

**Analysis of the Economic
Development Initiatives
Included in the
Governor's FY 2016
Budget Proposal**

June 2015



RIPEC Mission Statement

RIPEC is an independent, nonprofit and nonpartisan public policy research and education organization dedicated to the advancement of effective, efficient and equitable government in Rhode Island.

Through in-depth research, program monitoring, advocacy and public information activities, RIPEC:

- Suggests approaches to help improve the effectiveness and efficiency of government agencies;
- Promotes fiscal responsibility and sound management practices;
- Assists elected officials and their staffs in the development of sound policies and programs;
- Enhances understanding between the private sector and state and local governments;
- Provides objective information and conducts educational programs for the benefit of Council members, public officials, and the general public;
- Builds coalitions with other community groups to promote sound public policies; and
- Promotes a public policy agenda to foster a climate for economic opportunity.

Introduction

This Rhode Island Public Expenditure Council (RIPEC) report provides an overview of the Governor's economic development initiatives included within Article 29 of the FY 2016 proposed budget, as well as within Article 11 as it relates to visitor attraction and tourism. The report also references other relevant components of the proposed budget submission that, if enacted, would impact the manner in which economic development activities are conducted within the state. Lastly, the report provides an overview of best practices used by public bodies to evaluate and manage economic development programs.

In 2012, RIPEC released an analysis of Rhode Island's economic development structure titled "Defining Government's Role in Economic Development in the Ocean State." Following the report's release, the General Assembly took action on several of the report's recommendations. These steps included the creation of an Executive Office of Commerce, led by the newly-created position of Secretary of Commerce, a reorganization of the previous Economic Development Corporation into the Rhode Island Commerce Corporation and the establishment of a Council of Economic Advisors, among other reforms. The Governor's proposed economic development initiatives included in the FY 2016 budget submission represent the first attempt to utilize the state's new economic development structure.

The Governor's proposed economic development initiatives come in light of continued economic difficulties for Rhode Island. Although the state's unemployment rate has declined, job growth has been uneven and the percentage of residents in the labor force has declined. To combat this lingering economic weakness, the Governor has proposed a variety of economic development programs that are intended to provide the tools that state government needs to effectively promote economic growth. The following sections of this report analyze each of the proposed initiatives included in the FY 2016 budget submission.

Governor's Proposed Economic Development Programs

On Thursday, March 12, the Governor submitted her FY 2016 proposed budget for General Assembly consideration. The proposal includes several tax credit programs, economic development programs, investments and other initiatives intended to promote economic growth in Rhode Island. These programs are designed to strengthen, retain and grow existing businesses, as well as to attract new companies and additional investment to the state by:

- Expanding access to capital;
- Creating real estate tools;
- Encouraging construction of job-producing projects;
- Connecting businesses with research and development (R&D) assistance; and
- Catalyzing stronger partnerships in key industry sectors.

The Governor refers to the entire package of proposals, including some initiatives not contained within the budget, as the “Ocean State WAVE.” The four components of the WAVE plan are workforce development, advanced industries and innovation, visitor attraction and enterprise expansion and recruitment.

Article 11: Tourism and Visitor Attraction

Visitor attraction represents one component of the Governor’s Ocean State WAVE strategy to improve Rhode Island’s economy. To increase tourism, the Governor proposes focusing efforts on a statewide tourism and business marketing campaign. At the present time, most visitor attraction efforts in Rhode Island are conducted through regional tourism bureaus located throughout the state. To fund the proposed statewide visitor attraction program, the Governor proposes redirecting a portion of state hotel tax revenues from the regional tourism bureaus to the Rhode Island Commerce Corporation.

Currently, revenues generated by the 5.0 percent state hotel tax are divided between regional tourism districts, municipalities and the state. Rhode Island law establishes a total of eight tourism districts; seven of these districts include designated municipalities and the eighth district encompasses any remaining municipalities not included in one of the first seven districts. Table 1 illustrates the distribution of hotel tax revenues collected in each part of Rhode Island based on the physical location of the hotel. For example, hotel tax revenues generated by a hotel located in Providence are divided such that 31.0 percent of revenues are provided to the local Providence tourism council, 23.0 percent are provided to the Greater Providence-Warwick Convention and Visitors’ Bureau, 25.0 percent are provided to the city of Providence and 21.0 percent are deposited in the state General Fund.

Table 1
Current Rhode Island Hotel Tax Distribution

Region	Regional Tourism District	Prov./Warwick Visitors Bureau	Cities & Towns	General Fund
Warwick	31.00%	23.00%	25.00%	21.00%
Providence	31.00%	23.00%	25.00%	21.00%
Statewide*	-	7.00%	25.00%	68.00%
Aquidneck Island	47.00%	7.00%	25.00%	21.00%
All Other Districts	47.00%	7.00%	25.00%	21.00%

*All communities that are not part of a regional tourism district.
Source: Rhode Island General Laws

The Governor’s proposal would decrease the share of state hotel tax revenue provided to six out of the seven local tourism districts (the exception being the Aquidneck Island district) and redirecting those funds to the Rhode Island Commerce Corporation. The Greater Providence-

Warwick Convention and Visitors' Bureau would maintain its current share of the state hotel tax. In addition, the General Fund share of the state hotel tax would be transferred to the Rhode Island Commerce Corporation to implement and manage a Rhode Island Statewide Tourism and Business Marketing Campaign. Table 2 illustrates the allocation of the 5.0 percent state hotel tax under the Governor's proposal.

