. The department awarded five of the seven grants for other uses prior to 1993.

The department awarded \$3.3 million in working capital to ten different projects in fiscal years 1991 and 1992. One of the changes made by E. Peter Gillette when he became commissioner of DTED was to stop the use of funds for working capital.

Most of the projects funded were expansions of Minnesota businesses.

Most of the projects funded by the Department of Trade and Economic Development were expansions of Minnesota businesses. Table 2.8 shows that only two awards were made to relocate a company from another state. However, this does not reflect the only activity involving out-of-state businesses. We noted four awards that the department made to Minnesota firms to help them relocate some of their out-of-state facilities to Minnesota, awards to at least two out-of-state firms to open facilities in Minnesota as part of their expansion plans, and awards to firms to expand their Minnesota operations instead of locating in other states.

Table 2.7: Economic Recovery Fund, FY 1991-95, Type of Award by Use

Use	Loan		Forgivable Loan		Grant		Other ¹		Total	
	Number	Dollars	Number	Dollars	Number	Dollars	Number	Dollars	Number	Dollars
Building	7	\$2,070,000	1	\$500,000					8	\$2,570,000
Construction/Renovation	37	7,407,650	1	250,000	1	\$100,000	1	\$500,000	40	8,257,650
Machinery and Equipment	62	11,251,369	8	3,000,000	2	550,000	6	2,250,000	78	17,051,369
Equity	1	500,000							1	500,000
Infrastructure					30	7,658,489			30	7,658,489
Property	1	150,000							1	150,000
Site Improvement					1	250,000			1	250,000
Training					1	500,000			1	500,000
Working Capital	9	2,791,500			1	500,000			10	3,291,500
Multiple Uses ²	2	299,900	1	500,000	1	250,000	2	637,000	6	1,686,900
Total	119	\$24,470,419	11	\$4,250,000	37	\$9,808,489	9	\$3,387,000	176	\$41,915,908

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development files.

¹"Other" includes awards that are some combination of loans, grants, and forgivable loans.

²"Multiple uses" includes one loan for building and infrastructure, one "other" for building and infrastructure, one loan for construction and equipment, one forgivable loan for equipment and infrastructure, one grant for property taxes and training, and one "other" for training and construction.

Table 2.8: Economic Recovery Fund, FY 1991-95, Type of Award by Project Type

Project Type	Loan		Forgivable Loan		Grant		Other ¹		Total	
	Number	Dollars	Number	Dollars	Number	Dollars	Number	Dollars	Number	Dollars
Startup	17	\$4,016,000	1	\$500,000	7	\$1,786,924	2	\$1,000,000	27	\$7,302,924
Expansion	87	17,357,419	9	3,250,000	23	6,200,965	5	1,417,000	124	28,225,384
Relocation							2	970,000	2	970,000
Retention	1	200,000	1	500,000	1	75,600			3	775,600
Expansion/Relocation ²	8	1,480,000			5	1,245,000			13	2,725,000
Startup/Retention ³	6	1,417,000			1	500,000			7	1,917,000
Total	119	\$24,470,419	11	\$4,250,000	37	\$9,808,489	9	\$3,387,000	176	\$41,915,908

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development files.

¹"Other" includes awards that are some combination of grants, loans, and forgivable loans.

²"Expansion/Relocation" is the expansion of a Minnesota company that is accomplished either by relocating operations from another state or relocating from one Minnesota location to another.

³"Startup/Retention" is facilitating new ownership of an existing company, usually to prevent the business from closing.

JOB CREATION

It is difficult to know the precise effects of job creation programs.

The department views the primary purpose of the Economic Recovery Fund as creating new jobs and retaining existing jobs in the state. But evaluating the effect of DTED loans or grants on job creation is difficult for at least three reasons. First, it is impossible to determine whether an observed change in the number of jobs is attributable to a particular program. There are many complex forces in the economy, making it difficult to know what might have happened in the absence of the state program. Second, it is generally difficult to determine whether the creation of new jobs in one location did or did not come at the expense of jobs in another location within the state. According to economists, this so-called “displacement effect” is particularly common when aid is given to retail businesses. Finally, it is difficult to evaluate the secondary and side effects of jobs that are created. A business might spin off additional economic activity and, hence more jobs, or it might create more pollution or affect other jobs in a negative way.

Nevertheless, in this section we address several issues concerning the effect of the Economic Recovery Fund on job creation or retention. We used a variety of methods to do this. First, we reviewed job and wage information recorded in project progress reports that all grantees must file with DTED. We also reviewed unemployment compensation tax returns for companies that received grants and loans to verify the companies’ self reported data. In addition, we contacted 40 companies that received grants or loans to try to get a better idea of whether they would have created the jobs without state assistance.

