Minnesota Investment Fund

2018
EVALUATION REPORT

Program Evaluation Division

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

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OLA
OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA • James Nobles, Legislative Auditor

February 2018

Members of the Legislative Audit Commission:

The Legislature created the Minnesota Investment Fund (MIF) as a tool to induce new or existing businesses to add jobs and make investments in Minnesota.

The impact of the MIF program is unclear. Although many businesses that have received state subsidies have increased jobs, businesses do not have to demonstrate that they need the state's assistance to carry out their proposed projects. Without such evidence, it is plausible that some businesses that have received MIF funds would have expanded or increased hiring anyway. We recommend that the Legislature amend the law to provide greater assurance that MIF funding is necessary for individual projects.

In addition, we found that the MIF program needs more transparency and consistency. We recommend that the Legislature require the Minnesota Department of Employment and Economic Development (DEED) to establish publicly available criteria for determining when to award MIF funds, the size of the awards, and whether to require repayment of the awards.

Our evaluation was conducted by Joel Alter and David Kirchner (project managers) and Madeline Welter. The Department of Employment and Economic Development cooperated fully with our evaluation, and we thank the department for its assistance.

Sincerely,

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THE GREAT SEAL OF THE STATE OF MINNESOTA
L'ETOILE DU NORD
1858

Summary

Key Facts and Findings:

- The Minnesota Investment Fund (MIF) provides financial assistance to nonretail businesses planning to create or retain jobs. (pp. 22-23)
- MIF funding is limited to $1 million per project, and MIF funds must ordinarily be matched with funding from other sources. (p. 8)
- The Department of Employment and Economic Development (DEED) has wide discretion to administer the MIF program. (pp. 45-46)
- DEED distributes MIF funds through a two-part process; DEED first grants the money to local governments, and the local governments then loan the money to businesses. (pp. 4-5)
- MIF appropriations totaled $51 million for fiscal years 2014 through 2017, a substantial increase over previous funding levels. (pp. 13-14)
- DEED has overstated the amount of private investment leveraged by the MIF program, and its public reporting on the outcomes of MIF projects is incomplete. (pp. 34-35)
- Businesses seeking MIF funding do not have to demonstrate that they truly need state subsidies, raising questions about the impact of those subsidies. (pp. 28-29)
- DEED allowed some businesses to meet their MIF commitments by counting hiring and expenditures that occurred before they received their MIF award approvals. (pp. 62-64)
- DEED does not use consistent criteria to determine the amount of MIF loans or whether the loans will be forgiven. (pp. 52-55)
- DEED often does not require businesses to pay workers at the wage levels listed in their approved MIF applications. (pp. 57-58)
- A statute requiring MIF businesses to pay workers at least a minimum level of compensation is ambiguously worded. (pp. 59-61)
- Local governments sometimes receive money for local revolving loan funds as an outcome of the program, but these funds' purposes and value are unclear. (pp. 40-42)

Key Recommendations:

- The Legislature should require stronger assurances that MIF projects need state assistance in order to proceed. (pp. 29-30)
- The Legislature should consider restructuring the MIF program so that DEED makes loans directly to businesses, ending the creation of local revolving loan funds. (pp. 42-43)
- The Legislature should require DEED to set publicly available criteria for MIF award decisions, the size of awards, and loan forgiveness. (pp. 55-56)
- The Legislature should clarify the law requiring MIF businesses to pay a minimum compensation level to their employees. (pp. 61-62)
- DEED should require businesses to meet or exceed the employee wage levels on which the department based its MIF award decisions. (pp. 58-59)
- DEED should improve the usefulness and accuracy of its public reporting and tighten its administrative procedures. (pp. 26, 68)

The Minnesota Investment Fund has not created the level of investment DEED has claimed, and its impact on jobs is unclear.

The Legislature should require businesses to demonstrate that they truly need state assistance.

Report Summary

The Minnesota Investment Fund (MIF), administered by the Department of Employment and Economic Development (DEED), provides funding to nonretail businesses to help increase economic activity.

Businesses and local governments jointly apply for MIF funding, and can receive up to $1 million per project. In nearly all instances, businesses agree to increase employment in order to receive a MIF award. By law, MIF funding is ordinarily limited to 50 percent of a project's total cost.

After several years of little or no funding, legislative appropriations for the MIF program increased substantially starting in Fiscal Year 2014. Appropriations totaled $51 million for fiscal years 2014 through 2017.

In preliminary conversations, DEED staff encourage promising applicants and discourage those that appear unlikely to meet program expectations. Consequently, DEED has approved every MIF application it has formally scored in the last 15 years.

After approval of a MIF application, DEED grants money to the local government, which in turn loans the money to the business. DEED approves the terms of each loan and the requirements each business must meet.

Although the MIF program provides "loans" to businesses, DEED made 74 percent of the MIF loans awarded in fiscal years 2013 through 2017 partially or totally forgivable. When a loan is forgivable, the business does not have to repay the loan if it meets its hiring and wage commitments.

DEED made 138 MIF awards in fiscal years 2008 through 2017, totaling $65.9 million. However, 33 of these projects (involving $14.4 million in awards) were later cancelled.

The MIF program's impacts are unclear because businesses do not have to demonstrate they need the assistance in order to expand.

The MIF program's primary statutory purpose is to create jobs and foster business investment. However, while some MIF awards have likely contributed to job growth, the impact of others is questionable. In the MIF applications we reviewed, businesses typically provided unconvincing explanations about why they needed state assistance. For example, businesses rarely documented that they were unable to obtain private financing or had received competing subsidy offers from other states.

The Legislature should require businesses to demonstrate they need public assistance before receiving MIF funding. Businesses should demonstrate that, without state funding, (1) the business would not have access to sufficient funding to proceed with the project, or (2) the business would pursue the project outside of Minnesota.

DEED's public reports of investments and jobs created through the MIF program are incomplete and sometimes inaccurate.

DEED has publicly estimated that the MIF program leveraged $2.1 billion in private investment from 2013 through 2017. But $1.15 billion of this amount is from a single project, where DEED has inappropriately taken credit for a corporate merger that occurred months before a MIF application was submitted.

We also found inaccuracies in the numbers of jobs a DEED website attributed to the MIF program. In one instance, DEED's website said a project was projected to create 160 jobs when the business actually promised to create only 10.

Local governments help administer the MIF program, but the value of their involvement is questionable.

Local governments play a dual role. They are initially applicants to the MIF program, working together with businesses. But they also fulfill a number of administrative functions, including analyzing the financial health of the business, developing legal contracts, monitoring compliance, and handling financial transactions.

For most local governments, MIF projects occur infrequently. More than half of the 300 cities that have had a MIF project have had only one in the entire history of the program.

As a result, most local government staff have minimal knowledge of a program they are expected to help administer. Some local officials told us they were confused about their responsibilities and that DEED has not always been helpful.

Some local officials told us they acted simply as go-betweens, facilitating communication between DEED and businesses. Principal decisions were made by DEED staff.

When MIF loans are repaid, local governments may keep a portion of the repayments. State law contains no requirements for how local governments may use these repayments. However, DEED has administratively required local governments to use MIF repayments to create local revolving loan funds.

These local revolving funds are often underutilized. We surveyed local governments that had created such funds as a result of MIF projects. Forty-four percent of respondents said that they had never used their funds in the past decade, and an additional 15 percent said they had used them only once.

Involving local governments in MIF awards is unnecessarily complicated and provides minimal benefits. The Legislature should consider streamlining the MIF program so that DEED makes loans directly to businesses. Under this approach, all repayments would be recycled back into DEED's program funds, instead of sitting in local revolving loan funds that are often unused.

DEED's process for making MIF awards is not transparent and does not use consistent criteria.

DEED makes three key decisions regarding potential MIF projects: (1) whether a business should receive a MIF award, (2) how large a loan the business should receive, and (3) whether to forgive the loan.

State statutes offer little guidance for how DEED should make these decisions, implicitly granting DEED wide discretion.

DEED scores each application using department-created scoring criteria, but these criteria are easy to meet. Businesses receive many points for rather modest accomplishments. For example, any project projected to create at least 10 jobs receives the maximum possible points for job creation. DEED staff have also been generous in giving points to applicants for qualitative factors, such as the economic vulnerability of the local community.

DEED staff rarely document their reasoning for the size of MIF loans or decisions regarding loan forgiveness. They make decisions regarding MIF projects on a case-by-case basis, with little apparent consistency from one project to the next. DEED does not

The Legislature should consider reducing the role of local governments in Minnesota Investment Fund projects.

DEED's administration of the Minnesota Investment Fund program has been lax.

publicly explain how applications are scored or how award sizes are determined.

The Legislature should place greater limits on DEED's discretionary authority. Specifically, it should require DEED to set specific, publicly available criteria for MIF award decisions, the size of awards, and loan forgiveness.

DEED has not required businesses to pay workers the wages proposed in their approved MIF applications.

Businesses applying for MIF loans propose to create (or retain) a certain number of jobs at specific wage and benefit levels. DEED takes into account the average wage levels listed in applications when making decisions about awards, award size, and loan forgiveness.

However, when businesses sign the loan agreements that formally require them to meet certain commitments in order to receive state assistance, they usually do not promise to meet these wage levels. Instead, these DEED-approved agreements require workers to be paid at or above a much lower minimum rate. Over the past ten years, 60 percent of loan agreements have required businesses to pay a lower wage level than the originally proposed wages.

A law requiring businesses in the MIF program to pay workers at least a minimum compensation level is poorly worded.

State law requires that businesses participating in the MIF program pay their employees wages and benefits equal to at least 110 percent of the federal poverty guideline for a family of four. As written, the law could be interpreted to apply to all of a business's employees, although DEED enforces it only for new employees associated with the MIF project.

Further, the law does not clearly state whether DEED should enforce a minimum for *hourly* compensation ($13.01 per hour in 2017) or *annual* compensation ($27,060 per year in 2017). If the latter interpretation is used, it would be more difficult for businesses to use part-time employees to meet their MIF hiring obligations, a practice DEED has allowed.

It is also unclear to what extent DEED should require businesses to increase employee compensation each year as needed to keep pace with annual changes in the federal poverty guidelines. The Legislature should clarify the law.

DEED should improve its procedures for ensuring that businesses meet their commitments.

The department allowed some businesses to meet their commitments by counting hiring and expenditures that occurred before they received MIF awards. In some instances, businesses were credited for expenditures or hiring they made before they had even applied for MIF funding.

Further, DEED's files do not contain sufficient information to show that businesses have met their commitments under the MIF program. Monitoring reports have sometimes provided insufficient documentation of businesses' required activities. For example, reports may show all new employees hired but not indicate how many workers left employment during the same reporting period.

Generally, DEED should tighten its administrative procedures for the MIF program.

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THE GREAT SEAL OF THE STATE OF MINNESOTA
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Introduction

The Minnesota Investment Fund (MIF) is one of the state's primary economic development programs. Through this program, the Department of Employment and Economic Development (DEED) loans money to individual businesses to foster economic activity. DEED partners with local governments to administer this program, and local governments can retain a portion of MIF loan repayments.

The MIF program has existed since 1996 but has never previously been evaluated by our office. In April 2017, the Legislative Audit Commission directed the Office of the Legislative Auditor to evaluate the MIF program; state law requires that we evaluate at least one economic development incentive program each year.[1] In our evaluation, we addressed the following questions:

- **What have been the impacts of the Minnesota Investment Fund, particularly on jobs and wages?**

- **To what extent have local governments used local revolving loan funds seeded with Minnesota Investment Fund loan repayments, and for what purpose?**

- **How well does DEED administer the Minnesota Investment Fund? Does DEED have a clear basis for making project awards and determining whether loans need to be repaid?**

To conduct our evaluation, we reviewed applicable state laws and rules and closely examined DEED's internal MIF policies and procedures. We conducted interviews with DEED program administrators. We scrutinized both DEED's public reports regarding MIF outcomes and internal data that are not ordinarily released to the public. We also reviewed state accounting information regarding Minnesota Investment Fund revenues and expenditures.

In addition, we selected a random sample of 60 projects that received MIF awards between fiscal years 2012 and 2016, and systematically examined all documents in DEED's files related to these projects.[2] Additionally, for *all* awards made in fiscal years 2008 through 2017, we reviewed (1) DEED's project "review summaries" (used by the commissioner when making final award approvals) and (2) the loan agreements specifying the commitments made by businesses to receive MIF funding. To supplement our file reviews, we conducted site visits to 11 cities and 1 county to discuss MIF projects. As part of these visits, we sometimes spoke with representatives of businesses that had received MIF loans.

Using internal DEED data, we identified local governments that had received MIF awards since 1996 and appeared likely to have received MIF loan repayments. We sent each government entity a questionnaire to determine whether they still had the local revolving loan funds created using those repayments. If they did, we asked how these funds have

[1] *Minnesota Statutes* 2017, 3.9735, subd. 2.

[2] We chose not to include awards made in Fiscal Year 2017 in our sample to reduce the number of projects for which no project activity or DEED monitoring had yet occurred.

been used. We received 110 responses to the 112 questionnaires we sent (a 98 percent response rate).

Finally, we obtained and analyzed unemployment insurance data reported by all companies that have participated in the MIF program since 2008. However, as we discuss in Chapter 3, we found it difficult to draw firm conclusions from these data because of incomplete reporting.

Our evaluation focused on the state-funded MIF business subsidy program. Two other programs use the "Minnesota Investment Fund" name: a federally funded program (sometimes called the "federal MIF" program), and a disaster relief program. We did not evaluate these other programs.

Chapter 1: Background

The Minnesota Investment Fund (MIF) program provides financial assistance to selected nonretail businesses to help increase economic activity.[1] The 1996 Legislature created the MIF program as a successor to the Economic Recovery Grant program.[2] As used by the Department of Employment and Economic Development (DEED), the MIF program primarily seeks to foster job growth and business investment.

This chapter provides background information about the MIF program. We discuss how the program is administered and what happens over the duration of a MIF project. We examine the MIF program's key revenue sources and how the program's financial balances have changed in recent years. Finally, we review some general characteristics of recent MIF projects, such as where in Minnesota they have occurred.

Key Findings in This Chapter

- DEED provides MIF funds to businesses through a two-part process: DEED grants money to a local government, which then loans the money to a specific business.
- After several years of little or no funding, legislative appropriations for the MIF program increased substantially starting in Fiscal Year 2014.
- The Legislature has recently appropriated more money than DEED has spent, resulting in large fund balances.
- In the past five years, DEED has made the majority of MIF loans partially or fully forgivable.