Table 2
Proposed FY 2016 Rhode Island Hotel Tax Distribution

Region	Regional Tourism District	Prov./Warwick Visitors Bureau	Cities & Towns	Commerce Corp.*
Warwick	15.00%	23.00%	25.00%	37.00%
Providence	15.00%	23.00%	25.00%	37.00%
Statewide**	-	7.00%	25.00%	68.00%
Aquidneck Island	47.00%	7.00%	25.00%	21.00%
All Other	25.00%	7.00%	25.00%	43.00%

*General Fund share to RI Commerce Corporation
 **All communities that are not part of a regional tourism district.
 Source: State Budget Documents

The Governor's original proposal broadened the definition of "hotel" under the state hotel tax to include lodging in unlicensed houses, condominiums, apartments and other residential units. This would include small Bed and Breakfast facilities with fewer than three rooms and room rentals bundled with other amenities. Furthermore, the proposal narrows the definition of "occupancy" to exempt rentals for 30 or more days or for at least one calendar month from the hotel taxes. Additionally, the Governor's proposal would extend the state and local hotel taxes and state sales tax to the price markup added by room resellers (such as Priceline.com or Expedia.com). A budget amendment was subsequently submitted that proposes further amending the definition of "hotel" to include any facility offering a minimum of one room for rent as well as to include travel packages under the hotel tax. The amendment exempts homes rented in its entirety from the 5.0 percent state hotel tax, making short-term vacation home rentals subject to sales and local hotel tax.

Approximately \$2.2 million would be realized by redirecting hotel tax proceeds currently provided to local tourism districts and \$3.8 million would be realized from the hotel tax that previously was deposited in the General Fund, totaling \$6.0 million in new revenues for the Commerce Corporation. Extending the state hotel tax to include unlicensed lodging facilities and room resale would generate an additional \$0.4 million in revenue. In total, the Commerce Corporation would receive a total funding increase of \$6.4 million from the proposed changes. These revenues would be used to fund a proposed \$4.5 million tourism marketing campaign and \$1.0 million business marketing campaign, as well as other programs administered by the Commerce Corporation.

In FY 2015, Rhode Island spent slightly under \$7.0 million on all tourism efforts, both statewide and regional. Of that, approximately \$450,000 was spent on statewide efforts. In FY 2016, the Governor proposes to spend \$5.5 million of the redirected and new revenues on a dedicated statewide tourism campaign. This represents approximately a \$4.0 million increase in statewide tourism and marketing efforts. In addition, the Governor’s proposal would require that the regional tourism districts incorporate the state’s marketing campaign in their efforts in order to receive their share of the state hotel tax.

Article 29: Commerce Corporation and Economic Development

Article 29 contains 15 distinct programs, 12 of which are economic development programs or initiatives, two are education-related programs, and one program relates to inspections of projects receiving state incentives. The Governor’s proposed economic development initiatives included in Article 29 are:

- State Inspections of Commerce Corporation projects (Section 1);
- Rebuild Rhode Island Tax Credit (Section 3);
- Rhode Island Tax Increment Financing (Section 4);
- Tax Stabilization Incentive Program (Section 5);
- First Wave Closing Fund (Section 6);
- I-195 Redevelopment Project Fund (Section 7);
- Small Business Assistance Program (Section 8);
- Competitive Student Loan Reimbursement Fund (Section 9);
 - Competitive Student Loan Reimbursement Fund
 - Education Partnerships
- Main Street Rhode Island Streetscape Improvement Fund (Section 10);
- Innovation Initiative (Section 11);
 - Innovation Voucher Program
 - Innovation Network Program
- Industry Cluster Grants (Section 12); and
 - Startup and Technical Assistance Grants
 - Competitive Program Grants
- Anchor Institution Tax Credit (Section 13).

Several of the proposed programs and initiatives have different thresholds and requirements for projects undertaken in a “Hope Community.” In the Governor’s original budget submission, a “Hope Community” was defined as “a community where family poverty levels exceed the state median” and specified that these communities would include Providence, Central Falls, West Warwick, Pawtucket and Woonsocket upon passage of the budget. On April 15th, the Governor submitted a budget amendment to Article 29 that alters the definition to read, “a community

where family poverty levels exceed the most recent estimate by the U.S. Department of Commerce, Bureau of the Census, of the state median.”

Many of the programs proposed in the Governor’s budget are financed through a restructuring of a portion of the state’s existing General Obligation debt. The proposed debt restructuring, which would produce savings of \$83.9 million available to the state in FY 2016 and FY 2017, is discussed in greater detail later in this report. Table 3 provides a summary of the economic development initiatives included in Article 29.