DTED Progress Reports

Grantees (primarily city governments) must produce a progress report every six months through completion of the project, by obtaining project information from the company involved. The department uses the project reports to track whether the project is on budget and whether job creation goals are being met. The accuracy of the progress reports is critical for monitoring project progress and evaluating the effectiveness of the Economic Recovery Fund. Progress reports are often completed by the companies themselves with no verification of job creation from either the grantee or DTED.

We found that project progress reports contained some job creation and wage and benefit information that was inconsistent, incomplete, and in a few cases, inaccurate. Nonetheless, the progress reports are the best available source of information and we believe they provide a reasonable estimate of the jobs created after a DTED loan or grant is awarded. Progress reports are available for 155 of the 176 projects between 1991 and 1995. Reports are not available for 21 newly established projects.²⁶

According to the department, projects are generally to achieve job creation goals within two years of receiving funds. Because the projects are at varying stages of

²⁶ There were 185 projects awarded but nine projects were terminated before the money was disbursed.

The Economic Recovery Fund has assisted in creating over 8,300 jobs since 1991.

completion, we divided them into three subgroups: closed, open for more than two years, and open for less than two years. Projects are "closed out" when DTED determines that the project has made satisfactory progress towards budget and job creation goals. When DTED "closes" a project, the project's original goals have not necessarily been met. Loan officers told us that they would sometimes re-score projects and close them if they would score the minimum 400 points with fewer jobs created than originally planned.²⁷

As Table 2.9 shows, DTED has received final progress reports and has formally "closed out" 96 of the 155 projects. We consider job creation information for these projects to be complete. There are nine open projects that received funds in fiscal years 1991 and 1992 that should have met their job creation targets and closed by now. There are 50 open projects that received funds in fiscal years 1993, 1994, and 1995 that are still working to accomplish job creation goals. As a result, job creation information for these projects is preliminary. We found:

- **Economic Recovery Fund grants and loans for fiscal years 1991 through 1995 have assisted in the creation or retention of 8,337 jobs.**

Table 2.9: Economic Recovery Fund, FY 1991-95, Distribution of Funds and Jobs Created by Project Status

<u>Project Status</u>	<u>Number of Projects</u>	<u>Percent of Projects</u>	<u>Amount of Grants and Loans</u>	<u>Percent of Total Dollars</u>	<u>Jobs Created</u>	<u>Percent of Total Jobs Created</u>
Open < 2 years ¹	50	32%	\$12,410,654	35%	1,947	23%
Open > 2 years ²	9	6	2,482,500	7	491	6
Closed ³	<u>96</u>	<u>62</u>	<u>20,988,754</u>	<u>58</u>	<u>5,898</u>	<u>71</u>
Total	155	100%	\$35,881,908	100%	8,337	100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development reports.

¹Includes all projects originating in FY 1993-95 that have not been completed for which job creation information was provided.

²Includes all projects originating in FY 1991-92 that have not been completed for which job creation information was provided.

³Includes all projects that have been completed for which job creation information was provided.

Table 2.10 shows the distribution of the projects, grant and loan amounts, and jobs by area of the state. The table shows that:

- **Projects in the Metro region created the highest number of jobs.**

The percentage of total jobs created was higher than the percentage of total funds received within the following areas: Metro, Northwest, and West Central. It was lower in the Central, Northeast, Southeast, and Southwest areas.

²⁷ The department informs us that they have "closed out" 16 of the 96 closed projects we reviewed with fewer jobs than originally projected.

Table 2.10: Economic Recovery Fund, FY 1991-95, Distribution of Funds and Jobs Created by Region

<u>Region</u>	<u>Number of Projects</u>	<u>Percent of Projects</u>	<u>Amount of Grants and Loans</u>	<u>Percent of Total Dollars</u>	<u>Jobs Created</u>	<u>Percent of Total Jobs Created</u>
Central	33	21%	\$8,668,564	24%	1,677	20%
Metro	22	14	5,566,261	16	1,974	24
Northeast	15	10	4,478,420	12	721	9
Northwest	10	6	3,033,490	8	1,481	18
Southeast	37	24	7,862,173	22	1,112	13
Southwest	21	14	3,864,000	11	780	9
West Central	17	11	2,409,000	7	592	7
Total	155	100%	\$35,881,908	100%	8,337	100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development reports.

Individual projects received between \$20,000 and \$500,000 in grants or loans. Table 2.11 shows the job distribution by award amount. The number of jobs created is fairly commensurate with the size of the award. That is, in general, the larger the award the larger the number of jobs created.