Program Framework

DEED awards MIF money for specific business "projects." The law does not define "project," nor has DEED developed a formal definition. However, DEED administrators said their informal, working definition of a project is a business activity intended to foster business investment and job growth in a specific geographic location. Projects could include adding new equipment, expanding a facility, or renovating a space.

Administrative Organization

The MIF program is one of several economic development programs administered by DEED's Office of Business Finance in the agency's Economic Development Division. Office of Business Finance staff review MIF applications jointly submitted by businesses and local governments, guide local government staff through the administrative process, and monitor business performance. The office director, deputy commissioner for the division, and the DEED commissioner must approve all MIF projects.

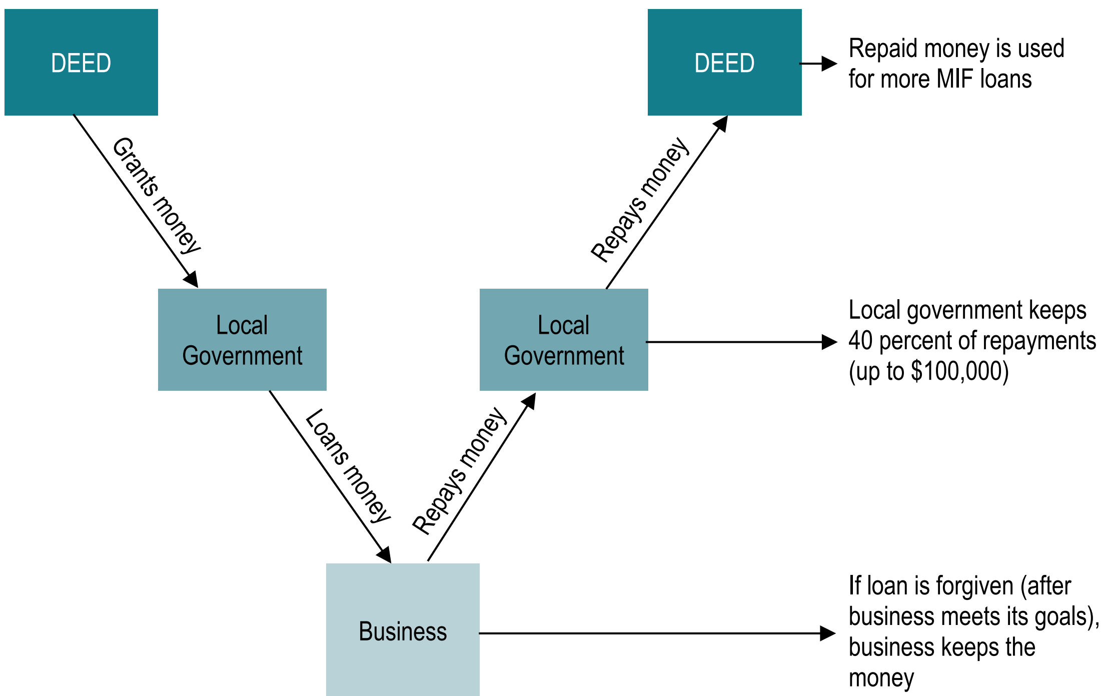
[1] DEED administers other programs called "Minnesota Investment Fund," including a federally funded program and a disaster relief program. These programs have different purposes and funding sources, and we did not evaluate them. We use "Minnesota Investment Fund" to describe only the state-funded economic development program unless otherwise noted.

[2] *Laws of Minnesota* 1996, chapter 452, sec. 29, codified in *Minnesota Statutes* 2017, 116J.8731. The Economic Recovery Grant program was created in 1984.

DEED provides MIF subsidies to businesses through a two-part process: DEED grants money to a local government, which then loans the money to the business.

DEED does not provide money directly to businesses.[3] Instead, when a MIF application is approved, DEED grants funding to a local unit of government.[4] DEED and the local government enter into a legally binding grant contract that specifies that the money is intended to assist a specific business. Then, the local government makes a loan directly to that business. When the business repays the loan, the money goes first to the lender (the local government), which then passes a portion of the repayment to DEED. Exhibit 1.1 illustrates this process.

Exhibit 1.1: The Minnesota Investment Fund Process



SOURCE: Office of the Legislative Auditor.

Thus, local governments serve dual roles. They are both (1) applicants to the program together with businesses and (2) administrators of the program together with DEED. At the start of the MIF process, the local government works with the business to develop an application. Once a project is approved, the local government carries out administrative

[3] The 2013 Legislature passed a provision allowing businesses to apply directly to DEED for a MIF loan. As of December 2017, DEED has not used this provision to make a direct loan to a business. Local governments cannot apply to DEED for MIF funding without a business partner.

[4] In most instances, the local government participant is a city, but in some instances a county or local economic development authority fulfills the local role.

tasks with DEED: it negotiates a loan agreement with the business, collects monitoring information on business progress, and handles certain financial transactions.

Local governments may keep some of the MIF loan repayments.

When a business repays a MIF loan, state law allows the local government to retain 40 percent of the repayments, up to $100,000.[5] The remainder is returned to DEED. DEED requires local governments to put the money received from repayments into a local revolving loan fund.[6] These funds must be used for the same purposes as MIF funds.[7]

Some local governments have used their revolving loan funds to support subsequent MIF projects. For example, the City of Isanti received part of the repayments from a 2008 MIF project awarded to the company Ever Cat Fuels, LLC. As the company paid off its loan, the city put its portions of the repayments into a local revolving loan fund. In 2015, Isanti committed $27,000 from this revolving loan fund to a new MIF project with the company SnoBear USA.

As we discuss later in this chapter, DEED has increasingly awarded forgivable MIF loans. Fully forgivable loans do not require repayment if goals are achieved and, as a result, do not generate revenues for revolving loan funds.

While DEED often makes the forgiveness decision, local governments can also choose to forgive (or not forgive) their portion of loan repayments. For example, DEED awarded a $370,000 MIF loan to Climatech in 2016. The City of Eden Prairie would have received $100,000 when the company repaid the loan, but it decided to forgive its portion. As a result, the company will repay $270,000 of the loan to DEED, and the city will not receive anything.

Program Eligibility

DEED has awarded MIF funds to many types of businesses. For example, recent recipients of MIF funds have included companies in areas such as meatpacking, information technology, biopharmaceutical services, and specialized welding. According to the program's administrator, DEED has primarily awarded MIF funds to projects that plan to increase employment, support higher wages in a community, promote private investment, and increase the tax base. DEED administrators also said they focus the program on businesses that generate new income to the state and could potentially locate outside the state while serving the same customers.

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[5] *Minnesota Statutes* 2017, 116J.8731, subd. 5.

[6] The law does not restrict the use of these funds and, in fact, does not require local governments to create a revolving loan fund at all. Local governments agree to these restrictions when they sign a MIF grant contract with DEED.

[7] The 2017 Legislature passed legislation giving local governments a one-time opportunity to use their local revolving loan funds for any lawful purpose after paying a 20 percent penalty to the state. *Laws of Minnesota* 2017, chapter 94, art. 6, sec. 24.

Aside from prohibiting retail projects, state law places few limits on the types of projects that are eligible for MIF funding.

There are two sets of MIF project eligibility criteria, as shown in Exhibit 1.2. First, state law specifies nine conditions for evaluating potential MIF projects. The law does not require all nine conditions to be true for a given project, nor does it weight them. A business can be eligible by meeting any one of conditions 1 through 6. The law specifies that a grant or loan cannot be made based solely on condition 7 (to retain an existing business) or condition 8 (to attract an out-of-state business).[8]

Exhibit 1.2: Minnesota Investment Fund Eligibility Requirements

State law requires that DEED evaluate potential MIF projects on their ability to do the following:

1. Create new jobs or retain existing jobs, or improve the quality of existing jobs.
2. Increase the tax base.
3. Demonstrate that investment of public dollars encourages private investment.
4. Demonstrate excessive public infrastructure or improvement costs beyond the means of the affected community and private participants in the project.
5. Provide higher wage levels to the community or add value to current workforce skills.
6. Support the development of microenterprises through financial assistance, technical assistance, advice, or business services.
7. Show whether assistance is necessary to retain an existing business.
8. Show whether assistance is necessary to attract an out-of-state business.
9. Promote or advance the green economy.

The law specifies that DEED cannot make a MIF grant or loan based solely on the existence of condition 7 or condition 8; it must also find that at least one of conditions 1 through 6 also exists.

State rules require applicants to describe how they will do at least one of the following:

1. Create or retain jobs.
2. Stimulate private investment.
3. Increase the local tax base.
4. Improve employment and economic opportunities for Minnesotans.

NOTES: "Green economy" is defined in *Minnesota Statutes* 2017, 116J.437, subd. 1, as "products, processes, methods, technologies, or services" intended to meet a number of environmental goals. Federal law defines a microenterprise as a sole proprietorship, partnership, or corporation that has fewer than five employees and generally lacks access to conventional loans, equity, or other banking services. 15 *U.S. Code,* secs. 6901-10 (1999).

SOURCE: Office of the Legislative Auditor, summary of *Minnesota Statutes* 2017, 116J.8731, subd. 4, and *Minnesota Rules* 4300.1901, subp. 2, published electronically January 18, 2005.

[8] *Minnesota Statutes* 2017, 116J.8731, subd. 4. When the ninth condition was added, the Legislature did not specify whether a project could qualify solely on the basis of that condition. *Laws of Minnesota* 2008, chapter 356, sec. 5.

Second, the law also directs DEED to make MIF eligibility decisions using its rules for federal Community Development Block Grants, as shown in Exhibit 1.2.[9] DEED uses both sets of criteria—which overlap, but are not identical—in making MIF awards.

State law prohibits the use of MIF funds for casinos, stores that are primarily used for retail sales, and professional sports facilities.[10] However, the law does not place any additional limits on the types of businesses that can receive MIF awards. The law does not suggest where projects should take place (for example, in the seven-county Twin Cities metro area versus Greater Minnesota), and businesses can receive MIF funds more than once.

The MIF program can be used for a variety of purposes, making it DEED's "workhorse" economic development program.

MIF is a flexible program that facilitates business and job growth. As a result, it is a logical program for the department to turn to when businesses look for state aid but do not meet the criteria for more narrowly defined programs.

A few key aspects of the MIF program make it attractive for many different businesses. First, businesses can apply for MIF funds at any time; applications are accepted on a rolling basis. Second, as we note later in this chapter, the program has recently had enough funding to support many projects. Third, businesses can receive MIF funding at the start of a project based on projected outcomes, as opposed to the end of a project based on actual outcomes. In some of the MIF projects we reviewed, companies wanted to use MIF funds to fill a gap in project funding or as a way to attract additional capital for their projects. For such companies, up-front payment is appealing. Finally, because the MIF program does not have a minimum job creation requirement, projects with other goals are eligible. For example, a 2016 MIF award benefitting Anchor Glass Container Corporation in Shakopee did not include a commitment to create any new jobs, but rather a commitment to retain 280 jobs.

Application Process

MIF projects can begin in multiple ways. Sometimes, local governments work with businesses to develop prospective MIF projects. In other instances, businesses initially work with DEED, which then connects the business with the appropriate local government officials. Some DEED employees work as the department's "sales staff" and promote DEED's programs (including the MIF program) to businesses looking to locate or expand in Minnesota. DEED received, scored, and approved funding for a total of 138 completed MIF applications between Fiscal Year 2008 and Fiscal Year 2017, or an average of about 14 awards annually.

Businesses and local governments submit applications jointly to DEED. The application requires details on the project, the business, and the community. For example, applicants must provide an explanation of why MIF funding is necessary, a narrative of community needs, a business credit check, and the results of the local government's financial analysis

[9] *Minnesota Statutes* 2017, 116J.8731, subd. 2.

[10] *Minnesota Statutes* 2017, 116J.8731, subds. 5 and 6.

of the project. Additionally, state rules require local governments to pass a resolution supporting the project.[11]

Because the MIF program involves the transfer of public money to for-profit entities, the program must follow the state's business subsidy law, which governs all types of state and local business subsidies.[12] The business subsidy law requires that all subsidies "meet a public purpose," and that recipients set "measurable, specific, and tangible goals."[13] DEED asks businesses to address their job and wage goals in the MIF application documents.

DEED has discretion to determine which projects to approve and how much state funding to provide.

Once DEED receives an application, state law requires it to evaluate the project using its rules for economic development projects funded by federal Community Development Block Grants.[14] These rules require that eligible projects be scored against a 600-point scale based on two major components: project design and financial feasibility.[15] The rules specify how many points can be awarded in each area (400 for project design and 200 for financial feasibility), and define a minimum passing score (400 points). Within these broad parameters, DEED has defined its own criteria and point allotments. The rules provide some definitions for each category, but the definitions are broad and could be interpreted in multiple ways.[16]

State statutes provide limited direction for determining the amount of MIF funding a project should receive. The law states that MIF loans must not exceed one-half of project costs; the remainder must be financed through company equity, bank loans, or other sources.[17] The law also sets the maximum DEED award for an individual MIF project at $1 million.[18] However, the law sets no criteria for the types of projects that may receive the maximum award or that may receive forgivable loans.

In the past 15 years, DEED has approved every MIF application it has formally considered.

According to DEED administrators, the department rarely receives MIF applications unexpectedly. In most instances, preliminary conversations take place between business representatives, local government officials, and DEED staff. These conversations may also

[11] *Minnesota Rules* 4300.1200, subp. 4(E). DEED also requires local governments to hold a public hearing.

[12] *Minnesota Statutes* 2017, 116J.993-116J.995.

[13] *Minnesota Statutes* 2017, 116J.994, subds. 1 and 3(a).

[14] *Minnesota Statutes* 2017, 116J.8731, subd. 2.

[15] *Minnesota Rules* 4300.1901, subp. 3, published electronically January 18, 2005.

[16] According to these rules, the evaluation of project design should include "an assessment of need, impact, and the capacity of the applicant to complete the project in a timely manner." Financial feasibility is "an evaluation of the effective use of program funds to induce economic development." *Ibid*.

[17] *Minnesota Statutes* 2017, 116J.8731, subd. 3. External marketing expenditures for renewable energy market development are not subject to the limitation that MIF funds pay no more than one-half of project costs.

[18] *Minnesota Statutes* 2017, 116J.8731, subd. 5. Occasionally, the Legislature designates in law an amount exceeding $1 million for specific MIF projects.

involve elected officials, consultants hired by the businesses, or regional economic development organizations. DEED staff frequently advise businesses about assistance available through various state programs and may encourage or discourage a MIF application based on their understanding of the business's circumstances, industry conditions, and project specifications.