Section	Program Title	Description	FY 2016 Cost*	FY 2017 Cost*
1	State Inspections	1. Modifies RI Commerce Corp. Board of Directors; 2. Projects receiving incentives from RI Commerce Corp. are only subject to state building/fire codes and inspections by state officials	\$ 0.3	\$ 0.3
2	Tax Incentive Reporting	Authorizes Secretary of Commerce to promulgate rules & regulations establishing reporting requirements for recipients of certain state incentives	\$ -	\$ -
3	Rebuild RI Tax Credit	Establishes tax credit worth 20% to 30% for real estate projects of at least 25,000 square feet with project costs of at least \$5.0 million and including at least 25 jobs	\$ -	\$ 12.1
4	Tax Increment Financing	Establishes a statewide Tax Increment Financing (TIF) program reimbursing developers for up to 30% of project costs from new tax revenues resulting from the development	\$ -	\$ -
5	Tax Stabilization Incentive	Reimburses municipalities up to 10% of property taxes lost from entering into tax stabilization agreements	\$ -	\$ 0.6
6	First Wave Closing Fund	Provides funding to ensure that certain transactions critical to the state are completed	\$ 5.0	\$ -
7	I-195 Redevelopment Project Fund	Provides funding to promote the development of the former I-195 land	\$ 25.0	\$ -
8	Small Business Assistance Program	Establishes a fund to allow businesses with fewer than 200 employees to gain access to capital	\$ 5.5	\$ -
9	Student Loan Reimbursement Fund	Creates a competitive student loan reimbursement fund for graduates in STEM fields	\$ 2.7	\$ 2.7
10	Main Street RI Streetscape Improvement Fund	Provides funding for improvements to streetscapes such as sidewalks, signage and lighting	\$ 1.0	\$ 1.0
11	Innovation Institute	Establishes a program providing funds for businesses with fewer than 500 employees to purchase research assistance from the state's higher education institutions	\$ 1.0	\$ 1.0
12	Industry Cluster Grants	Provides funding to support activities within industry clusters and to close cluster gaps	\$ 0.8	\$ 1.3
13	Anchor Institution Tax Credit	Establishes a tax credit for businesses that convince other businesses in their supply chain to relocate operations to RI	\$ 1.8	\$ 3.9
Total Article 29 Expenditures			\$ 43.1	\$ 22.9

*General Revenue Expenditures only; in \$ millions
SOURCE: State Budget Documents; House Fiscal Office; Senate Fiscal Office

Article 29, Section 1

Commerce Corporation Organizational Reforms; Inspections of Projects Receiving State Incentives

The Governor has proposed modifying the organizational structure of the Rhode Island Commerce Corporation. In Section 1 of the Article 29 budget amendment, the Governor proposes changing the structure of the Commerce Corporation Board of Directors by replacing the Governor as chairperson with the Secretary of Commerce, who currently serves concurrently as Executive Director, and creating a distinct Executive Director position. The amendment also replaces the Executive Director on all boards and commissions with the Secretary of Commerce, but permits the Secretary to send a designee on his or her behalf. In addition, the proposed change would allow the governor to remove members of the Board at will; current law only allows removal for “just cause.”

Section 1 also proposes changes to the inspections process for Commerce Corporation projects or other projects receiving state incentives administered by the Commerce Corporation. Under the Governor’s proposal, these projects would only be subject to the state building and fire codes. Additionally, all inspections of projects to ensure compliance with these codes would be conducted by the state building commissioner and state fire marshal.

Article 29, Section 2

Tax Incentive Reporting

Section 2 adds additional reporting requirements to the Secretary of Commerce for any person or entity that receives a business tax credit, modification and/or incentive under any provision of the general laws. The budget amendment submitted by the Governor subsequently specified that only recipients of five tax credits would be subject to the proposed requirements: the Manufacturing Investment Tax Credit, High Performance Manufacturing Tax Credit, High Performance Tax Credit, Research and Development Property Tax Credit and Research and Development Expenses Tax Credit. The Secretary of Commerce, through rules and regulations, would define the type of information that would be required and the procedure for collecting it as well as the consequences for not providing it in a timely manner. The Governor’s proposal also specifies that failure to provide requested information within 60 days could result in a suspension or denial of the incentive that a person or business was receiving.

Article 29, Section 3

Rebuild Rhode Island Tax Credit

Section 3 proposes the Rebuild Rhode Island Tax Credit, which would provide tax credits to projects of \$5.0 million or more where the applicant has committed capital investment or equity not less than 20.0 percent of the total cost of the project, but where a financing gap still remains

and would prevent the project from being undertaken if tax credits were not provided. The Commerce Corporation may lower the project floor below \$5.0 million if a project is located in a Hope Community. Projects eligible for tax credits are:

- New or rehabilitated commercial real estate projects (of at least 25,000 square feet and containing 25 full-time employees after construction);
- Multi-Family residential projects (of at least 20,000 square feet and having at least 20 residential units in a Hope Community); or
- Mixed-use projects (of at least 25,000 square feet).

The tax credits would be valued at the lesser of 20.0 percent of the cost of the project or the amount needed to close the financing gap, after taking into consideration all other forms of public and private funding sources available to the project. In addition, projects would be eligible for a higher level of credit, an additional 10.0 percent, or up to 30.0 percent of the total cost of the project, if they fall into one of the following categories:

- Rehabilitation of a historic property;
- Targeted industry clusters;
- Located in a transit area;
- Residential projects that include at least 20.0 percent affordable housing;
- Industrial property remediation; and
- Business facilities that meet environmental or sustainability standards, such as LEED.