We noted earlier that small businesses received a disproportionately smaller amount of awards and funds. This may be due to the inability of small firms to create jobs at the same level as larger firms. Table 2.12 shows the job distribution by establishment size. As the table shows, firms with less than 20 employees created 25 percent of the total jobs, and larger companies created more jobs with less money than smaller companies. Firms with more than 500 employees created 22 percent of the total jobs with only 10 percent of total funds received.

Table 2.11: Economic Recovery Fund, FY 1991-95, Distribution of Funds and Jobs Created by Award Amount

<u>Amount in Thousands</u>	<u>Number of Projects</u>	<u>Percent of Projects</u>	<u>Amount of Grants and Loans</u>	<u>Percent of Total Dollars</u>	<u>Jobs Created</u>	<u>Percent of Total Jobs Created</u>
Under \$50	11	7%	\$392,934	1%	163	2%
\$50 to 99	20	13	1,351,739	4	251	3
\$100 to 149	26	17	2,825,324	8	631	8
\$150 to 199	30	19	5,373,792	15	1,208	14
\$200 to 249	9	6	1,914,609	5	351	4
\$250 to 299	12	8	3,001,500	8	766	9
\$300 to 349	5	3	1,521,500	4	510	6
\$350 to 399	5	3	1,839,490	5	863	10
\$400 to 449	8	5	3,276,000	9	568	7
\$450 and over	29	19	14,385,000	40	3,026	36
Total	155	100%	\$35,881,908	100%	8,337	100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development reports.

Table 2.12: Economic Recovery Fund, FY 1991-95, Distribution of Funds and Jobs Created by Establishment Size

Establishment Size	Number of Projects	Percent of Projects	Amount of Grants and Loans	Percent of Total Dollars	Jobs Created	Percent of Total Jobs Created
0 to 4 employees	33	21	\$7,764,324	22%	1,704	20%
5 to 9	8	5	1,343,000	4	117	1
10 to 19	12	8	1,392,339	4	292	4
20 to 49	27	17	5,2983,000	15	793	10
50 to 99	21	14	3,875,003	11	658	8
100 to 249	25	16	8,058,748	22	1,823	22
250 to 499	17	11	4,570,074	13	1,124	13
500 to 999	4	3	1,223,920	3	504	6
1,000 or more	6	4	2,265,000	6	1,312	16
Unknown	2	1%	106,500	0	10	0
Total	155	100%	\$35,881,908	100%	8,337	100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

Table 2.13 shows the distribution of jobs by the Standard Industrial Classification (SIC) codes. We found SIC numbers for 146 companies from their application forms or from the Department of Economic Security. Table 2.13 shows:

- **Manufacturing companies created over 60 percent of total jobs.**

As we discussed earlier, grants and loans are more likely to truly "create" jobs when they are awarded to manufacturing firms with no Minnesota competitors. DTED awarded almost 80 percent of Economic Recovery funds to manufacturing firms between 1991 and 1995. In 1993, the manufacturing industry in Minnesota accounted for approximately 20 percent of total state employment. Projects in the services industry created 22 percent of total jobs with eight percent of total dollars received.

Table 2.13: Economic Recovery Fund, FY 1991-95, Distribution of Funds and Jobs Created by Industry Type

Industry	Number of Projects	Percent of Projects	Amount of Grants and Loans	Percent of Total Dollars	Jobs Created	Percent of Total Jobs Created
Agriculture, Forestry, Fishing	2	1%	\$ 137,739	0%	22	0%
Manufacturing	118	76	27,981,003	78	4,982	60
Transportation, Public Utilities	0	0	0	0	0	0
Trade	6	4	1,490,000	4	515	6
Finance, Insurance, Real Estate	8	5	1,746,256	5	664	8
Services	13	8	3,013,910	8	1,830	22
Unknown	8	5	1,513,000	4	323	4
Total	155	100%	\$35,881,908	100%	8,337	100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

Job Creation by Type of Award

We were interested in whether the type of award was related to the number of jobs created. To answer this question, we separated projects into three award types: loans, grants, and grant/loans. The grant/loan category includes forgivable loans and awards that are a combination of grants, loans and forgivable loans. In most cases, projects in the grant/loan category are grants or forgivable loans where the first \$100,000 of the award is a loan repaid to the local government to capitalize a revolving loan fund. Table 2.14 shows that projects receiving grants created 35 percent of total jobs with only 20 percent of funds distributed. Grants created jobs at the lowest cost per job of \$2,516, or \$2,198 for projects that were completed. Of course, grants are not paid back and, therefore, do not generate any future economic activity. Most of the program's loans are repaid to the General Fund for future use.