DEED staff said the department uses these preliminary conversations to screen out potential applicants whose projects are ineligible or will not successfully pass DEED's project review process. For example, DEED staff said that they advise potential applicants seeking assistance for a retail project that such projects are ineligible for MIF under state law. Similarly, DEED staff may warn that a project that would create very few jobs may not score highly enough to receive MIF funding, and they may suggest other state programs that would be a better fit. In years when program funding was scarce, DEED staff told some potential applicants not to apply for the MIF program because the department had no funds to award.

As a result of these efforts, DEED has not formally denied a MIF application for many years.[19] Every business that has submitted an application has either received a MIF award or withdrawn from the process before DEED made an official decision.

In the past five years, DEED has made the majority of MIF loans partially or fully forgivable.

Between fiscal years 2013 and 2017, 74 percent of MIF awards included provisions for partial or total forgiveness if the business met its project commitments. Forgivable awards made up $40.1 million of the $52.7 million awarded during this period.[20] DEED has awarded partially or fully forgivable loans much more frequently over the past five years than it did in the earlier years of the MIF program, as shown in Exhibit 1.3. Even in the late 1990s, when yearly award counts were similar to those in recent years, fewer awards were forgivable. According to DEED staff, a number of factors have influenced the increase in forgivable loans, including recent increases in appropriations, the growing demand for forgivable loans by businesses due to a strong economy, consultants who have advised businesses to seek forgivable loans, and the availability of competing incentives to businesses.

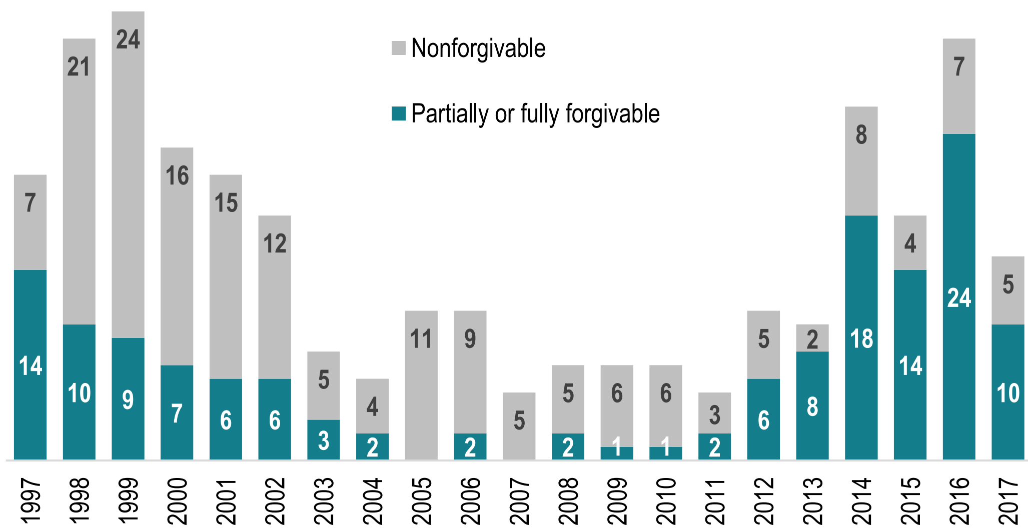
Project Management

After a business receives a MIF award, DEED and local governments administer MIF projects by (1) developing legal agreements, (2) ensuring compliance with statutory requirements, and (3) monitoring the progress of businesses toward the commitments they have made. Chapters 2 and 3 include information on how these processes work in practice.

[19] In DEED's internal data, seven projects have been marked as "denied" since 2003. At our request, DEED staff reviewed records and confirmed that all had been miscoded—the applications had been withdrawn by applicants before DEED made an official decision. (In some instances, they were withdrawn and resubmitted as new projects that were approved.) We did not ask DEED staff to review files from earlier than 2003 to determine how long it has been since DEED formally denied a MIF application.

[20] These figures include $6.3 million in forgivable awards for projects that were ultimately cancelled.

Exhibit 1.3: Number of Partially and Fully Forgivable Minnesota Investment Fund Awards, Fiscal Years 1997-2017



NOTES: Awarded projects that were later cancelled are included in this count. Also, this exhibit excludes five projects in fiscal years 2000, 2002, 2003, and 2010 for which DEED files were missing data.

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

Legal Agreements

Once the director of the Office of Business Finance, a deputy commissioner, and the commissioner approve a MIF project, DEED sends an award letter to the business and the local government. These award letters indicate the award amount but do not set the conditions of the MIF award.

DEED uses binding legal agreements to specify the conditions businesses must meet to receive MIF funding.

The two-part process involves two legal agreements. First, DEED develops a grant contract with the local unit of government. Second, the local government negotiates a loan agreement with the business. The grant contract between DEED and the local government defines the obligations of both the local government and the business. The grant contract also sets the loan terms and key project dates. DEED requires that the terms, dates, and requirements in the loan agreement between the business and the local government be generally consistent with those in the grant contract. The MIF loan agreement also contains the business subsidy agreement required by law and often includes a list of project expenses.[21]

Although it is not a party to the loan agreement, DEED must approve the final loan document. DEED will not provide funds if it disagrees with the terms of the loan agreement developed by the local government and business.

The law sets few specific requirements for business commitments. Businesses must identify job creation or retention goals, but the law does not set a minimum number of jobs per MIF project.[22] State law does mandate minimum employee compensation for all MIF projects. Businesses receiving MIF funds must pay their employees total compensation of at least 110 percent of the federal poverty guideline for a family of four on an annualized basis.[23]

Each grant contract and loan agreement is separately negotiated from project to project. As a result, requirements vary from one project to the next.

Business Requirements

In order to receive MIF funds to disburse to the business, the local government submits business invoices and payment requests to DEED. After DEED provides MIF funds to the local government, the local government provides the money to the business as reimbursement for qualified purchases. Such reimbursements can occur any time after a business completes the legal agreements and submits the necessary documentation.

Ordinarily, businesses have two years to meet MIF commitments, but the deadline can be extended for up to one year.

Generally, the business subsidy law requires businesses to meet goals within a two-year period.[24] The actual point at which this two-year period begins is supposed to be "the date that the recipient receives the business subsidy," but the law specifies different starting points for subsidies involving property improvements or equipment.[25] A business may receive a one-year extension if it needs additional time to meet its goals; the local government must hold a public hearing before deciding on an extension.[26]

[21] *Minnesota Statutes* 2017, 116J.994, subd. 3. A business subsidy agreement contains eight components: (1) a description of the subsidy; (2) a statement of public purpose; (3) specific goals for the subsidy; (4) a description of financial obligation if the recipient does not meet the goals; (5) a statement of why the subsidy is needed; (6) a commitment to continue operations in the jurisdiction where the subsidy is used for at least five years after the benefit date; (7) the name and address of the parent corporation, if applicable; and (8) a list of all financial assistance for the project.

[22] *Minnesota Statutes* 2017, 116J.994, subd. 4.

[23] *Minnesota Statutes* 2017, 116J.8731, subd. 5. We discuss this requirement in detail in Chapter 3.

[24] *Minnesota Statutes* 2017, 116J.994, subd. 4.

[25] *Minnesota Statutes* 2017, 116J.993, subd. 2.

[26] *Minnesota Statutes* 2017, 116J.994, subd. 6. Under *Minnesota Statutes* 2017, 116J.8731, subd. 7, DEED can also suspend loan repayments for up to two years.

The business subsidy statute requires that a business commit to operating in the same location where it received the subsidy for at least five years.[27] However, the penalties listed in business subsidy law for violating this provision are fairly weak, and DEED has not included additional penalties in its standard loan agreement.[28] Some business recipients of MIF funds have moved or closed prior to the end of the five-year period.[29] DEED staff told us if a business closes or moves after the two-year project period, it is usually up to the local government to decide how to respond. However, a local government's options are limited, especially if the loan has already been forgiven.

Monitoring and Close Out

Local governments are required to submit annual progress reports about each MIF project to DEED. These reports include information on project costs and the business's progress toward job and wage goals during the two-year project period (and the extension, if applicable). DEED and local governments also monitor progress through periodic telephone calls, e-mails, and on-site visits.

DEED assesses the project at the end of the two-year period and determines whether or not the business met its commitments. For successful projects where repayment is required, some businesses choose to pay back the entire loan immediately, while others make payments for several years after the project is complete. If a business has not met its commitments, DEED has the discretion to offer the business several options, including: (1) a one-year extension of the project period, (2) accelerated repayment of the loan, (3) a reduction in the size of the loan to reflect the project's outcomes, or (4) cancellation of the project. These options are not mutually exclusive. For example, Magnum Machining, Inc., a Deerwood company that received MIF funds in 2011, requested and received a one-year extension at the end of the two-year period. However, even with the extension, the company did not meet its hiring goals and had to repay its loan on an accelerated schedule.

Financial Trends

DEED makes MIF awards on a "rolling" basis; applications may be submitted to DEED at any time. Such a process depends on having a reserve of funding for worthy projects, regardless of when they are submitted. In recent years, DEED has had such funding available, but that has not always been the case.

Revenues

The MIF program receives funding from two major sources: legislative appropriations and repayments from past MIF loans.

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[27] *Minnesota Statutes* 2017, 116J.994, subd. 3(a).

[28] The law states that a subsidy recipient that fails to meet the five-year requirement may not receive another business subsidy for a period of five years from the date of its move, or until it satisfies its repayment obligation, whichever occurs first. *Minnesota Statutes* 2017, 116J.994, subd. 6(b).

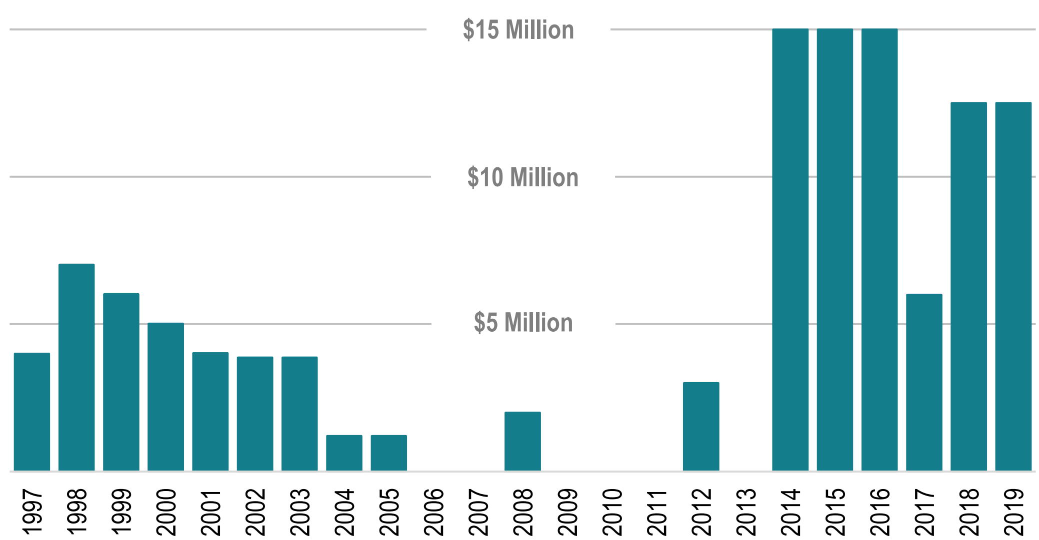
[29] Business subsidy recipients may be authorized to move if the grantor approves the move following a public hearing. *Minnesota Statutes* 2017, 116J.994, subd. 3(e).

After several years of little or no funding, legislative appropriations for the MIF program increased substantially starting in Fiscal Year 2014.

Prior to Fiscal Year 2014, the most money appropriated for the MIF program in a single year was just over $7 million in Fiscal Year 1998. As shown in Exhibit 1.4, between fiscal years 2006 and 2013, the Legislature appropriated only $5 million to the program in total and appropriated no money at all in some years.

This pattern changed in 2014. In fiscal years 2014 through 2016, the Legislature appropriated $15 million annually to the MIF program. For Fiscal Year 2017, the Legislature reduced MIF appropriations to $6 million, although the Legislature increased appropriations to $12.5 million a year for fiscal years 2018 and 2019.

Exhibit 1.4: Appropriations for the Minnesota Investment Fund Program, Fiscal Years 1997-2019



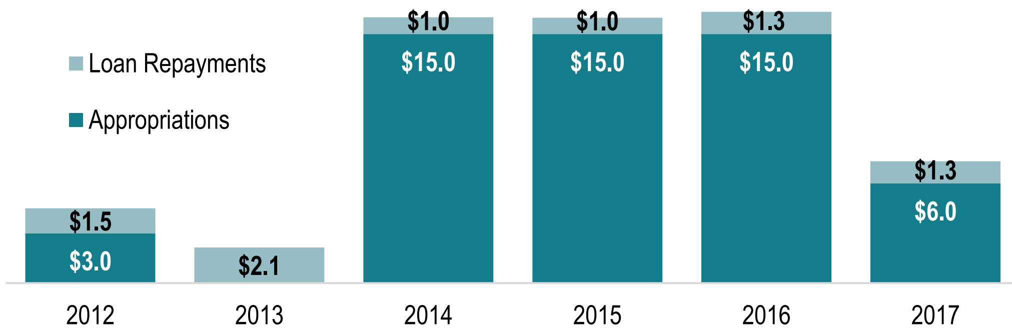
SOURCE: Office of the Legislative Auditor, analysis of appropriation laws.

Between fiscal years 2012 and 2017, DEED received an average of $1.4 million in MIF loan repayments each year. MIF loan repayments that are returned to DEED are placed in a revolving loan account to support future MIF projects. In years when there is little money appropriated to the MIF program by the Legislature, DEED may rely more heavily on the revolving loan fund as a source of revenue for future projects. More than half of DEED MIF loans made in fiscal years 2008 through 2013 required repayment. As appropriations have increased in recent years, MIF loan repayments have represented a smaller share of total program revenue, as shown in Exhibit 1.5.

After the Legislature increased appropriations for Fiscal Year 2014, DEED began to use forgivable loans much more frequently than it had in the past. DEED does not receive repayments from forgivable loans unless a business does not meet its goals, so most of the money awarded in recent years will likely not return to the state revolving loan fund. At the same time, DEED has awarded more total MIF money, so even the smaller proportion of

Exhibit 1.5: Minnesota Investment Fund Revenue Sources, Fiscal Years 2012-2017

In millions



SOURCE: Office of the Legislative Auditor, analysis of state accounting system data.

repayable loans will generate income for the revolving loan fund. Because the amount of money returning to the fund depends in part on how successfully businesses meet their goals, it is difficult to predict the future net effect of these recent trends on the balance of the state revolving loan fund.