The Governor proposes using \$12.1 million the proposed debt restructuring to finance the Rebuild Rhode Island Tax credits in FY 2017. No funds have been allocated for FY 2016 because the Commerce Corporation believes that it is unlikely that projects could be completed and receive a certificate of occupancy issued during FY 2016. The Commerce Corporation estimates that this program would result in a minimum financial commitment of \$60.0 million by the state over 5 years. The Commerce Corporation also estimates that the \$60.0 million in state investment could yield an estimated \$300.0 million in total investment, if the per project value of the credits equals 20.0 percent of the total project cost.

Tax Credits under the proposed program are intended to be transferable, would carry forward for a period of 5 years and would be refundable at 90.0 percent of their value. In addition, the Rhode Island Commerce Corporation may grant awarded projects exemption from state sales and use taxes. Credits would not be awarded until the project has been completed and a certificate of occupancy has been issued.

The proposed article requires the Rhode Island Commerce Corporation to consult with the Department of Administration to determine the annual amount of credits available for the program based on the State's "revenue capacity" as determined by an analysis performed by the Office of Management and Budget and the Department of Revenue. The Commerce Corporation

would not be authorized to issue credits if the Department of Administration determined that the credits would exceed the existing and anticipated revenue capacity of the state.

Section 3 also directs the Commerce Corporation to promulgate rules and regulations regarding implementation of the Rebuild Rhode Island Tax Credit program. These regulations would include, but are not limited to:

- An identification of specific targeted industries;
- The specific delineation of incentive areas;
- The development of an application process for those seeking tax credits;
- An application review process conducted by the Office of Management and Budget and the Department of Revenue indicating the fiscal impact that the project would have on the state's budget; and
- Procedures for the reduction of a tax credit award if a commercial project fails to meet the minimum jobs threshold.

The Rhode Island Commerce Corporation provided examples of programs similar to the Rebuild Rhode Island Tax Credit proposal that exist in other states. The following summarizes the elements of the programs (available in Connecticut and New Jersey) that were used to develop the Rebuild Rhode Island Tax Credit program.

- **The Urban and Industrial Site Reinvestment Tax Credit (Connecticut)** is a discretionary program providing dollar-for-dollar transferable corporate tax credits up to 100.0 percent. The program requires a capital investment of \$20.0 million but lowers this requirement to \$5 million in distressed areas.
- **Historic Tax Credit Program (Connecticut)** provides a transferable credit of 20.0 percent of eligible project costs or 25.0 percent if affordable housing is included.
- **Enterprise Zone (Connecticut)** provides a 10-year tax credit equal to the portion of corporate business tax directly attributed to relocation, expansion or project renovation. The state provides towns with partial reimbursement of reduced tax abatement revenue.
- **Economic Redevelopment and Growth Program (New Jersey)** provides for transferable tax credits as an incentive for projects that have demonstrated insufficient revenues to provide a reasonable developer return. The credit can be assigned to lenders for project financing for an amount from 20.0 to 30.0 percent of project cost. Eligible projects require equity participation of at least 20.0 percent.

This section defines a project “financing gap” as in all other sections of Article 29 and specifies that Rhode Island Commerce Corporation shall be responsible, through rules and regulations, for further defining what constitutes a financing gap. The section also defines a financing gap as the

amount of funding that Rhode Island is required to invest in a project to gain a competitive advantage over an alternative location in another state.

Article 29, Section 4

Tax Increment Financing

The Rhode Island Tax Increment Financing Act of 2015, as included in Section 4, establishes a statewide tax increment financing (TIF) program. The program is designed to be revenue neutral and requires no funding in the FY 2016 proposed budget or in the outer years. Under the proposal, qualified projects could receive up to 30.0 percent of the total cost of the project from the net new revenues generated by the project so long as that amount does not exceed 75.0 percent of the newly generated revenue. This would reserve at least 25.0 percent of the newly generated revenue for the state. A project could then use the revenue pledged by the TIF to secure financing for the project either through private bonds or through revenue bonds issued by the Rhode Island Commerce Corporation. Revenue generated from taxes on income, sales and use, insurance companies, banks, public service corporations, business corporation taxes, and any tax realized from venue ticket sales or parking taxes as may be established and levied under state law are eligible to be considered in state tax increment financing agreements.

The definition of incremental revenue includes (i) “net new revenue” which is defined by the Commerce Corporation, in consultation with the Department of Revenue and (ii) “existing revenue at substantial risk of loss to the State of Rhode Island” as defined by the Commerce Corporation in consultation with the Department of Revenue.

The Rhode Island Commerce Corporation provided RIPEC with examples of similar programs in other states. The following section summarizes the elements of programs (available in Massachusetts, Connecticut and New Jersey) that were used to develop the Tax Increment Financing Program.