Table 2.14: Economic Recovery Fund, FY 1991-95, ERF Dollars Spent per Job Created by Project Status and Award Type

Project Status	Award Type	Number of Projects	Amount	Jobs Created	Dollars per Job
Open < 2 years ¹	Loan	32	\$6,620,800	792	\$8,355
	Grant/Loan ⁴	9	3,970,000	603	6,584
	Grant	<u>9</u>	<u>1,819,854</u>	<u>552</u>	<u>3,297</u>
	All Types	50	\$12,410,654	1,947	\$6,374
Open > 2 Years ²	Loan	6	\$1,495,000	245	\$6,102
	Grant/Loan	1	250,000	64	3,906
	Grant	<u>2</u>	<u>737,500</u>	<u>182</u>	<u>4,052</u>
	All Types	9	\$2,482,500	491	\$5,056
Closed ³	Loan	72	\$13,669,111	3,097	\$4,414
	Grant/Loan	6	2,417,000	571	4,236
	Grant	<u>18</u>	<u>4,902,643</u>	<u>2,230</u>	<u>2,198</u>
	All Types	96	\$20,988,754	5,898	\$3,559
Total	Loan	110	\$21,784,911	4,134	\$5,269
	Grant/Loan	16	6,637,000	1,238	5,363
	Grant	<u>29</u>	<u>7,459,997</u>	<u>2,964</u>	<u>2,516</u>
	All Types	155	\$35,881,908	8,337	\$4,304

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

¹Includes all projects originating in FY 1993-95 that have not been completed for which job creation information was provided.

²Includes all projects originating in FY 1991-92 that have not been completed for which job creation information was provided.

³Includes all projects that have been completed for which job creation information was provided.

⁴Includes forgivable loans and awards that are a combination of grants, loans, and forgivable loans.

Job Promises

Most companies meet their job creation goals.

At the beginning of a project, each company promises to create a specific number of jobs and the promise becomes part of the grant or loan agreement in most cases. We compared the job creation goal found in the project files with the number of new jobs actually reported on progress reports. As Table 2.15 shows, we found:

- **Ninety-five of the 155 projects met or exceeded promised job creation goals. Overall, the companies receiving grants or loans created more jobs than they promised. As a group, 78 of the 96 projects that are closed created as many jobs as they promised.**

Table 2.15: Economic Recovery Fund, FY 1991-95, Jobs Promised and Created by Project Status

Project Status	Number of Projects	Projects that Met Job Goals ⁴	Number of Jobs Promised	Number of Jobs Created	Percent of Jobs Promised
Open < 2 years ¹	50	13	2,101	1,947	93%
Open > 2 years ²	9	4	570	491	86
Closed ³	<u>96</u>	<u>78</u>	<u>5,594</u>	<u>5,898</u>	<u>105</u>
Total	155	95	8,264	8,337	101%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

¹Includes all projects originating in FY 1993-95 that have not been completed for which job creation information was provided.

²Includes all projects originating in FY 1991-92 that have not been completed for which job creation information was provided.

³Includes all projects that have been completed for which job creation information was provided.

⁴Includes all projects that met or exceeded job goals or were below job goals by less than 1 FTE job.

The table shows that for closed projects and projects more two years old, 82 of the 105 companies had met job creation goals. The 23 companies that had not met job goals fell short by a total of 1,022 jobs including nine firms that went out of business during the period resulting in 885 fewer jobs than promised. The 50 projects that have been open less than two years have yet to create 665 new jobs.

Table 2.16 shows that projects with grants created the highest percentage of jobs promised (130 percent). As Table 2.17 shows, firms with over 50 employees had greater success than smaller firms at creating more jobs than promised.

Table 2.16: Economic Recovery Fund, FY 1991-95, Jobs Promised and Created by Award Type

<u>Award Type</u>	<u>Number of Projects</u>	<u>Number of Jobs Promised</u>	<u>Number of Jobs Created</u>	<u>Percent of Jobs Promised</u>
Loan	78	3,779	3,342	88%
Grant/Loan ¹	7	528	635	120
Grant	20	1,857	2,412	130
Total	105	6,164	6,389	104%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs. It includes all projects that have been completed and all projects more than two years old that have not been completed for which job creation information was provided.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

¹Includes forgivable loans and awards that are a combination of grants, loans, and forgivable loans.