Expenditures

Legislative appropriations to the MIF program do not expire at the end of a biennium. DEED can make MIF awards until all funding has been spent. Between fiscal years 2012 and 2017, DEED spent a total of $33.4 million, with an average of $5.6 million each year.

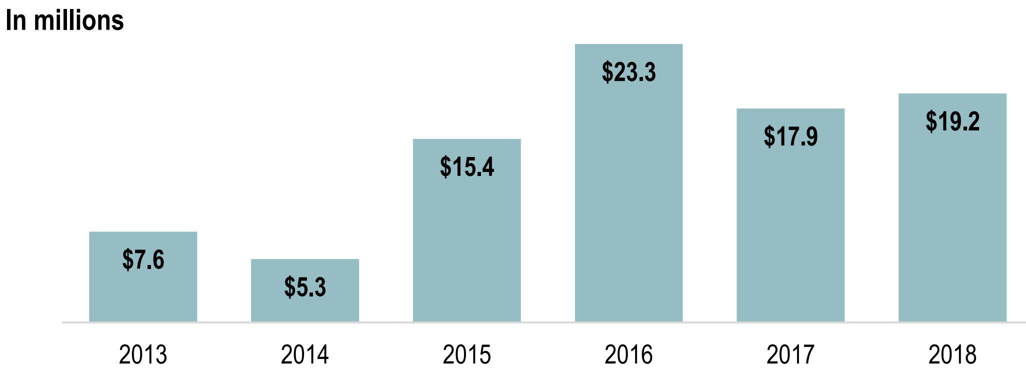
DEED staff told us that, previously in MIF's history, there were some years when DEED could award MIF funds for only part of a year because it quickly spent all of its available funding. In fiscal years 2012 through 2017, however, DEED did not come close to exhausting its MIF balances.

Over the past several years, the Legislature has appropriated more money to the MIF program than DEED has spent, which has resulted in large fund balances.

The recent increase in appropriations has greatly increased the amount of money available for MIF projects, as shown in Exhibit 1.6. In the past six years, annual starting balances averaged $14.8 million and ranged from $5.3 million at the beginning of Fiscal Year 2014 (after a year when the MIF program received no legislative appropriations) to $23.3 million in Fiscal Year 2016. The balance of available MIF funding at the start of Fiscal Year 2018 was about $19.2 million.[30]

[30] This amount includes money for MIF projects that was set aside, or "encumbered," in previous years, but not yet spent.

Exhibit 1.6: Annual Starting Balances of the Minnesota Investment Fund, Fiscal Years 2013-2018



NOTES: Balances include unspent funds from (1) previous appropriations, (2) carry forward funds, and (3) money that DEED has set aside for specific projects. Starting balances do not include legislative appropriations for that fiscal year.

SOURCE: Office of the Legislative Auditor, analysis of state accounting system data.

Project Characteristics

DEED made MIF awards to 138 projects in fiscal years 2008 through 2017, totaling $65.9 million.[31] The largest award for any single project was $4 million, and the smallest was $80,000.[32] The median award was $400,000. DEED awarded more than two-thirds of the money during this period in the form of partially or fully forgivable loans. The types of businesses receiving MIF funds have varied greatly, as shown in Exhibit 1.7.

Geographic Distribution

As Exhibit 1.8 shows, MIF awards have not been evenly distributed throughout the state. In the past ten years, awards have been primarily concentrated in the central and southeastern parts of the state, while awards have been much less common in northern and western Minnesota. The seven-county Twin Cities metropolitan area received about 46 percent of all awards in the past ten years (63 awards). In contrast, the 26 counties that make up economic development regions 1, 2, 4, and 6W received a total of four awards in this same time frame. Because DEED makes awards as it receives applications, the regional breakdown largely depends on which businesses and local governments apply for MIF loans.

[31] These figures are based on all awards during this ten-year period, including some that were later cancelled before legal agreements were signed or funds were disbursed. An additional 36 projects were withdrawn during this same time period, meaning the project began the application process but was discontinued prior to DEED's official award decision.

[32] During this ten-year period, the Legislature mandated three awards exceeding the $1 million cap on MIF awards. We discuss these legislatively mandated awards later in this chapter.

Exhibit 1.7: Businesses that Received Minnesota Investment Fund Awards, Fiscal Year 2017

Company Name	Location	Primary Product or Service	Employees in Minnesota Prior to MIF Award
Al-Corn Clean Fuel	Claremont	Ethanol production	34
Anchor Glass Container Corporation	Shakopee	Bottle manufacturing	300
Biomerics, LLC	Brooklyn Park	Medical device manufacturing	45
Federal Cartridge Company	Anoka	Shooting sports and outdoor recreation products	1,878
F.O.G. Firearms & Cartridge Company	Walker	Firearms and ammunition manufacturing	6
Hearthside Food Solutions, LLC	Lakeville	Food manufacturing and packaging	532
Hydrostat, Inc.	Rice	Industrial cylinder refurbishment	35
Manufacturing Partners, Inc.	Becker	Machined firearms and military munitions	37
Medieval Metalwerx	Mankato	Circle track race components and chassis	2
Prime Therapeutics, LLC	Eagan	Health benefits and pharmacy services	2,093
Tactacam	Caledonia	First-person point-of-view cameras	0
Uponor, Inc.	Apple Valley	Plumbing, fire sprinkler, radiant heating, and cooling system supplier	652
Vyriad	Rochester	Biotechnology	2.5
Wabash National Corporation	Little Falls	Semi-trailers and liquid transportation systems	0
Zierke Built Manufacturing	Fairmont	Custom fabrication	35

NOTES: The number of employees is based on the number of total full-time-equivalent employees listed in each company's MIF application. We did not independently verify these reported numbers. The recipients listed here include projects that were later cancelled.

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

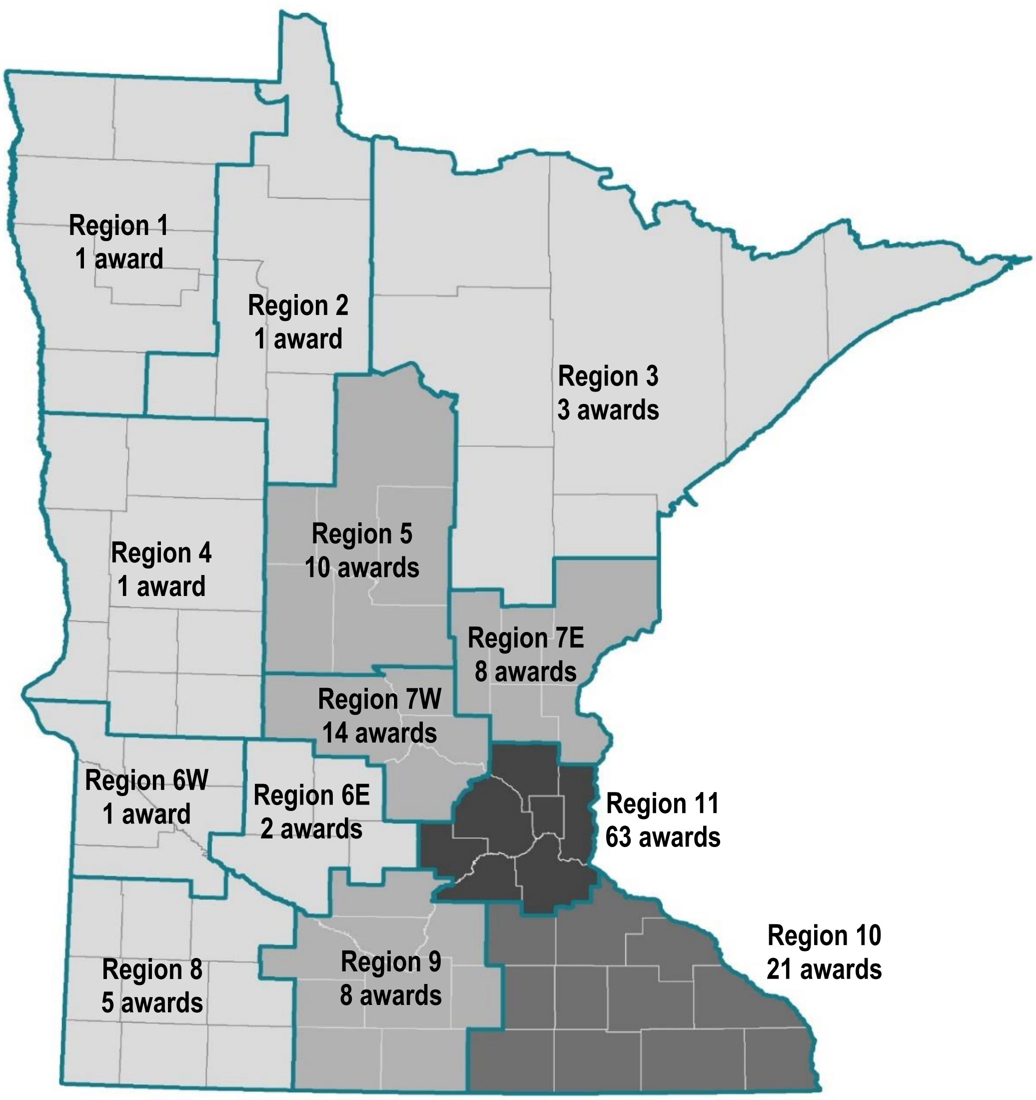
In addition, the geographic distribution of awards partly reflects the location of nonretail businesses in the state. For example, the Twin Cities region has a majority of the state's nonretail employers (56 percent in 2016), which helps explain its large share of MIF awards. The four regions mentioned above that together accounted for only four MIF awards in the past ten years (which was 3 percent of the total awards given in that period) had 9 percent of the state's nonretail employers in 2016.

Starting in Fiscal Year 2014, Twin Cities metropolitan area projects have increasingly received MIF awards.

From the start of the program in Fiscal Year 1997 through Fiscal Year 2013, Greater Minnesota businesses received most MIF awards; DEED made about 74 percent of MIF awards outside the Twin Cities metropolitan area during this period. However, since the increase in appropriations in Fiscal Year 2014, businesses in the Twin Cities area have received about half of the awards.

The Twin Cities metropolitan area received a larger proportion of the total MIF dollars awarded in the past few years, and awards for projects in the Twin Cities area tended to be larger than awards in Greater Minnesota. Exhibit 1.9 shows that the average award in the Twin Cities area has been about $105,000 more than the average award elsewhere in the state since Fiscal Year 2014. In addition, a much larger proportion of Twin Cities awards have been forgivable; since Fiscal Year 2014, 40 out of 45 MIF awards (89 percent) granted to businesses in the Twin Cities area have been partially or fully forgivable, compared to 26 out of 45 MIF awards (58 percent) granted to businesses in Greater Minnesota.

Exhibit 1.8: Minnesota Investment Fund Awards by Economic Development Region, Fiscal Years 2008-2017



NOTES: Listed awards include projects that were later cancelled.

SOURCE: Office of the Legislative Auditor, analysis of Department of Employment and Economic Development data.

Exhibit 1.9: Comparison of Minnesota Investment Fund Awards by Region, Fiscal Years 2008-2017

	Fiscal Years 2008-2013	
	Twin Cities Metro Area	Greater Minnesota
Total money awarded	$7,696,500	$10,236,000
Total money forgiven	$3,649,000	$ 5,713,000
Average award	$ 427,583	$ 341,200
Total number of awards	18	30
Total number of forgivable loans	9	11

	Fiscal Years 2014-2017	
	Twin Cities Metro Area	Greater Minnesota
Total money awarded	$26,346,575	$21,633,500
Total money forgiven	$23,267,325	$12,774,000
Average award	$ 585,479	$ 480,744
Total number of awards	45	45
Total number of forgivable loans	40	26

NOTES: This analysis is based on all MIF awards DEED made in fiscal years 2008 through 2017. Some projects were later cancelled or had the amount of the award reduced.

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

Legislatively Mandated Awards

The Legislature has occasionally awarded MIF funds directly to a business by specifying a project in law.[33] Typically, such awards have been larger than the $1 million cap applied to DEED-awarded projects.

The Legislature has directly awarded several MIF projects in recent years.

Cirrus Aircraft Corporation	Duluth	$4 million
Digi-Key Electronics	Thief River Falls	$4 million
Comlux	Richfield	$3 million
Takeda (Millennium Pharmaceuticals)	Brooklyn Park	$2 million
Enerkem	Inver Grove Heights	$0.7 million

As shown in the box on this page, the Legislature's awards have included up to $3 million for Comlux in Richfield in 2009, $5 million for a biopharmaceutical manufacturer in 2013 (later reduced by DEED to $2 million and awarded to Takeda in Brooklyn Park), and $4 million for Cirrus Aircraft Corporation in Duluth in 2015.[34] The 2017 Legislature designated $4 million for Digi-Key Electronics in Thief River Falls and $700,000 for Enerkem in Inver Grove Heights.[35]

The Legislature has sometimes mandated loan forgiveness contingent on a company's successful completion of its goals. For example, of the projects listed above, the legislation

[33] The Legislature has also occasionally transferred MIF funds to other projects that are not a part of the MIF program. For example, the 2016 Legislature transferred $450,000 for a grant to the Lake Superior-Poplar River Water District. *Laws of Minnesota* 2016, chapter 189, art. 7, sec. 2, subd. 2(q).

[34] *Laws of Minnesota* 2009, chapter 78, art. 1, sec. 3, subd. 2(e)(1); *Laws of Minnesota* 2013, chapter 85, art. 1, sec. 3, subd. 2(a); and *Laws of Minnesota* 2015, First Special Session, chapter 1, art. 1, sec. 2, subd. 2(a)(2), respectively. Comlux ultimately did not locate in Minnesota, and DEED cancelled the MIF project.

[35] *Laws of Minnesota* 2017, chapter 94, art. 1, sec. 2, subds. 2(e)(2) and (3).

for the awards to Takeda, Cirrus Aircraft Corporation, and Digi-Key Electronics directed DEED to provide fully forgivable loans.[36]

Cancelled Projects

MIF projects are often cancelled after DEED makes an award. DEED technically initiates the cancellation process, but cancellation can be based on either a business or DEED decision. So far, roughly 33 out of 138 MIF projects (24 percent) awarded between fiscal years 2008 and 2017 have not gone forward. The total amount of money awarded to these cancelled MIF projects was $14.4 million.[37] In nearly all cases, projects were cancelled before the business signed a loan agreement with the local government. Because DEED only provides funding on a reimbursement basis after the loan agreement is signed, cancelled projects usually end before any state funds are spent.