- **The Massachusetts I-Cubed** program provides financing to certified economic development projects. Projects are only eligible if it is determined that the project would not have happened or would not achieve the contemplated level of development, jobs or other economic activity without the program.
- **Connecticut TIF** is a discretionary program that supports large-scale development projects that generate significant hotel and sales tax to the State. A developer can receive up to 30.0 percent of new incremental taxes generated by the project.
- **New Jersey ERG** program uses a TIF structure for commercial projects (hotel, retail and mixed use) that generate new incremental tax revenues, primarily sales tax. Tax reimbursements are 20.0 to 40.0 percent of project cost utilizing a bonus system based on

economic development criteria to earn up to the 40.0 percent maximum. Annual reimbursements are based on 75.0 percent of annual State tax generated by the project.

Article 29, Section 5 Tax Stabilization Incentive

The Tax Stabilization Incentive program is designed to encourage municipalities to enter into tax stabilization agreements with projects of at least \$10.0 million (unless located in a Hope Community¹) and result in the creation of at least 50 new full-time jobs, result in at least 20 residential housing units (of which at least 20.0 percent are affordable or workforce housing) or results in the adaptive reuse of a historic structure. Under this program, municipalities would receive no more than 10.0 percent of the foregone tax revenue for the term of the agreement, which may not be longer than 20 years. Total program reimbursements made by the Commerce Corporation may not exceed the lesser of 10.0 percent of qualifying foregone tax revenue or the annual appropriation made to support the program. No funding is proposed for the program in FY 2016; \$0.6 million in general revenue is proposed for FY 2017.

Article 29, Section 6 First Wave Closing Fund

Section 6 recommends using \$5.0 million of the \$64.5 million in funds made available in FY 2016 from the proposed debt restructuring for the creation of a “First Wave Closing Fund.” The fund is intended to “promote the retention and expansion of existing jobs, stimulate the creation of new jobs, attract new business and industry to the state, and stimulate growth in real estate developments and/or businesses that are prepared to make meaningful investments and foster job creation in Rhode Island” and would be administered by the Rhode Island Commerce Corporation to provide “lynchpin financing unavailable from other sources, bringing to closure transactions that are of a critical or catalytic nature for Rhode Island’s economy and communities.” Awards may take the form of a loan or grant and may be used for:

- Working capital, equipment, furnishing, or fixtures;
- The construction, rehabilitation, or purchase of real property;
- As permanent financing; or
- Other such purposes that the Rhode Island Commerce Corporation approves.

The section requires that the Commerce Corporation take into consideration the overall economic impact of the proposed recipient and project, the amount of a project financing gap, strategic importance of the project, quality and number of jobs produced, the industry that would

¹The Commerce Corporation may lower the project floor if the project occurs in a Hope Community. Qualifying projects in a Hope Community would require a capital investment by the developer of \$5.0 million and result in the creation of at least 25 new full-time jobs.

be impacted and competitive offers from other states or countries when making award decisions. Under this section, the Commerce Corporation is required to publish a report that contains information on the commitment, disbursement, and use of funds allocated under the program and, to the extent possible, track the economic impact of projects that have been completed using the fund.

Article 29, Section 7

I-195 Redevelopment Project Fund

Section 7 recommends using \$25.0 million of the \$64.5 million from the proposed debt restructuring for the establishment of a “I-95 Redevelopment Project Fund.” The fund would be administered by the I-195 Redevelopment District Commission and approval for funding would be determined by the Commission and require the concurrence of the Secretary of Commerce. The fund is established with the stated goal “to promote the development and attraction of advanced industries and innovation on and near the I-195 land in order to enhance Rhode Island’s economic vitality.” The 195 Commission may use funds to support capital investment requirements for anchor institutions or other catalytic projects, to fill a project’s financing gap, to acquire nearby land, and to construct public infrastructure and facilities (including transportation, parks, greenways, performance venues, and community facilities when making award decisions. The section specifically prohibits the use of funds to finance a sports stadium or other facility used primarily for sporting activity.

The Rhode Island Commerce Corporation provided RIPEC with examples of similar programs in other states. The Commerce Corporation cites the Roosevelt Island/Cornell University Applied Sciences Campus in New York City as the most relevant example of a program that the state seeks to emulate. In that project, New York City partnered with Cornell to build a two-million square foot applied science and engineering campus on Roosevelt Island. To facilitate the agreement, New York City provided access to city-owned land and up to \$100.0 million in city capital as well as a 99-year lease for the site on Roosevelt Island with an option to purchase the land at the end of the lease. Cornell supported the project through the use of a \$350.0 million gift received from an anonymous donor.

Under this section, the 195 Commission is directed to publish a report on the use of the fund at the end of each fiscal year detailing the commitment, disbursement, and the use of funds allocated under the fund and, to the extent possible, track the economic impact of projects that have been completed using the fund. Current legislative language does not place a limit on the amount of funding that can be provided to a single project or initiative.

Small Business Assistance

Article 29, Section 8

Section 8 proposes using \$5.5 million of the \$64.5 million from the proposed debt restructuring to establish a “Small Business Capital Access Fund” to be administered by the Rhode Island Commerce Corporation or partner lending organizations chosen through a competitive process. The intent of the program is to “assist small businesses that encounter difficulty in obtaining adequate credit or adequate terms for such credit.” Financial awards made through the program may take the form of traditional loans or conditional grants.