Table 2.17: Economic Recovery Fund, FY 1991-95, Jobs Promised and Created by Establishment Size

<u>Establishment Size</u>	<u>Number of Projects</u>	<u>Number of Jobs Promised</u>	<u>Number of Jobs Created</u>	<u>Percent of Jobs Promised</u>
0 to 4 employees	20	1,807	1,473	82%
5 to 9	4	124	101	81
10 to 19	10	156	170	109
20 to 49	15	552	545	99
50 to 99	16	541	580	107
100 to 249	19	1,214	1,474	121
250 to 499	13	774	943	122
500 to 999	2	182	145	80
1,000 or more	5	806	948	118
Unknown	1	8	10	125
Total	105	6,164	6,389	104%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs. Includes all projects that have been completed and all projects more than two years old that have not been completed for which job creation information was available.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

Wages and Benefits

In 1993, the Legislature added a requirement that DTED report on wages and benefits of the jobs created with the department's assistance.²⁸ Beginning in July 1994, DTED began requiring companies to report wage and benefit information in progress reports.

²⁸ *Minn. Laws* (1993), Ch. 252, subd 1 (18).

Wages

One hundred five projects provided wage information for 4,979 of the 8,337 jobs created between 1991 and 1995. Most of the projects that reported wage information originated between 1993 and 1995. As we noted earlier, companies were inconsistent in providing wage information.²⁹ Some companies reported the wages for jobs created every six months over the two year period. Others reported all of the wages for jobs created over the past two years in the final report. The date of hire and the wage paid were unclear many times.³⁰ Frequently, we were unable to accurately match dates with the wages reported so adjusting for inflation was impossible.

Nonetheless, our examination of wages gives a picture of the level of jobs the state has assisted in creating with the Economic Recovery Fund subsidy. Table 2.18 shows the distribution of wages per hour for all jobs, by project status. We found:

- The average wage for the jobs created was \$8.64 per hour. The median wage was \$7.20 per hour.

The average wage of the jobs created was \$8.64 and the median was \$7.20.

Table 2.18: Economic Recovery Fund, FY 1991-95, Average and Median Wage by Project Status

Project Status	Number of Projects	Number of Jobs	Average Wage	Median Wage
Open < 2 years ¹	43	1,971	\$9.79	\$8.00
Open > 2 years ²	5	121	8.21	7.25
Closed ³	57	2,887	7.87	7.00
Total	105	4,979	\$8.64	\$7.20

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

¹Includes all projects originating in FY 1993-95 that have not been completed for which wage information was provided.

²Includes all projects originating in FY 1991-92 that have not been completed for which wage information was provided.

³Includes all projects that have been completed for which wage information was provided.

As Table 2.19 shows, the average wage of jobs created by Economic Recovery Fund projects was lower than the average wage of jobs in all regions in the state in 1993. Figure 2.3 shows the distribution of wages for the jobs. The department notes that the jobs they are assisting in creating are usually entry-level and as a

²⁹ We refer here to companies because, although grantees (mostly cities) are responsible for filing the progress reports, in almost all cases the report is prepared by the company and forwarded by the local unit of government to DTED.

³⁰ For example, a company would report the creation of 100 production jobs between 1991 and 1992 with wages starting between 8 and 10 dollars an hour.

Table 2.19: Economic Recovery Fund, FY 1991-95, Average and Median Wage by Region

Region	Number of Projects	Number of Jobs	Median Wage	Average Wage	1993 Region Average Wage ¹
Central	22	1,173	\$7.00	\$8.18	\$9.54
Metro	16	1,069	9.00	10.78	13.85
Northeast	9	483	7.26	9.35	10.63
Northwest	6	600	5.95	6.73	8.88
Southeast	29	913	7.71	9.12	10.48
Southwest	13	253	6.58	7.95	8.89
West Central	10	488	5.50	6.20	8.62
Total	105	4,979	\$7.20	\$8.64	\$12.36

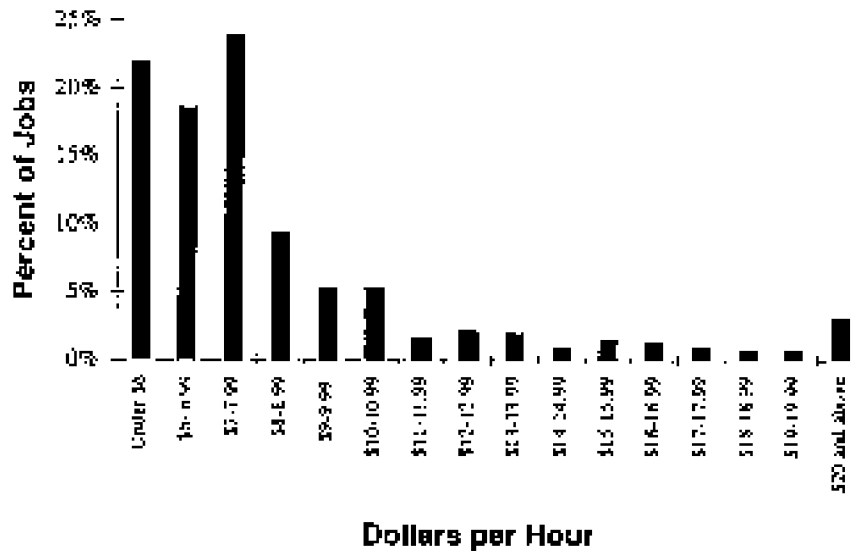
Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