Projects have been cancelled for a variety of reasons. In the course of our evaluation, we encountered instances in which companies decided that they no longer wished to use the MIF funds they had been awarded because (1) the company was sold, (2) the company's executive leadership changed, or (3) the company decided to seek funding from an economic development program other than MIF. In some other cases, DEED has cancelled projects after companies have failed to make progress toward project goals. Projects in the Twin Cities metropolitan area have been cancelled at rates slightly higher than projects in Greater Minnesota between fiscal years 2008 and 2017.

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[36] As of early 2018, these projects are still ongoing, and it is not yet known if they will meet their goals.

[37] Some ongoing projects are still in their early stages and might be cancelled at a later date.

Chapter 2: Impact

The Minnesota Investment Fund (MIF) is designed to encourage businesses to achieve goals such as job growth, job retention, and increased investment. As Minnesota tries to foster business development, the MIF program may be a useful tool. However, it is difficult to determine the extent to which the program has met its goals.

The skepticism we express in this chapter about program impacts is consistent with prior research regarding the impact of business incentive programs. Over many years, academic researchers have used a variety of methods—some quite sophisticated—to assess public business incentives, ranging from tax policies to subsidies for individual businesses.

In general, academic researchers have questioned whether public business incentives are cost-effective. For example, a recent analysis suggested that state taxes and business incentives have a statistically insignificant effect on a state's gross domestic product.[1] The author summarized past evidence on business incentives by stating "that in some cases they can affect business location decisions, but that in many cases they are excessively costly and may not have the promised effects."[2] We briefly summarize previous research on business subsidies in the appendix of this report.

Key Findings in This Chapter

- Businesses seeking MIF funding do not have to demonstrate that they truly need state subsidies, raising questions about the impact of those subsidies.
- The Department of Employment and Economic Development (DEED) has provided limited information to the public on the MIF program's impacts.
- DEED has significantly overstated the amount of private investment leveraged by the MIF program.
- Local revolving loan funds created through the MIF program are useful for some cities, but others find them to have little practical value.

Based on our review of MIF projects, businesses in the MIF program often have not provided sufficient evidence of their need for public assistance. In this chapter, we offer recommendations to increase the state's role in this program, improve public reporting on program impacts, and more effectively target assistance to businesses that need it.

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[1] Timothy Bartik, *A New Panel Database on Business Incentives for Economic Development Offered by State and Local Governments in the United States* (Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 2017), 108-111, http://research.upjohn.org/reports/225.

[2] *Ibid.*, 116.

Program Purpose

In 1996, the Legislature adopted into law a statement of purpose for the MIF program.[3]

State law says the purpose of the Minnesota Investment Fund is to create or retain jobs and support new or existing businesses.

The law says that the MIF program shall "provide financial and technical assistance…for the creation of new employment or to maintain existing employment, and for business start-up, expansions, and retention."[4] These are the only "goals" explicitly identified as such in the purpose statement of the MIF statute.

However, the statute also alludes to other program goals. The law lists "means" by which the MIF program's goals are to be accomplished. Embedded in this list are what appear to be additional goals for the program. These include:

- Creating above-average economic growth that is consistent with environmental protection.
- Increasing and diversifying the local tax base.
- Improving productivity.
- Stimulating or leveraging private investment to ensure economic renewal and competitiveness.
- Improving the quality of existing jobs, including increased wages and opportunities for individuals to achieve a "reasonable standard of living."[5]

Minnesota laws that pertain to all business subsidy programs (including MIF) also specify some of the goals listed above. All business subsidies must meet a public purpose, "which may include, but may not be limited to, increasing the tax base."[6] Also, businesses receiving subsidies must sign agreements that set goals for job creation, job retention (if applicable), and the wages of the created or retained jobs.[7]

State law does not establish measurable objectives for the MIF program. For example, although job creation is a key program goal, the law does not specify a target number of jobs to be created by MIF projects annually.

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[3] *Laws of Minnesota* 1996, chapter 452, sec. 29, codified in *Minnesota Statutes* 2017, 116J.8731, subd. 1.

[4] *Minnesota Statutes* 2017, 116J.8731, subd. 1.

[5] *Ibid*.

[6] *Minnesota Statutes* 2017, 116J.994, subd. 1. The business subsidy law is *Minnesota Statutes* 2017, 116J.993-116J.995.

[7] *Minnesota Statutes* 2017, 116J.994, subds. 3(a) and 4.

Over time, the Legislature has specified additional MIF goals, but few MIF projects have addressed them.

For example, the 2008 Legislature amended state law to authorize the allocation of MIF funds to projects that promote the "green economy."[8] In 2009, the Legislature added a statutory provision supporting MIF's use for "strategic investments in renewable energy market development."[9] The 2010 Legislature added a provision authorizing the use of MIF to support the development of "microenterprises."[10] These changes have modified the law's provisions about which types of projects or expenditures are eligible for funding; they have not modified the law's overarching statement of purpose.

Based on our review of projects approved during the past decade, we are doubtful that such statutory changes have had much, if any, impact. For all awards made in fiscal years 2008 through 2017, we reviewed (1) DEED's project "review summaries" (used by the commissioner when making final award approvals) and (2) the loan agreements specifying the commitments made by businesses to receive MIF funding. We also selected a random sample of 60 projects that received MIF awards between fiscal years 2012 and 2016, and we systematically examined all documents in DEED's files related to these projects.[11] In recent years, there have been only a few MIF projects involving very small businesses (microenterprises), or that are directly related to the green economy or renewable energy. In general, DEED told us, it has focused its efforts on projects intended to create jobs, foster private investment, support higher wages, and increase the tax base; this is consistent with the MIF law's general statement of purpose.

DEED's Reports on Program Impacts

State law requires DEED to produce a summary report every two years on business subsidies provided by state agencies and local governments.[12] The law does not require DEED to report specifically on the outcomes of the MIF program, and DEED's business subsidy report does not provide information on the MIF program separate from other programs. However, DEED produces "annual program summaries" for a variety of DEED-administered programs, including the Minnesota Investment Fund.[13]

DEED's public reports on the impact of the Minnesota Investment Fund are incomplete and sometimes inaccurate.

For purposes of accountability, legislators and the public should have access to useful, accurate information on whether the MIF program is accomplishing its intended purposes.

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[8] *Laws of Minnesota* 2008, chapter 356, sec. 5, codified in *Minnesota Statutes* 2017, 116J.8731, subd. 4. The MIF statute references a definition of "green economy" in state law.

[9] *Laws of Minnesota* 2009, chapter 78, art. 2, sec.19, codified in *Minnesota Statutes* 2017, 116J.8731, subd. 3.

[10] *Laws of Minnesota* 2010, chapter 347, art. 1, sec. 5, codified in *Minnesota Statutes* 2017, 116J.8731, subd. 4. The MIF statute references a definition of "microenterprises" in federal law.

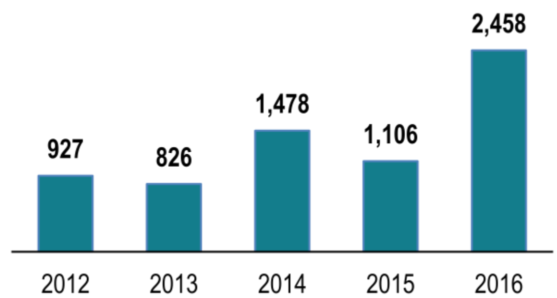
[11] Fifteen of the projects in our sample were cancelled before they received MIF funding.

[12] *Minnesota Statutes* 2017, 116J.994, subds. 8-9.

[13] DEED, "Annual Program Summaries," https://mn.gov/deed/about/what-we-do/agency-results/program-summaries/, accessed November 13, 2017.

DEED's "annual program summary" on its website for the MIF program includes only statewide totals for (1) dollars awarded and (2) jobs created and retained. As shown in the box on this page, DEED's data show that, over a five-year period, the MIF program created or retained an average of 1,359 jobs annually, with a high of 2,458 in Fiscal Year 2016.[14] The site contains no definition of what constitutes a "created" or "retained" job—for example, whether these data reflect a company's original projection of the jobs it would create or, alternatively, the number that were actually created.

DEED reported that the MIF program created about 6,800 jobs over five fiscal years.



A separate DEED website contains information on individual MIF projects from recent years.[15] That site has a state map showing the location of projects, and it provides project-specific data on the "amount [of MIF funding] awarded," "projected new jobs," and "leverage attained." For example, the data indicate that the MIF program was projected to create as few as 5 jobs for some individual projects and as many as 330 jobs for another.[16]

DEED's public reports have several limitations. First, DEED's report on individual MIF projects has contained inaccuracies. Exhibit 2.1 shows instances in which DEED's website information was inconsistent with data we reviewed in DEED project files; the errors in the exhibit represented 16 percent of the businesses for which DEED presented information. The errors varied in size, and they included a mix of under-reports and over-reports. For example, DEED's website says Viracon (Owatonna) projected the creation of 197 jobs in a 2014 project, but the loan agreement for this project promised only 9 full-time-equivalent jobs. For a 2013 project involving Rosemount, Inc., of Shakopee, DEED's website says the company projected it would create 57 jobs, but the company's loan agreement showed that it actually promised 125 full-time-equivalent jobs.

One source of error in DEED's project-specific report is that it has inconsistently reflected amendments to original MIF award amounts and job projections. For example, Price Mechanical, Inc., (Maple Grove) created far fewer jobs than it had originally projected, and DEED subsequently recovered most of this company's original MIF award.

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[14] DEED collects data on jobs created or retained within the companies directly assisted by the MIF program. When a company expands its economic activity, there may be ripple effects that benefit other businesses—for example, if the MIF-assisted business purchases construction materials or equipment from other Minnesota businesses. DEED has occasionally conducted analyses that examined the broader economic impacts of MIF projects.

[15] DEED, "Business Awards Finance Map," https://mn.gov/deed/business/financing-business/deed-programs/finance-awards/, accessed October 30, 2017.

[16] The recent projects with five projected new jobs were (1) Action Manufacturing of Marshall, which received a $240,000 MIF award in 2013 and (2) Louis Industries, Inc., of Paynesville, which received an $80,000 award in 2013. The project with 330 projected jobs was Comcast of St. Paul, which received a $1 million MIF award in 2015.

Exhibit 2.1: Inaccuracies in DEED's Public Reporting of Minnesota Investment Fund Awards

Business	Location	DEED's Publicly Reported Jobs Projected	Actual Jobs Promised in Loan Agreement
Action Manufacturing	Marshall	5	10
C4 Welding, Inc.	Sauk Rapids	23	40
Jostens, Inc.	Owatonna	160	10
Link Snacks, Inc. (2014)	Minneapolis	25	20
Pearson's Candy Company	St. Paul	59	40
Price Mechanical, Inc.	Maple Grove	8	31
Prime Design (IEM, Inc.)	West St. Paul	29	30
Rosemount, Inc. (2013)	Shakopee	57	125
Sign-Zone, LLC	Brooklyn Center	42	25
Viracon (2014)	Owatonna	197	9

Business	Location	DEED's Publicly Reported Award Amount	Actual Award Listed in Loan Agreement
Jostens, Inc.	Owatonna	$500,000	$ 47,620
Kraft Heinz Company	New Ulm	450,000	435,000
Louis Industries, Inc.	Paynesville	78,100	80,000
Price Mechanical, Inc.	Maple Grove	180,660	700,000

NOTES: In the column showing DEED's publicly reported jobs projected and award amounts, these numbers reflect the "projected new jobs" and "amount awarded" shown on DEED's "Business Finance Awards Map" (see web address below). DEED's website does not define these terms. In the column showing jobs promised in loan agreements, jobs are specified in the loan agreements as full-time-equivalent positions.

SOURCES: Office of the Legislative Auditor, based on data from DEED's "Business Finance Awards Map," https://mn.gov/deed/business/financing-business/deed-programs/finance-awards/, accessed October 30, 2017; and MIF loan agreements between local governments and businesses formalizing the businesses' commitments.

For this project, DEED's website does not show the original number of jobs projected (31) or the original MIF award ($700,000); it shows the actual number of jobs created (8) and the final amount the business received ($180,660). In contrast, Jostens, Inc., of Owatonna also committed to create far fewer jobs (10) than it had originally projected and thus received a significantly reduced MIF award (about $47,000), but DEED's website shows the original number of jobs projected (160) and the original award amount ($500,000).

None of DEED's public reports have information on the MIF program's employee wage impacts.[17] Businesses seeking MIF loans provide DEED with information on proposed wage levels in their MIF applications. After DEED provides businesses with MIF funding, it collects information regarding the actual wages that MIF-assisted businesses have paid to newly hired employees. However, DEED's public reports do not summarize data on the MIF program's proposed or actual employee wage levels. Also, although state law identifies "increases in wages" as one way that the MIF program should improve the

[17] DEED's biennial business assistance report contains information on wages projected or paid to employees in projects that have received public assistance, but the report does not distinguish MIF projects from projects assisted by other programs.

quality of existing jobs, DEED does not compare wage levels in individual businesses before and after MIF awards.[18]

Finally, DEED's public reports on the MIF program lack other key information, including the following:

- There is no information on other possible program goals mentioned in state law for the MIF program, such as increases in the tax base or improvements in productivity.[19]
- DEED's listing of project awards does not distinguish between projects that received forgivable loans and projects with loans scheduled for repayment.
- DEED's list of projects does not include those that were cancelled subsequent to DEED's decision to award MIF funding to the projects.

RECOMMENDATION

DEED should improve the usefulness and accuracy of its public reports on the Minnesota Investment Fund.

Because individual MIF projects often take two or more years to complete, it may be reasonable for DEED's public reports to rely partly on data showing *projected* jobs, wages, and leveraged private investment. However, DEED should carefully describe projections as such, and it should define its terms. For example, it should clarify whether the numbers of projected jobs it reports include both "new" and "retained" jobs.

In addition, DEED's public reports should include more information about the actual outcomes of MIF projects. Some businesses do not meet the job and wage goals they originally committed to, and data on actual outcomes would provide a truer measure of impact.[20]

DEED should more closely scrutinize the project data that it publicly reports. DEED should ensure that its public reports accurately and consistently present information regarding project awards, jobs, and wages. In Chapter 3, we note that DEED relies considerably on job and wage data that are reported by assisted businesses. DEED should verify self-reported data to the extent possible, and it should also publicly disclose the limitations of the data it reports.