In utilizing funds made available for the program, the Rhode Island Commerce Corporation is required to consider: 1. Financing programs for companies that require capital outside of conventional senior debt or equity financing channels, 2. Direct lending of subordinated and mezzanine debt, 3. Collateral support in the form of credit enhancement, 4. Pledge of cash collateral accounts to lending institutions to enhance collateral coverage of individual loans, and 5. Technical assistance to small businesses. Additionally, ten percent of the program funds will be deployed as “micro-loans” ranging in size from \$2,000 and \$25,000, to businesses with less than 200 employees and difficulty obtaining financing from traditional lenders.

Information provided by the Commerce Corporation provided to RIPEC indicates that state funding is intended to leverage private funding sources and encourage financial institutions to increase lending throughout the state. The Commerce Corporation believes if all program funding is deployed in conjunction with the Small Business Administration program, state funds could account for 15.0 percent to 20.0 percent of an individual loan amount and create an additional \$20.0 to \$25.0 million in bank lending. Participating lenders must submit annual reports to the Commerce Corporation detailing the number of program loans made, the amount of program funding used for loans, the use of loan proceeds by the borrowers, the number of jobs created or retained, a description of the economic development generated, and the status of each outstanding loan.

Article 29, Section 9

Competitive Student Loan Reimbursement Fund

Section 9 would establish a Competitive Student Loan Reimbursement Fund that would be administered by the Rhode Island Commerce Corporation. The purpose of the Fund is to reimburse recent graduates earning an associate, bachelor or graduate degree in environmental science, computer technology, engineering or medicine for up to 100.0 percent of loan repayment expenses for a period of four years. To be eligible for an award through the program, an individual must reside in Rhode Island throughout the four-year period and work at least 35 hours per week for an employer in the state. Additionally, at least two-thirds of the awardees

annually must be permanent residents of Rhode Island or have attended an institution of higher education in Rhode Island. The Fund would be capitalized using \$1.8 million in general revenues in FY 2016.

Section 9 also would establish a second program within the Commerce Corporation designed to support partnerships between high schools, the Community College of Rhode Island, other institutions of higher education and employers to offer courses leading to high school diplomas and associate degrees. Funds from the program could be used to establish partnerships between the institutions, hire coordinators, compensate instructors and administrators, purchase books or other supplies, underwrite coursework and for other educational expenses. The program would be funded with \$0.9 million in general revenues in FY 2016.

Article 29, Section 10

Main Street Rhode Island Streetscape Improvement Fund

Section 10 proposes using \$1.0 million of the \$64.5 million from the proposed debt restructuring for a “Main Street Rhode Island Streetscape Improvement Fund.” The program would provide loans, matching grants and other forms of funding for improvement of streetscapes including enhanced sidewalks, wayfinding signage, upgraded building facades, improved lighting and other initiatives in support of creating an attractive environment for small businesses to develop. The fund will be administered by the Rhode Island Commerce Corporation, which will develop rules and regulations regarding loan and grant amounts, including criteria for awards, on a rolling basis.

Article 29, Section 11

Innovation Initiative

Section 11 proposes using a total of \$1.0 million – \$0.5 million from the \$64.5 million from the proposed debt restructuring and \$0.5 million in requested general revenue appropriations – for an “Innovation Initiative.” The program is intended to foster innovation in small businesses and increase demand for technological services. The Initiative, which consists of an “innovation voucher program” and an “innovation network program,” would be administered by the Rhode Island Commerce Corporation.

The innovation voucher program would allow small businesses with fewer than 500 employees to apply for awards valued between \$5,000 and \$50,000 to be used to purchase research and development support (R&D) from Rhode Island institutions of higher education or other providers. Eligible services would include research, technological development, product development, commercialization, market development, technology exploration and improved business practices. The program would be funded with \$0.5 million in FY 2016.

The proposed innovation network program would provide matching grants to nonprofits, for-profits, universities or co-working space operators that offer technical assistance, capital, or space to businesses in advanced or targeted industries. The proposal specifies that the Commerce Corporation will identify which industries qualify for grants under the program, but lists life sciences and healthcare, food and agriculture, clean technology and energy efficiency and cybersecurity as being eligible. Administered by the Rhode Island Commerce Corporation and subject to available appropriations, grants issued under this program must be matched by private sector or non-profit partners through cash or in-kind contributions.

The section requires the Commerce Corporation to produce an annual report that details the total amount, number and description of innovation vouchers and matching grants awarded and services purchased.

Article 29, Section 12 Industry Cluster Grants

Section 12 recommends using \$0.75 million of the \$64.5 million from the proposed debt restructuring to establish an “Industry Cluster Grant Fund.” In addition, \$1.3 million in funding is proposed for this program in FY 2017. The program would be administered by the Rhode Island Commerce Corporation and includes two grant subprograms financed through the Fund. The first subprogram, referred to as Startup and Technical Assistance Grants, would provide awards between \$75,000 and \$250,000 to support industry cluster activities that enable collaboration between businesses and other institutions. The Commerce Corporation is directed to determine the specific criteria for awarding grants and establish an application process for those seeking funds through the program.