¹1993 Minnesota Average Covered Employment and Wages, Department of Economic Security.

Sixty-three percent of the jobs paid wages less than \$8.00 per hour.

Figure 2.3: Economic Recovery Fund, FY 1991-95, Wage Distribution



Source: Program Evaluation Division analysis of Department of Trade and Economic Development wage reports.

result they tend to pay lower wages. As one can see from examining the figure, the distribution of the jobs created is skewed towards the lower wage levels with 63 percent of the jobs paying less than \$8.00 per hour. About 42 percent of the jobs paid less than \$7.00 per hour. In comparison, the 1993 poverty level for a family of four was \$14,350, or the equivalent of \$6.89 per hour.

Table 2.19 also shows that the Metro area had the highest average wage at \$10.78 per hour and a median wage at \$9.00 per hour. The Northwest and West Central areas reported the lowest average wages per hour at \$6.73 and \$6.20 respectively, with a median wage of \$5.95 in the Northwest region and \$5.50 in the West Central region. Approximately 90 percent of jobs created in these two regions had wages below \$8.00 per hour. Projects receiving forgivable loans and combination loan/grant awards created jobs with higher wages than projects receiving loan or grant awards. Establishments with fewer than 20 employees created jobs with higher average wages than larger firms.

Table 2.20 shows the average and median wages by the year of the project's origination. Because of the way companies report to DTED, the jobs could have been created in any fiscal year. For example, projects originating in 1991 could have hired people and reported to the department in 1993. The table shows a slight trend of increasing wages by the year of project origination, although some of the increase may be due to inflation. Table 2.21 shows that state grants and loans tended to create jobs with higher wages than those from the federal program.

There is a trend toward increasing wages but inflation probably accounts for some of the increase.

Table 2.20: Economic Recovery Fund, FY 1991-95, Average and Median Wage by Fiscal Year of Award

<u>Fiscal Year Project Originated</u>	<u>Number of Projects</u>	<u>Number of Jobs</u>	<u>Median Wage</u>	<u>Average Wage</u>
1991	7	205	\$6.79	\$7.36
1992	17	619	7.00	7.57
1993	26	1,070	7.40	9.22
1994	32	1,682	7.00	8.31
1995	<u>23</u>	<u>1,404</u>	<u>7.50</u>	<u>9.26</u>
Total	105	4,979	\$7.20	\$8.64

Note: "Economic Recovery Fund" refers to both state and federal funded programs.

Source: Program Evaluation Division analysis of Department of Trade and Economic Development data.

One partial explanation for distribution of wages being skewed towards lower paying jobs is because the state and federal program are linked. The federal program predated the state program by one year, and partially as a result, the state program adopted the same rules for awarding grants as the federal program. The Economic Recovery Grant statute clearly focuses on job creation as a goal of the program. Projects funded by the federal Community Development Block Grant are required to fill 51 percent of the jobs created with low and moderate income (LMI)

Table 2.21: Economic Recovery Fund, FY 1991-95, Average and Median Wage by Source

<u>Source</u>	<u>Number of Projects</u>	<u>Number of Jobs</u>	<u>Average Wage</u>	<u>Median Wage</u>
State	89	4,160	\$8.87	\$7.50
Federal	16	819	7.51	6.00
Total	105	4,979	\$8.64	\$7.20

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

State-funded projects have created higher-paying jobs than federal-funded projects.

individuals.³¹ The state-funded program requires that jobs be filled by or made available to LMI persons. Jobs that do not require specialized training are considered "available to" LMI persons. In many cases this has resulted in the approval of projects that created lower-skill, lower-wage jobs. However, in the current economic environment, when unemployment rates in many areas of the state are around 3 percent, the state might want to reconsider the LMI restriction on state funds. In our opinion, the state program should have the flexibility to assist companies that might require specialized training and offer higher salaries.