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[18] *Minnesota Statutes* 2017, 116J.8731, subd. 1. In addition, *Minnesota Statutes* 2017, 116J.8731, subd. 4, identifies projects paying "higher wage levels to the community" as a condition that can qualify projects for MIF funding, but we did not see evidence that DEED has formally compared project wage levels to wages in the broader community.

[19] While all MIF projects have job and wage goals, not all projects aim to increase the tax base or improve productivity.

[20] For some MIF projects, DEED has reported actual jobs created in the portion of its website labeled "projected new jobs." But, without distinguishing "projected" and "actual" jobs, this is potentially confusing. If DEED chooses to report actual jobs created on its website (in addition to projected jobs), it should properly label the data and try to ensure that jobs reported as actually created were, in fact, a direct outgrowth of the assisted projects.

DEED should also convey information in its public reports about MIF projects that were later cancelled. Although cancelled projects ultimately did not receive MIF funding, such reporting would provide transparency about the full range of MIF projects that DEED deemed worthy of funding.

Lastly, DEED should consider reporting other measures of performance that align with the MIF program's statutory purpose statement. For example, it would be useful to know the extent to which the MIF program results in increases in the state's property tax base. On the other hand, we recognize that some goals referenced in the MIF purpose statement—such as improvements in productivity and job quality—would be difficult to measure.

Business Impacts

The Minnesota Investment Fund is supposed to foster job growth and business investment in the state. It is currently difficult to conclude whether the MIF program has created all of the impacts that DEED and businesses have attributed to it.

Scope of Impacts

Minnesota law says that the MIF program should create or retain permanent private sector jobs "in order to create above-average economic growth."[21] This statement could refer either to growth in local economies or in the state's overall economy.

Few Minnesota businesses directly benefit from the Minnesota Investment Fund.

The MIF program is too small to meaningfully affect statewide economic growth, although it may have important impacts on individual businesses or communities. The Legislature has increased MIF funding in recent years, but the program still reaches a limited number of businesses. There are more than 80,000 nonretail employers in Minnesota. For fiscal years 2013 through 2017, DEED awarded MIF funding to an average of about 20 businesses annually.

Likewise, jobs created in MIF-assisted businesses represent a small share of all Minnesota jobs (and all recently created jobs). There are about 2.5 million private sector employees in Minnesota, and the state's economy added a total of about 179,000 private sector nonretail jobs over a recent five-year period. DEED reported that businesses receiving MIF awards during that same period projected they would create about 6,800 jobs, which would have been 4 percent of the total actually created.[22]

Even among employers that have added large numbers of jobs, MIF-assisted businesses account for a small share. On average, DEED has given about 12 MIF awards annually in recent years to businesses that proposed to add at least 40 jobs. Typically, companies pledge to add these jobs within a two-year period. However, about 700 businesses

[21] *Minnesota Statutes* 2017, 116J.8731, subd. 1(1).

[22] Because projected jobs are expected to be created in the future, companies may have created some of these jobs after the five-year period.

statewide increased their total employment by at least 40 jobs between January 2015 and December 2016.[23]

Some private organizations that advocate on behalf of Minnesota businesses have recognized that programs offering incentives to individual businesses (such as MIF subsidies) have a limited impact. For example, a 2017 document issued by the Minnesota Business Partnership said: "Tax incentives or subsidies for particular businesses may occasionally help attract and retain jobs, but policymakers should focus on improving the overall business tax climate and promoting broad-based economic vitality."[24] Likewise, an official for the Minnesota Chamber of Commerce told us that MIF subsidies can be a useful tool for individual businesses in certain situations, but his organization prefers to focus on policy changes—such as property tax relief—that would have impacts on a broader array of businesses.

The "But-For" Test

To ensure that public subsidies to businesses are an effective use of state resources, policymakers should consider whether the subsidies induced the assisted businesses to add jobs or make private investments. As a general rule, governments should not assist private businesses to promote development that would have occurred without the public investment. For example, one leading researcher on business subsidies wrote the following:

> If the new [business] activity would have occurred anyway, the fiscal effects are clearly negative and equal to the subsidy cost. Such subsidies should be avoided.…[25]

State law governing one of Minnesota's longstanding economic development programs—tax increment financing—requires municipalities to make the following determination before a project can proceed: "The proposed development or redevelopment would not reasonably be expected to occur solely through private investment within the reasonably foreseeable future."[26] Such a determination is often called a "but-for" test, because it requires public officials to assert that a project would not occur *but for* the proposed public financing.

State law does not require DEED (or any public body) to determine that a Minnesota Investment Fund project needs a subsidy to proceed.

Neither the Minnesota Investment Fund law nor the state's general business subsidy law require MIF projects to meet a "but-for" test. Rather, state law requires businesses seeking

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[23] This analysis was provided by DEED's Labor Market Information Office, based on the Quarterly Census of Employment and Wages. The analysis included private businesses that had employees throughout the full two-year period. It excluded employers in the following categories: retail trade; arts, entertainment, and recreation; and accommodation and food services.

[24] Minnesota Business Partnership, *Blueprint for Fiscal Policy Reform* (Minneapolis, January 2017), 5, https://mnbp.com/wp-content/uploads/2017/01/4_Blueprint_Fiscal.pdf.

[25] Timothy Bartik, *Local Economic Development Policies*, Upjohn Institute Working Paper 03-91 (Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 2003), 9, http://research.upjohn.org/up_workingpapers/91/.

[26] *Minnesota Statutes* 2017, 469.175, subd. 3(b)(2)(i).

MIF assistance to "demonstrate why the grant is necessary for a project."[27] Neither Minnesota statutes nor state rules specify what "necessary" means, nor do they indicate the type of evidence businesses should provide to demonstrate that a MIF award is "necessary."

DEED requires that businesses applying for MIF attest that their proposed projects "would not happen to the extent outlined" without MIF support.[28] However, this is merely an assertion by the business; DEED does not ask businesses to provide evidence to support the statement, nor does it require public officials to validate it.

DEED requires MIF applicants to "explain why MIF financing is necessary for this project to move forward," but our reviews of MIF files indicated that responses to this question were typically brief (if they existed at all) and unconvincing.[29] Most applicants did not provide details about their inability to get private financing for a project or about competing subsidy offers from other states the company had received. Examples include the following:

- When asked why MIF financing was necessary, one applicant said: "Numerous items were considered in the company's final decision including this MIF financing…." The application provided no details on these other considerations or how the MIF program factored into the decision. The applicant mentioned that the company considered expansion in Texas but provided no details about this option or why it was rejected.

- Another application said: "MIF financing is necessary for this project to assist in managing our growth, hiring and training new employees, and purchasing the necessary equipment." The application did not clarify why MIF support was essential, or why the project could not be pursued entirely with private financing.

RECOMMENDATION

The Legislature should require stronger assurance that use of the Minnesota Investment Fund is essential for a business project to proceed.

State policy should discourage public funding for business projects that could move forward without it. While it will always be challenging to determine what a business would do in the absence of MIF assistance, a but-for requirement may help restrict subsidies to the businesses that most need them.[30] In our view, the Legislature should consider requiring businesses receiving MIF subsidies to demonstrate that, without MIF assistance, (1) the

[27] *Minnesota Statutes* 2017, 116J.8731, subd. 7.

[28] This statement is weaker than the statutory but-for test cited above for tax increment financing. Generally, projects where public subsidies supplement a business's resources will always be able to happen "to a greater extent" than projects based on the business's resources alone. Thus, a business can readily attest that, without MIF assistance, the project would not happen "to the extent outlined" in the MIF application.

[29] As noted earlier, we systematically reviewed DEED's entire project files for 60 randomly selected MIF projects to which DEED awarded MIF funding in fiscal years 2012 through 2016. In addition, we reviewed many other files or parts of files during our evaluation.

[30] Implementation of a but-for requirement cannot guarantee that public subsidies will be limited to projects that would not otherwise proceed. Our office has previously observed that Minnesota's statutory but-for test for tax increment financing was open to interpretation. For prior discussions of the but-for test, see: Office of the Legislative Auditor, Program Evaluation Division, *Tax Increment Financing* (St. Paul, 1986) and *Tax Increment Financing* (St. Paul, 1996); and Joel Michael, *Tax Increment Financing Project: The "But For" Test and Public Costs and Benefits* (St. Paul: House of Representatives Research Department, 1987).

business does not have access to financing that would enable the project to proceed or (2) the proposed job gains would likely occur in another state. This statutory requirement would clarify the reasons that MIF financing could be deemed "necessary."

In addition, it is equally important for DEED to assess—through its application forms, instructions, and application review process—whether applicants for MIF assistance have demonstrated a need for MIF funding. In fact, a demonstrated need for assistance—based on the criteria we suggest above—should be a centerpiece of the application. DEED should expect businesses seeking MIF awards to provide substantive evidence that at least one of the two conditions in the preceding paragraph is present. By requiring documentation—rather than mere assertions—DEED may improve the likelihood that MIF projects are inducing jobs and private investment that would not occur otherwise.

Job Impacts

As noted earlier, state law declares that job creation and retention is a primary goal of the Minnesota Investment Fund. The MIF program can fulfill this goal if it helps existing Minnesota businesses expand their operations in the state, convinces businesses to keep jobs in Minnesota that are already here, or entices out-of-state businesses to begin operations in Minnesota.

In some cases, Minnesota Investment Fund grants or loans appear to have played a direct role in job creation that, in all likelihood, would not otherwise have occurred.

For example,

- In northwestern Minnesota, the city of Dilworth (with a population under 5,000) had a deteriorating, long-vacant department store. An India-based company (AXIS Clinicals) that conducts clinical trials of pharmaceuticals investigated the possibility of establishing its first U.S. location in the Fargo area. The company chose the Dilworth location, assisted by a $1 million MIF award in 2015 (half of which was forgivable), a $779,000 Job Creation Fund subsidy, and some local funding.[31] It seems plausible that this large employer would have located elsewhere—perhaps in North Dakota—without MIF assistance.

- A Duluth-based aircraft company (Cirrus Aircraft Corporation) received Federal Aviation Administration approval in late 2016 to produce its first jet. According to a senior company official, Cirrus seriously considered expanding its Tennessee facility—instead of its Duluth facility—to build a paint facility for the new jet. The company said it had difficulty getting bank financing to expand in Duluth because it did not own the land where the expansion would occur.[32] However, the 2015 Legislature appropriated $4 million in MIF funding, which—combined with general obligation bonds from the City of Duluth—helped to persuade the company

[31] This project received an extension on its MIF loan in 2017 because it had filled only half of the 100 jobs it initially committed to create.

[32] The land at the expansion site is owned by the City of Duluth and managed by the Duluth Airport Authority. According to a company executive, Cirrus needed to locate this facility at an airport due to the nature of its business; it could not simply build at any location.

to expand in Duluth.[33] The company has committed to adding 150 full-time-equivalent jobs.

- A small Minnesota company (Medieval Metalwerx) that makes dirt track race cars and related components wanted to move from its existing location to a larger one. The company proposed building a new facility in Mankato, and DEED awarded $192,000 in MIF funding to this project in 2017. A company official told us that the MIF award was a key factor in obtaining additional bank financing that made the project possible. The project is expected to create eight new full-time-equivalent jobs.

In these cases, it appeared to us that some amount of MIF funding was justified to help ensure that these projects proceeded.

However, some jobs attributed to the Minnesota Investment Fund program might have been created without state support.

The following are examples of projects we reviewed in which the need for MIF seemed questionable:

- Acucraft Fireplaces (The Maxson Company) in Elk River received a $100,000 forgivable MIF loan. However, at the time DEED approved the award in 2015, the company had already been approved for a bank loan that could have covered the items it purchased using MIF assistance.

- An Oakdale company (Optimize Social Media) wanted to expand with assistance from a $129,000 forgivable MIF loan. Local officials who prepared the MIF application in 2017 and reviewed the company's finances told us the company would have expanded in Oakdale even without MIF financing.

- A company (Link Snacks, Inc.) received a $100,000 forgivable loan in 2014, which it used to buy office furniture as part of a business expansion at its Minneapolis location. The company asserted that this expenditure would lead to the creation of 20 new jobs, including 13 that had hourly wages of at least $48 an hour (or annual incomes of at least $99,840). DEED found that the company added the promised jobs, but we think it is questionable whether an award of $100,000 for furniture induced the business to increase its annual payroll costs by more than $2 million.

- In 2016, DEED made a MIF award to the City of Minneapolis to again help Link Snacks expand its Minneapolis operations through a forgivable loan. The city welcomed the company's expansion into a downtown space that had previously been hard to fill. However, city staff who assisted with the MIF application told us that, to their knowledge, the company (1) had not considered other locations for the expansion and (2) could have raised the needed capital for this project on its own.

In addition, as we discuss in more detail in Chapter 3, DEED's policies raise further questions about whether MIF funds induced the business expansions. Specifically, DEED sometimes allowed companies to attribute to a MIF project the expenditures incurred and

[33] *Laws of Minnesota* 2015, First Special Session, chapter 1, art. 1, sec. 2, subd. 2(a)(2).

employees hired *before* they received MIF awards. If the company was already making expenditures and hiring employees, it seems reasonable to question whether the MIF award induced the project to occur.

As noted earlier, the absence of a but-for test for the MIF program also raises questions about which projects truly needed public subsidies. Unless businesses are required to demonstrate in reasonable detail that their projects—without MIF subsidies—would not have been financially feasible or would have occurred outside Minnesota, there will be doubts about the MIF program's role in causing businesses to add jobs.

In some cases, businesses that received MIF awards have proceeded with their projects while opting to forgo the MIF funding—raising questions about whether state assistance was essential at the time of the award. For example, DEED awarded Olympus America (Gyrus ACMI) a $1 million forgivable MIF loan in 2014 to help it complete a $37 million project in Brooklyn Park. But, due to discomfort with certain MIF program requirements, the company decided not to use its MIF award. Nevertheless, the company completed its project.

Not all projects assisted by the Minnesota Investment Fund have met their job commitments, but DEED has taken steps so that the state faces minimal financial risk in such cases.

In Chapter 1, we noted that more than 20 percent of MIF projects are eventually cancelled. For instance, companies that have been approved for MIF funding may decide they no longer wish to participate in the program, or projects may reach their "compliance date" without significant progress toward project goals.[34] Among 23 closed, noncancelled projects we reviewed in depth, 19 projects met or surpassed their original job commitments.[35] Some other projects we reviewed in depth were still ongoing, and it was too soon to assess whether they would meet their job goals.