The second grant program, titled Competitive Program Grants, would provide competitive awards ranging from \$100,000 to \$500,000 to support activities intended to overcome identified cluster gaps and constraints on cluster growth or to improve the effectiveness of clusters. The Commerce Corporation is directed to issue rules and regulations outlining application process for those seeking funds through the program and the criteria for awarding grants, including objective evidence of an entity’s organizational capacity, degree of internal acceptance of the proposed program, economic rationale for the proposed activity and an entity’s ability to raise funds to sustain the activity after the grant funds have been expended.

The proposal requires the Commerce Corporation to produce an annual report detailing the total amount, number and description of grants awarded, and the specific activities undertaken by recipients.

**Article 29, Section 13
Anchor Institution Tax Credit**

Section 13 proposes using \$1.8 million of the \$64.5 million from the proposed debt restructuring in FY 2016 and FY 2017 to create an “Anchor Institution Tax Credit” program. The program would award tax credits to businesses that successfully convince another business in their supply chain to relocate to Rhode Island. To be eligible for a tax credit under the program, the business that relocates to Rhode Island must employ no fewer than 10 individuals in the state in FY 2015 to FY 2018 and no fewer than 25 individuals in the state in FY 2019 and FY 2020.

Through rules and regulations, the total credit amount and criteria for award per qualifying business would be determined by the Commerce Corporation. Tax credits may be provided to qualifying businesses for a period of five years and may be used against corporate income tax. Tax credits awarded through the program are intended to be transferable and may be redeemed in exchange for payment by the state worth the full value of the tax credit, or the total value of the tax credit remaining (prorated equally over each year remaining on the term of the credit).

Program Finance

The majority of the economic development initiatives included in the Governor’s FY 2016 budget proposal are funded through a restructuring of \$160.0 million in existing state General Obligation debt. This includes many of the proposed programs located in Article 29 as well as other initiatives included elsewhere in the budget proposal. The proposed debt refinancing would result in an increase in debt service costs of \$13.6 million between FY 2016 and FY 2032, but based on current projections, would result in net present value savings of approximately \$225,000. The refinancing would provide the state with \$64.5 million in savings in FY 2016 and \$19.4 million in savings in FY 2017; across the two fiscal years, the state would have an additional \$83.9 million in funds made available.

**Table 4
FY 2016 Governor's Economic Development Investments from Debt Restructuring (\$ millions)**

Program	Allocation
First Wave Closing Fund	\$5.00
I-195 Development Fund	\$25.00
Innovation Initiative	\$0.50
Competitive Sector Grants Pilot	\$0.75
Affordable Housing Fund	\$3.00
Main Street RI Streetscape Improvements	\$1.00
Infrastructure Bank	\$2.00
Small Business Assistance	\$5.40
Anchor Tax and Other Approved Credits	\$1.80
Rhode Island School Building Authority	\$20.00
Total	\$64.45

Source: Rhode Island Office of Management and Budget

The Governor proposes using \$44.5 million of the \$64.5 million in funds available in FY 2016 to finance an Economic Development Initiatives Fund administered by the Executive Office of Commerce. This Fund would include many of the proposed programs included in Article 29 as well as an Infrastructure Bank and Affordable Housing Fund. In addition to the Economic

Development Initiatives Fund, the Governor proposes using the remaining \$20.0 million in funds to capitalize a School Building Authority Capital Fund that would finance school construction projects. The budget authorizes the Secretary of Commerce to transfer funds between any of the programs included in the Economic Development Initiatives Fund so long as notice is provided to the Director of the Office of Management and Budget and the chairpersons of the House and Senate Finance Committees.

Operating Budget

In addition to funds made available by the proposed debt refinancing and committed to specific programs, the Governor’s budget also proposes increases the Rhode Island Commerce Corporation’s budget using general revenues. In FY 2016, the Governor proposes increasing the Commerce Corporation’s operating budget to \$20.9 million, an increase of \$13.3 million from the FY 2015 revised budget. The primary sources of the increased funding are \$7.6 million in increased state appropriations, including \$3.6 million for proposed economic development programs and \$6.4 million in redirected state hotel tax revenues.

	FY 2015R	FY 2016P	Change
<i>State Appropriations</i>			
General Revenues	\$ 3.9	\$ 7.9	\$ 4.0
New Program Appropriations	-	3.6	3.6
<i>Subtotal</i>	\$ 3.9	\$ 11.5	\$ 7.6
<i>Other Revenues</i>			
Hotel Tax Revenue	-	6.4	\$ 6.4
Other Revenues	3.0	3.0	-
<i>Subtotal</i>	\$ 3.0	\$ 9.5	\$ 6.4
Total Funding	\$ 7.0	\$ 20.9	\$ 14.0

SOURCE: House Fiscal Office

RIPEC Comments

The economic development initiatives included in the Governor's FY 2016 budget proposal represent an ambitious effort to improve Rhode Island's economic climate and increase overall economic growth in the state. Rhode Island's economy has struggled to recover from the damaging impact of the Great Recession and growth remains uneven several years after the recession ended. In response, the General Assembly has enacted a number of reforms in recent years that were designed to overhaul the way that Rhode Island government approaches economic development. In relying heavily on the newly-established Executive Office of Commerce to implement many of her proposals, the Governor has chosen to embrace these reforms and leverage them to improve the state's economy.