We recommend:

- **DTED should separate the requirements for state funds from the federal CDBG program.**

Benefits

Eighty-three companies, primarily from projects funded between 1993 and 1995, provided information about benefits for 3,619 of the 8,337 jobs created between 1991 and 1995. Table 2.22 shows that projects in the Northwest region had the lowest percentage of jobs with health and life insurance benefits. Large firms provided more benefits to a larger percentage of jobs created than smaller firms.

When information was available, we found that:

- **Approximately 90 percent of the jobs created provided health care, 56 percent dental, 85 percent life, and 62 percent retirement benefits.**

Most jobs provided employee benefits.

Verification of Job Creation

We wanted to determine if companies' self-reported job creation data was accurate, and whether jobs created were retained after the project was "closed out" by

³¹ The federal government requires the jobs be filled by or made available to LMI persons. The state has chosen the stricter standard.

Table 2.22: Economic Recovery Fund, FY 1991-95, Benefits Provided by Region

<u>Region</u>	<u>Number of Projects</u>	<u>Jobs Providing Benefits</u>				<u>Number of Jobs</u>
		<u>Health</u>	<u>Dental</u>	<u>Life</u>	<u>Retirement</u>	
Central	16	871 94%	460 50%	869 94%	384 41%	928 100%
Metro	14	757 99%	747 98%	759 99%	681 89%	764 100%
Northeast	6	372 93%	239 60%	342 86%	379 95%	398 100%
Northwest	5	144 61%	140 59%	140 59%	140 59%	236 100%
Southeast	22	493 77%	182 28%	490 77%	329 51%	639 100%
Southwest	10	190 92%	67 33%	150 73%	104 50%	206 100%
West Central	10	396 88%	180 40%	330 73%	226 50%	449 100%
Total	83	3,222 89%	2,015 56%	3,080 85%	2,243 62%	3,619 100%

Note: "Economic Recovery Fund" refers to both the state and federal funded programs.

Source: Program Evaluation Division analysis of the Department of Trade and Economic Development reports.

DTED. We examined data from Department of Economic Security (DES) unemployment tax returns to determine employment levels on various dates.³²

With the assistance of DES research staff, we collected information on wages and employment at the quarter nearest the grant award date for all awards made between July 1990 and December 1993. We were able to collect information on 112 of the 143 awards made in that time period. Twenty-six companies appeared to be reporting incorrectly to DES, and five companies had more than one award during the period. We collected the same information at a point two years later when job creation is supposed to be complete. Finally, we collected information on employment and wages for all companies in December 1994.

³² There are some limits to the DES data. Firms are supposed to report separately for all locations in the state. Unfortunately, not all firms report correctly. Many multi-location companies report all locations in the state as one, resulting in a decrease in the number of companies whose employment could be verified. Another limitation is that the number of employees reported includes anyone who worked during that quarter. As a result, part-time employees inflate the reported employment level. Fortunately, the reporting creates a bias in a conservative direction. We can be comfortable knowing that if the data show less employment than promised, it is not an artifact of the way the data is collected or reported.

We found:

- **Almost all companies' employment levels reported on their tax returns were consistent with employment reported to DTED.**

In other words, companies appear to be reporting the same employment levels to both of these state agencies. Since companies would have an incentive to over-report employment to DTED and under-report it to DES, we believe reported employment levels are accurate.

Because businesses are supposed to create permanent jobs, we also reviewed whether companies had met their job creation goals and had retained the jobs. The Department of Trade and Economic Development "closes out" a project as soon as it has met the job creation goal. Companies often meet their job goal within six months to a year of the loan or grant award date. We found:

- **Ninety-one of the 112 companies maintained employment levels at the level agreed to in the loan or grant agreement.**

Sometimes the jobs created were not permanent.

Unfortunately, sometimes employment decreases after the project is "closed out" by DTED. Twenty-one companies did not meet or did not maintain employment at the agreed to level. Three of the companies had gone out of business, five companies did not meet their job goal within two years, and 13 companies met their job creation goals but employment levels fell after the project was "closed out."³³ Employment levels at five companies fell to levels lower than when they had applied for the loans. One company had a forgivable loan but had not met its job goals in the required two year period.

We also found that:

- **DTED does not consistently follow-up on companies' job creation claims.**

Grantees had not submitted many of the progress reports that we were interested in; in some cases they were years late. We also found some companies are supposed to continue to report job creation status after their grant/loan is "closed out" but we noted several instances where the reports had not been filed and there was no follow-up from DTED. DTED has also failed to follow-up on at least one company with a "forgivable" loan that had not met its job creation goal. We recommend:

- **DTED should develop a system to consistently follow-up on job creation progress reports. DTED should also develop a process for following up on and collecting repayments from companies that do not meet job creation requirements.**

We think periodically checking the companies' job and wage levels using unemployment insurance information would also be a good idea. By getting wages and

³³ Since December 1994, one additional company with 109 jobs has gone out of business.

employment information when the project starts and at periodic benchmark dates, the department will have a better idea of the economic effects of the program.