DEED's loan agreement template for MIF projects has provisions to protect the state's interests. Although the requirements may vary among individual projects, loan recipients are expected to commit collateral, lines of credit, real estate mortgages, or other guarantees in case they default on their loans.[36] DEED told us that all MIF projects in recent years have been subject to such requirements. Also, if a business does not meet its job

[34] A project's "compliance date" is the date by which it is expected to achieve its job and wage commitments. This date is ordinarily two years from the project's "benefit date," which is the date when MIF-financed equipment becomes operational or the date a building certificate of occupancy is issued for real property financed through the MIF program.

[35] Our analysis excluded two other closed projects: one that aimed for job retention rather than job creation, and one that did not have DEED project closing documents in the project file. In addition, DEED cancelled at least one of the projects we excluded from our analysis when it was clear that the company could not meet its job goals.

[36] We are aware of one instance in which the state (and a local government) did not recoup MIF loans that were supposed to be repaid. In that project, the company met its job commitment, but it subsequently filed for bankruptcy and was unable to make loan repayments.

commitments, DEED's loan agreement template authorizes the state to recover MIF payments in proportion to the share of promised jobs that were not added.[37]

As we discuss further in Chapter 3, DEED requires local governments to submit periodic monitoring reports that help DEED assess whether a company is meeting its commitments. When DEED's review of these reports at the end of the project period shows that companies have fallen short, DEED has generally moved promptly to recover state money. In the projects we reviewed closely, whenever DEED found that a business did not meet the job and wage goals listed in its loan agreement, the department proportionately reduced the size of the award or took other appropriate action. If the businesses had already received payments from DEED, the department took steps to require repayment.

Subsidy per New Job

Earlier, we noted that academic researchers have questioned the cost-effectiveness of business incentive programs. Even when a public agency subsidizes projects that would not have proceeded in the absence of public funding, it is important to consider whether the amount of subsidy per job was reasonable.

For projects awarded in fiscal years 2008 through 2017, we examined the number of jobs that businesses proposed to create at the time of their MIF awards and the amount of subsidy per proposed job that DEED awarded.[38] State law provides DEED with no guidance about how much money it should spend per new job.

DEED's subsidies per job in the Minnesota Investment Fund program have varied widely, ranging from about $1,700 to more than $40,000 per job.

Over the ten-year period we examined, DEED awarded a total of about $63.4 million to businesses that committed to create about 8,900 jobs. Among these projects, the median number of promised new jobs per project was 40; the median subsidy per promised job was $9,000.

However, the amounts of DEED's MIF subsidies—calculated on a per-job basis—varied considerably among projects. At the low end, a project awarded in Fiscal Year 2012 received a subsidy of $1,667 per proposed job.[39] At the other extreme, two projects (awarded in fiscal years 2015 and 2016) each received loans exceeding $40,000 per

[37] Once there is a completed loan agreement between the city and business, the business may submit invoices to the city and receive reimbursements with MIF funding for allowable expenses. These payments may be made to the business before job commitments have been met.

[38] For this analysis, we reviewed documents for 133 projects, including ones that were subsequently cancelled. We excluded five projects that (1) focused on job retention rather than job creation or (2) did not have a "review summary" in DEED's project files. (DEED staff submit a "review summary" to the DEED commissioner prior to the grant awards.) In some cases, the commitments of new jobs reported in the review summaries submitted to the DEED commissioner were revised in subsequently developed loan agreements.

[39] This subsidy was for a $500,000 forgivable award for a project by Prime Therapeutics, LLC, of Eagan, later modified to $499,000. The loan agreement required the company to use the award to create 300 full-time-equivalent jobs, each paying a base wage of at least $13 an hour.

proposed job.[40] In Chapter 3, we discuss DEED's practices for determining the size of MIF awards and raise questions about inconsistencies we observed.

Impact on Private Investment

State law says that the Minnesota Investment Fund should create or retain jobs partly through "stimulation or leverage of private investment to ensure economic renewal and competitiveness."[41] MIF projects must include private sources of financing, with the public MIF subsidy accounting for no more than half of project costs.[42]

DEED has substantially overstated the amount of private funding leveraged by the MIF program.

DEED has reported large amounts of "leverage attained" by MIF projects. For the period from July 2013 through October 2017, DEED's publicly reported data showed that more than $2.1 billion in investment was leveraged by MIF awards. For individual MIF projects, the reported amounts of leveraged dollars ranged from a low of $100,000 for one project to a high of $1.15 billion for another. The latter project (the Post Holdings, Inc., MIF project in Lakeville) by itself accounted for more than half of the MIF-leveraged funds reported by DEED in this time period.[43]

However, we do not believe that the MIF program induced the $1.15 billion private investment reported by DEED for the Post Holdings project. St. Louis-based Post Holdings entered into an "agreement and plan of merger" in January 2015 with MOM Brands, a company headquartered in Lakeville.[44] Months after the merger, DEED received an application from the City of Lakeville and MOM Brands for a MIF loan. The loan (plus a city tax abatement) was intended to convince Post Holdings to keep a headquarters facility and at least 251 jobs in Lakeville rather than move them to another state.

DEED counted the entire sale price of MOM Brands as a private expenditure that was leveraged by the MIF program. Besides the fact that the acquisition of MOM Brands occurred well before DEED awarded a MIF loan to Post Holdings, it is implausible that a $750,000 MIF loan would be a decisive factor in a company's completion of a $1.15 billion

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[40] The two projects were: (1) Viracon of Owatonna, which received a forgivable $400,000 MIF loan for a commitment to create nine jobs, each paying a wage of at least $10.25 an hour and having combined wages and benefits of at least $15.24 an hour; and (2) NatureWorks, LLC, of Minnetonka, which received a partially forgivable $250,000 MIF loan for a commitment to create at least six jobs, each with wages and benefits of at least $24 an hour. Two other projects approved by DEED initially provided awards of $50,000 per new job, but the subsequent loan agreements substantially increased the number of required new jobs.

[41] *Minnesota Statutes* 2017, 116J.8731, subd. 1.

[42] *Minnesota Statutes* 2017, 116J.8731, subd. 3(1).

[43] DEED's data suggest that, in aggregate, each dollar awarded through the MIF program has leveraged about $53 in investments. By excluding the reported Post Holdings leverage alone, the amount leveraged per dollar of MIF funding would decline to $24. The actual amount of leveraged dollars that should be attributed to MIF projects is open to question, given the absence of a but-for test for the MIF program and the other concerns expressed in this section.

[44] MOM Brands issued a press release at that time which said: "MOM Brands today announced that it has entered into a definitive agreement for the sale of the company to Post Holdings, Inc. in a transaction valued at approximately $1.15 billion."

acquisition. We saw no evidence in DEED files that the MIF loan to retain a headquarters in Lakeville had any impact on the company's earlier acquisition of MOM Brands.

The Post Holdings project had the largest inaccuracy we saw in reported leverage amounts, but there were others. For example, DEED reported that a MIF award to The Kraft Heinz Company in New Ulm leveraged investments of $100 million. However, the grant contract and loan agreement for this project required $20 million in private investment, and project invoices showed a total of $21 million in project expenditures.

In addition, DEED's reported amounts of "leverage attained" in MIF projects have included more than just private investments, which may be misleading. In projects that have involved both local government subsidies and MIF subsidies, DEED's website has included the local subsidies in its reports of leveraged dollars. Counting non-MIF public subsidies as leveraged investments is potentially misleading because DEED sometimes publicly refers to MIF-leveraged amounts as "leveraged private investment" or "company investments."

Wage and Benefit Impacts

One purpose of the MIF program is to ensure reasonable or increased compensation for employees in the assisted businesses. Specifically, the law mentions:

- Investments in technology and equipment that increase productivity and "provide for a higher wage."
- Improvements in the quality of existing jobs, "based on increases in wages or improvements in the job duties, training, or education associated with those jobs."
- Improved opportunities for residents to "create a reasonable standard of living, consistent with federal and state guidelines on low- to moderate-income persons."[45]

After DEED makes a MIF award and enters into a grant contract with a local government, the local government and business enter into a legally enforceable loan agreement. The loan agreement typically requires that wages for each new job created by a MIF project exceed a specified "base wage"—that is, the lowest hourly wage that the loan agreement allows the business to pay to new employees.[46]

In 98 loan agreements we reviewed for projects awarded in fiscal years 2008 through 2017, the median base wage requirement was $13.00 an hour.[47] For individual projects, base wages required by loan agreements ranged from $10.00 to $31.66 an hour.[48] For a full-time, full-year job, a $13.00 an hour wage results in an annual salary of $27,040. Such an annual wage was approximately equal to 110 percent of the federal poverty guideline for a

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[45] *Minnesota Statutes* 2017, 116J.8731, subds. 1(1), (4), and (5).

[46] Often, loan agreements also establish a minimum hourly value for the employee benefits package.

[47] Our analysis excluded projects during this period that did not have loan agreements and those in which the loan agreements did not specify a base wage.

[48] We also examined base benefit levels in loan agreements. Some loan agreements that did not specify a base benefit level specified a base hourly wage and base hourly total compensation; in such cases, we computed the difference between these two as the implicit base benefit level. Among projects with either an explicit or implicit base benefit level, the median base benefit level was $3.50 per hour.

family of four for Federal Fiscal Year 2017.[49] About one-third of MIF loan agreements did not specify employee compensation requirements beyond base wages, but those that did had a median base total compensation requirement of $17.14 an hour (wages and benefits).

We also reviewed DEED reports that summarized wages and benefits *actually paid* to employees in a sample of MIF projects. Specifically, we examined DEED's project closing documents for 18 projects that received MIF awards in fiscal years 2012 through 2016.[50] We did not audit the data to determine whether DEED properly counted new employees and accurately calculated their average compensation levels.[51]

For the projects we reviewed, businesses typically paid their employees more than the minimum compensation requirements listed in loan agreements.

Exhibit 2.2 shows the average wages paid to employees in each project we reviewed, based on the businesses' reports to local governments. The per-project average hourly wage reported in DEED closing documents ranged from $16.66 in one project to $56.63 in another; the midpoint of these per-project averages was about $25 an hour.[52] Thus, although MIF loan agreements typically set fairly modest benchmarks for employee compensation, most businesses provided average compensation well above the base levels in the loan agreements. For example, the loan agreement for a Polaris Industries, Inc., project in the city of Wyoming required the company to pay new employees an average of $18.75 an hour in total compensation (wages and benefits); according to DEED's project closing document, the company's actual average compensation for its new employees totaled more than $56 an hour.

Just as it is difficult to prove that the MIF program has caused businesses to add jobs, it is also difficult to conclusively determine the program's impact on compensation. The program's effects depend on the extent to which projects meet a but-for test: that is, whether MIF awards have induced companies to create jobs (with particular wage and benefit levels) they otherwise would not have created.

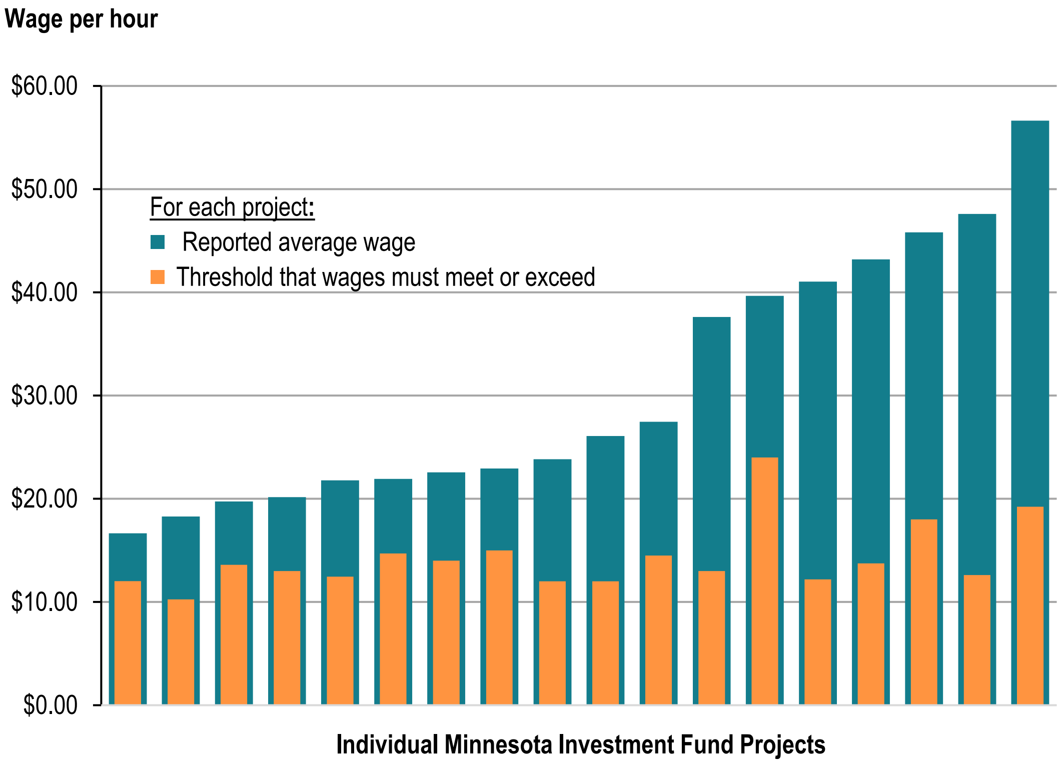
[49] *Minnesota Statutes* 2017, 116J.8731, subd. 5, requires that businesses receiving MIF funding pay their employees total compensation (including benefits) that "on an annualized basis is equal to at least 110 percent of the federal poverty level for a family of four." During the period for which we reviewed MIF projects, 110 percent of the federal poverty guideline for a family of four ranged from $23,320 (in Federal Fiscal Year 2008) to $27,060 (in Federal Fiscal Year 2017).

[50] Among the 60 projects in the sample described earlier, 18 had DEED project closing documents that indicated the average actual wages for the project.

[51] We observed that DEED's project closing documents incorrectly reported the average wage and/or benefit levels that had been *proposed* by most businesses at the time their MIF awards were made.

[52] The $25 an hour "midpoint" is the median of the average per-project wage levels reported in DEED project closing documents for 18 projects.

Exhibit 2.2: Reported Average Wages for Selected Minnesota Investment Fund Projects



NOTES: Each bar represents a project that received an award in fiscal years 2012 through 2016. Each project's average hourly wages represent those reported in DEED's closing documents at the time of project completion, based on employees the business said it hired after receiving the MIF award. The "threshold that wages must meet or exceed" represents the minimum wage level that each loan agreement required for newly hired employees. The fifth and fourteenth orange bars in this chart include both wages and benefits, reflecting loan agreement requirements specific to those projects.