To better understand the economic development proposals made by the Governor, it may be useful to divide them into two categories. The first category includes programs and initiatives that are intended to promote and stimulate large-scale hard assets. Programs included in this group are the I-195 Redevelopment Project Fund, Rebuild Rhode Island Tax Credit, Tax Increment Financing, Tax Stabilization Incentive Program and First Wave Closing Fund. The second category includes programs and initiatives that are intended to assist small businesses. Programs included in this group are the Small Business Assistance Program, Main Street Rhode Island Streetscape Improvement Fund, Innovation Initiative and Industry Cluster Grants. Ultimately, however, benefits from programs included in one category may also be realized by businesses in the second category.

In addition to establishing new economic development programs, the Governor also seeks to increase the Rhode Island Commerce Corporation's operating budget. The Senate Fiscal Office states that the Governor's proposed increase in state appropriations to the Commerce Corporation would result in base funding levels that the agency last received in FY 2001. Ensuring that the Commerce Corporation has sufficient resources to conduct economic development activities, including implementation of the Governor's proposed initiatives, will be an essential part of improving Rhode Island's economy.

The Governor also proposes reforming the state's visitor attraction strategy by redirecting revenues from the state hotel tax to fund a coordinated statewide tourism and business marketing campaign. A 2014 report, commissioned by the Rhode Island Commerce Corporation and produced by Nichols Tourism Group and the Radcliff Company, found that a lack of pro-active statewide marketing was having a detrimental impact and was an influencing factor on the state's declining market share of national tourism expenditures. According to the report, funding for statewide tourism efforts in Rhode Island was the least of any state in the country during FY 2013 and FY 2014. The analysis attributes \$1.8 billion of additional visitor spending that was unrealized in 2013 alone as a result of the state's loss of market share since 2007.

To reverse Rhode Island's declining tourism market share, the report recommended a stabilized \$4.0 million statewide marketing budget to position Rhode Island just above the median levels nationally. The report projects that an effective campaign funded at this level would result in approximately 500,000 to 670,000 new visits to the state and generate \$210.0 to \$280.0 million in expenditures. The report estimates that the resulting state sales and hotel tax revenue would total \$9.0 to \$12.0 million and that the new visitor spending could support an additional 2,500 to 3,300 jobs for the state.

One notable aspect of the Governor's proposal involves the use of a one-time revenue source made available through a refinancing of existing state debt to finance numerous economic development initiatives. Though we applaud the Governor for avoiding long-term funding commitments that could worsen the state's structural budget deficit, we suggested in our analysis of the FY 2016 Budget as Proposed (available [here](#)), that alternatives to the debt refinancing be considered with regards to funding the proposed economic development initiatives.

The revenue and expenditure estimates adopted at the May 2015 Revenue and Caseload Estimating Conferences (REC/CEC) have resulted in approximately \$123.7 million in additional funding being available in FY 2015 and approximately \$50.0 million available in FY 2016 (as compared to estimates from the November 2014 REC/CEC). The state should explore the possibility of using these surplus funds to pay for some, or all, of the economic development proposals made by the Governor. This would allow a potential debt restructuring to be used to reduce out-year budget deficits by reducing annual debt service costs in future years. Additionally, policymakers should be aware of the fact that several of the Governor's proposed economic development initiatives would require expenditures in the outer years.

A second area for consideration involves the checks and balances needed to protect taxpayer investments in economic development efforts. These checks and balances should include legislative oversight and reporting requirements that ensure funds allocated for the proposed programs are being used effectively. In 2013, the General Assembly included several program accountability requirements in the legislation that established the Executive Office of Commerce and reformed the Rhode Island Commerce Corporation. The law required that the Commerce Corporation establish accountability standards, reporting standards and outcome measures for each program that it administers. Although the law allows the Board of Directors to determine the precise processes, standards and measures, it does dictate certain principles that the Board must adopt:

- A set of outcomes against which the Board will measure each program's and offering's effectiveness;
- A set of standards for risk analysis for all of the programs, especially loan and loan guarantee programs; and

- A process for reporting all loans, loan guarantees and other financial commitments made through the Corporation that includes the purpose of the loan, financial data and other related information.

Rhode Island law also requires that the Department of Revenue evaluate existing tax incentives on a rotating three-year cycle, with new incentives reviewed within five years of creation, and determine both fiscal and economic results. The current law also requires that the Governor's budget submission include a recommendation as to whether each incentive should be continued, modified or ended for each incentive for which an evaluation was completed.

Over the last several years, the Government Finance Officers Association (GFOA) has explored best practices for evaluating and managing economic development incentives. Several general principles have arisen out of these efforts that are recommended for public bodies that are charged with administering incentive programs. While economic development agencies should be granted flexibility in determining what specific kinds of analyses and assessments are required for an individual project, the legislature, through statute, could mandate basic requirements.

In summary, RIPEC believes that the General Assembly should favorably consider the additional economic development tools and incentives proposed by the Governor to help Rhode Island state government become competitive in attracting and retaining businesses. Equipping the Commerce Corporation with tools that it can use to improve the state's economy and providing the resources necessary to manage these programs will allow the state to create a more competitive economic climate. This year's budget cycle, with additional financial resources available, represents an opportune time to invest in the economic capacity of the state and provide for economic growth and activity that will benefit the state and its finances for years into the future.