PERSPECTIVES OF FIRMS RECEIVING GRANTS

We also wanted to determine whether companies would have undertaken the job creation projects if they had not received a loan or grant from the state.³⁴ We asked key decisionmakers (Presidents, CEOs, General Managers, Vice Presidents, etc.) at a sample of 40 companies that had received loans or grants what they thought would have happened if they had not received public assistance. Our sample was not a random one and so we do not know if it is representative of all companies that received grants. We talked with representatives of almost all of the firms receiving grants or loans of the maximum amount of \$500,000 between 1991 and 1995 and also a number of firms receiving smaller awards.³⁵ The executives we spoke with represented firms that had received \$16.5 million in Economic Recovery Funds. Because we wanted the executives to speak freely, we told them their remarks would not be associated with their company in our report.

We asked the executives if they had considered other locations in Minnesota and or in other states. Sixty-five percent (26 of 40) had considered other locations for their expansion. Twenty of the 26 companies had considered locations in other states. Fourteen of the companies only considered locations in Minnesota, four of those because the project was tied to a specific Minnesota location. Some of the 14 companies that only considered Minnesota locations told us that they had not seriously consider other states although they had been contacted by them.

The most important factor for companies choosing Minnesota locations was the good labor force.

Fifteen of twenty-six companies that considered other locations mentioned more than one factor as being important in their location decision. The most important factors for companies in choosing a Minnesota location were traditional factors such as Minnesota's good labor force, the economics of the project worked out here, and good access to markets. These reasons were coupled in many cases with the fact that most companies (36 of 40) were already located in Minnesota. Almost one-half of the executives already living in Minnesota explicitly mentioned the desire to remain at their current location or to expand in Minnesota if at all possible. It appears that "quality of life" factors played an important part in many of the decisions. However, the most frequently mentioned factor (17 of 40 executives) was city and state financial incentives. For most executives this was not the most important factor, but for six it was the most important factor. Some sample comments about the most important location decision factors:

³⁴ We acknowledge that there is no precise way to determine what would have happened at these companies if they had not received a grant or a loan. Also, company executives, knowing that we were evaluating the effectiveness of the Economic Recovery Fund and having benefited from it in the past, might have overstated the influence of the incentive on their location or expansion decisions.

³⁵ Two firms receiving large grants refused to speak with us and we did not pursue the matter.

- Economic viability, availability of raw product, labor pool, taxes, regulations, incentives.
- Existing labor pool, availability of education, facility capacity, economic variables, and incentives.
- We would always prefer to expand in Minnesota if the economics are appropriate.
- Labor force was the most critical factor, also relationship with the state university, and the (Economic Recovery Grant) funding mitigated financial advantages of locations in other states.

Another executive told us:

We all live in this community and wanted to stay. But we received offers from all over the country and if we want to stay competitive we have to ... go where it is best financially for the company. The (Economic Recovery Grant) funding allowed us to stay.

Three-fourths of the executives heard about the Economic Recovery Fund program through city or local economic development officials although several mentioned more than one source of information. Many of the executives we interviewed had been extensively “wooded” by other states. One executive told us that they really had not thought of relocating until they were approached by Iowa, South Dakota, and Kansas with offers that made them realize it was expensive to do business in Minnesota.

Seventeen of 40 executives said that without state assistance, their companies’ expansion would have occurred in another state.

Twenty-eight of the executives said that the “same project” would probably or definitely not have happened in Minnesota without the state’s participation, although one company told us that the same project would have definitely gone ahead and six said that it probably would have. Fifteen said that some expansion would have occurred in Minnesota regardless of the loan/grant, but it would have been smaller, taken longer, or created fewer jobs. Seventeen executives said the expansion would have occurred in another state without the ERF assistance.

Discussions with these 40 executives leads us to several conclusions. First, there is real competition for Minnesota businesses to move or expand in surrounding states rather than in Minnesota. Second, the Economic Recovery Fund has been an important factor for some companies deciding to stay and expand their business in Minnesota. Third, although there is no way to know for sure, we believe many (22 of 40) of the Economic Recovery Fund projects, would have gone forward even without the state’s assistance. Some projects, however, might have been smaller or taken longer without the state aid.