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

Local Government Impacts

As discussed in Chapter 1, a MIF project involves collaboration between DEED, a local government, and a new or expanding business. Local governments submit MIF applications in cooperation with businesses, and state law provides opportunities for local governments to retain a portion of repaid MIF loans.

Administrative Impacts

A MIF project—from conception to closure—typically occurs over a period of several years. As shown in Exhibit 2.3, local governments have significant responsibilities throughout that process. Even before submitting a MIF application to DEED, local governments are expected to perform numerous tasks—such as checking a business's credit and legal history for any noteworthy problems, and conducting a public hearing on the MIF project. Subsequently, local governments play roles in drafting the application for MIF funding, as partners in legal documents (notably, the grant contract with DEED and the loan

Exhibit 2.3: Local Government Responsibilities in Minnesota Investment Fund Projects

- **Preliminary Review of Eligibility.** Make preliminary determination in consultation with the Department of Employment and Economic Development (DEED) about whether a business meets minimum program requirements.

- **Business's Credit and Legal History.** Obtain credit reports on the business. Determine whether there are adverse findings or concerns related to the business or key business owners, including tax liens, judgments, court actions, filings with regulatory agencies, criminal records, pending lawsuits, or bankruptcies.

- **Public Hearing and Local Resolution.** Hold a public hearing on the proposed project to provide citizen notification and opportunities for input prior to submitting an application to DEED. Submit to DEED a copy of the meeting minutes, public notice, affidavit of publication, and local government resolution that authorizes local officials to proceed with the project.

- **Application.** Complete a Minnesota Investment Fund (MIF) application form (in conjunction with the business) and submit it to DEED. Among other things, the application must:

  - ✓ Describe the community's economic needs.
  - ✓ Describe steps taken to review the business's credit and any adverse actions against the business.
  - ✓ Describe the local government's ability to manage the grant, revolving loan fund, state and local compliance requirements, and implement the project.
  - ✓ Obtain a letter from tax assessor detailing any impacts on tax base.
  - ✓ Disclose any conflicts of interest.

- **Underwriting analysis.** As part of the application, conduct a financial underwriting analysis "of project/business financials for the proposed project."

- **Grant Contract.** After receiving a MIF grant from DEED, enter into a grant contract with DEED.

- **Loan Agreement.** After the grant contract has been finalized, enter into a loan agreement with the business.

- **Project Monitoring.** Submit required annual progress reports on the project to DEED.

- **Payment Requests.** Submit payment request documentation to DEED.

SOURCE: Office of the Legislative Auditor, based on Department of Employment and Economic Development, *State Minnesota Investment Fund Staff Manual* (undated).

agreement with the business), and in monitoring the business's compliance with MIF requirements.

Local governments sometimes struggle to fully understand their Minnesota Investment Fund program responsibilities.

For most local governments, MIF projects occur infrequently or on an irregular basis. More than half of the 314 Minnesota local governments that received awards through the MIF program since 1996 have had a single project. During that span of more than 20 years, only six local governments were approved for at least ten separate projects.[53] Consequently, cities may undertake MIF projects with a limited knowledge of program requirements.

DEED provides some helpful tools for local governments. In particular, DEED has a two-page checklist of items that must be completed as part of the MIF application process and templates for the MIF legal documents to which the local governments are signatories.[54]

On the other hand, DEED's assistance for some aspects of the local administrative role has been inadequate. For instance, the MIF application requires local governments to "conduct a financial underwriting analysis of project/business financials for the proposed project."[55] The application instructions provide no additional explanation of what such an analysis should entail, and officials in several cities told us they have struggled to comply with these requirements. In one city, local officials asked DEED to clarify the nature of financial underwriting and the standards that should be applied. Initially, DEED told the city officials that it would not specify how to do this analysis. Later, DEED sent the city a document called "Underwriting Guidelines," but each page had a watermark that said "DEED Use—Other Entities Must Develop Own Guidelines." The city's economic development director told DEED that it would be difficult for him to make a recommendation on the MIF project without further guidance from DEED regarding which standards to apply.

Officials we interviewed in 13 local agencies expressed mixed views about MIF's administrative requirements, but a majority expressed concern that certain aspects of the program are burdensome or unclear.[56] For example, in addition to concerns about the underwriting standards mentioned above, some local officials said they are unclear about which MIF loans qualify for forgiveness or the reimbursement requirements for the MIF program. Officials we interviewed in most local agencies described the MIF program as time-consuming or challenging for their staff to administer.[57] While some local governments rely on their own economic development, legal, or finance staff to administer MIF projects, others lack this internal expertise and use consultants or nonprofit organizations to help with parts of the process.[58]

The value of local governments' efforts to help administer MIF projects is not always apparent.

Despite the roles local governments play in administering MIF projects, DEED has primary administrative responsibility for the MIF program. It is not uncommon for DEED officials to discuss possible MIF projects with businesses before they discuss these projects with local governments. In subsequent stages, the local governments may act as go-betweens,

[53] Those local governments were the cities of St. Cloud (18 projects), Duluth (17), Rochester (11), Minneapolis (10), Brooklyn Park (10), and St. Paul (10).

[54] Although the key legal agreements are the grant contract and loan agreement, DEED also has templates for security agreements, promissory notes, and guaranties.

[55] DEED, "Minnesota Investment Fund Program (MIF) Application: State Funds" (revised March 20, 2017), 3.

[56] Most of the 13 local agencies in which we conducted interviews have had multiple MIF projects.

[57] In several cases, officials said MIF was more time-consuming for local staff than other economic development programs that have been used in their cities, such as the Job Creation Fund.

[58] One city told us that it pays $5,000 to $10,000 to obtain legal expertise for each MIF project, although the city usually negotiates to get the assisted companies to pay these costs.

facilitating communication between DEED and businesses. Local officials sometimes invest large amounts of time in administrative functions, such as preparing application forms or monitoring reports. But, at times, DEED has made key project decisions without much local input. In one case, a local official told us the considerable efforts of city staff were "meaningless." Economic development officials in another city said that when MIF projects are proposed for their city (sometimes with DEED's support), they generally support the projects even if they question their merits.

DEED performs some of the same administrative activities that it requires local governments to perform. For example, DEED requires local governments to conduct financial analyses of proposed MIF projects, but DEED staff conduct similar reviews. DEED also monitors MIF-funded projects to see whether businesses' job and wage commitments have been met, as do local governments.

Also, it is unclear that local governments obtain meaningful public input on MIF projects. DEED requires local governments to hold public hearings on MIF projects before applications for MIF funding have been submitted to DEED. But, until the application is completed, a project's details—such as proposed revenue sources, proposed uses of public funds, location, and timing—may be undefined. We reviewed one project in which even the company's name was not disclosed at the public hearing.

Local Revolving Loan Funds

State law has enabled local governments to benefit financially when MIF loans are repaid. The law says: "A local community or recognized Indian tribal government may retain 40 percent, but not more than $100,000, of a [MIF] grant when it is repaid…."[59]

DEED requires local governments to create revolving loan funds with their shares of repaid MIF loans, but the purposes and impacts of these funds are unclear.

State law does not specify that funds retained by local governments from repaid MIF loans must be used to create local revolving loan funds. In fact, the MIF statute does not even mention local revolving funds. However, DEED requires local governments to create revolving loan funds with money retained from MIF loan repayments. This requirement appears in the legally binding grant contracts that DEED enters into with local governments before disbursing MIF funds.

The MIF statute also does not specify how local governments may spend funds they retain from repaid MIF loans. State law says that MIF loans repaid to the **state** must be placed in a revolving loan account in the state treasury, and funds appropriated to DEED from this account "must be used in the same manner as are funds appropriated to the Minnesota [I]nvestment [F]und."[60] For MIF loans repaid to **local governments**, however, state statutes are silent. DEED has imposed its own requirements, declaring that local revolving funds seeded with MIF loan repayments must follow the same project selection and expenditure requirements that DEED follows when administering MIF projects.

[59] *Minnesota Statutes* 2017, 116J.8731, subd. 5.

[60] *Ibid*.

We used DEED records to identify all MIF awards since Fiscal Year 1997 that might have been used to create a local revolving loan fund. We then sent a questionnaire to each of the local governments involved in these projects.[61] Eighty-one of the 110 local governments (mostly cities) that responded to our survey told us they currently have a revolving loan fund created by retaining a portion of businesses' repaid MIF loans. According to the respondents, the amount in these revolving loan funds throughout the state totaled $10.85 million as of June 30, 2017.[62]

We asked survey respondents how many times in the past decade they spent money from their local revolving loan fund for any purpose.[63] As shown in the box below, the most common response was "never." One economic development director told us her city "tucked its revolving loan fund between the mattresses," to be used only as a last resort. Another economic development director told us that she was unaware, until recently, that her city even had a MIF-seeded local revolving fund. Some local government officials told us that the amounts in their revolving loan funds are too small to provide an attractive incentive to businesses. Others said that businesses can readily get loans from other private or public sources. In addition, some city officials said they do not have the staff required to administer and monitor business loans.

Most local governments said they rarely used their MIF-created local funds from 2008 through 2017.

Never	44%
One time	15
Two times	6
Three to five times	16
More than five times	11
Don't know	8

Many local governments said in our survey that they value their MIF-seeded revolving loan funds, but their historical use of the funds does not always support their survey responses. Among local governments with such funds, 56 percent described this fund in our survey as a "very important" local economic development tool; 32 percent said it was "moderately important" or "slightly important," and 6 percent said it was "not important."[64] But about one-fifth of respondents that described the fund as "very important" have not used it since at least 2008, and another one-fifth have used it only once.[65]

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[61] We sent questionnaires to 112 local governments and received replies from 110 (98 percent).

[62] This total is based on the amount that local governments said was in their "MIF-generated revolving loan funds," but we did not independently verify these amounts. The amounts reported by some local governments far exceeded the amounts that, by our calculations, were available to them through MIF loan repayments since 1996. However, it is plausible that some local governments created revolving loan funds before 1996 (under the program that preceded the MIF program, called the Economic Recovery Grant program), and these funds might have been included in the amounts reported to our office. Also, it is possible that some local governments have comingled funds from the state MIF program with funds from locally generated funds or funds from related programs (such as the "federal MIF" program and the MIF disaster recovery program).

[63] We asked about expenditures from July 2008 through June 2017. In our question about how many times local governments spent money from their local revolving funds, we asked respondents not to include expenditures made in response to 2017 legislation (described later in this section) that permitted expenditures for non-MIF purposes.

[64] In addition, 5 percent of respondents said "don't know."

[65] Sixty percent of survey respondents that have spent money from their revolving loan funds since 2008 said they used it for a loan or grant to a business not receiving any state assistance.

The 2017 Legislature authorized a "onetime exception to restrictions on use of Minnesota Investment Fund local government loan repayment funds."[66] The Legislature said that local governments could—between August 2017 and June 2018—transfer 20 percent of their uncommitted MIF balances to the state General Fund and be able to use the remaining 80 percent "as a general purpose aid for any lawful expenditure."[67] In effect, the Legislature temporarily voided the restrictions on local revolving loan funds imposed by DEED in exchange for a 20 percent penalty. Of the local governments with MIF-related revolving loan funds that responded to our survey, 19 percent said they intended to pay the 20 percent penalty and use some or all of their revolving loan funds for the general purposes authorized by the 2017 Legislature. As of January 2018, DEED told us that 13 local governments had received approval to use this provision of law. These governments will return about $321,000 to the state General Fund; in turn, they can spend nearly $1.3 million of their MIF revolving loan fund balances for locally determined purposes.

Recommendations

Local governments have made important contributions to MIF applications and project administration. However, it is not essential that local governments play these roles.

RECOMMENDATION

The Legislature should consider restructuring the Minnesota Investment Fund program so that loans are made directly by DEED to participating businesses.

The Legislature should consider removing the formal role of local governments in the MIF program. Under this streamlined process, DEED would make loans directly to businesses. Most of the activities necessary to complete a MIF project could be performed by the benefitting business or DEED staff. This approach would be similar to that used for another of DEED's commonly used business subsidy programs, the Job Creation Fund.

In our view, the requirement for a two-step process—in which DEED first grants money to a local government, and the local government then loans money to a business—is unnecessarily complicated. Such a process requires the development of two legal documents (a grant contract and a loan agreement) when a single document could suffice.

Another reason to increase DEED's involvement—and reduce that of local governments—is because MIF uses state money. Local governments do not have a strong incentive to carefully scrutinize the finances of MIF projects because MIF funding is not locally generated. DEED already reviews proposals for MIF projects, and it is reasonable to require DEED to bear full administrative responsibility for state appropriations made to DEED for this program.

Some local government officials told us they appreciate being a part of the MIF process, and we think this participation could continue informally. State law should require DEED to notify local governments of any MIF applications DEED receives for projects that would occur within their boundaries. During the application review process, DEED should solicit input from local governments. Also, perhaps there would be value in having local

[66] *Laws of Minnesota* 2017, chapter 94, art. 6, sec. 24.

[67] *Ibid.*

governments continue to participate in the process of monitoring businesses' compliance with MIF job and wage commitments.

We asked DEED about the feasibility of implementing a streamlined process (such as the one recommended here), and a DEED official told us this would require DEED to hire additional loan officers. Local governments do not receive state reimbursement for administrative costs they incur when preparing MIF applications or overseeing MIF projects, but we agree that DEED's workload would increase if it assumed responsibility from local governments for project administration duties.

RECOMMENDATION

The Legislature should consider amending state law to discontinue the practice of directing a portion of MIF loan repayments to local governments.

Earlier, we said that half of the local governments with MIF-seeded revolving loan funds told us they consider these funds to be important local economic development tools. However, the evidence indicates that many local governments have had difficulty finding useful ways to spend these funds. As a result, money sometimes remains in local revolving funds for years—as one local official told us, "out of sight, out of mind." In effect, many of the local revolving loan funds do not revolve. It is unclear how money that is never (or rarely) spent can be an important tool for economic development, despite the opinions of some local officials.

In addition, local revolving loan funds are not available to all communities. The only local governments that benefit from retaining a portion of MIF repayments are ones that (1) have already administered successful MIF projects and (2) received repayable rather than forgivable MIF awards. Cities such as Le Center, Plymouth, and Winona have local revolving loan funds, while cities such as Mankato, Minneapolis, and Moorhead do not. It is unclear whether the local governments that have been able to retain MIF repayments under current law have greater economic needs than those that have not.

Finally, it is hard to justify the continued diversion of MIF repayments to local governments without a greater sense of an underlying state purpose. State statutes have no provisions regarding MIF-related revolving loan funds, including the purposes for which funds may (or may not) be used.

The Legislature should consider amending *Minnesota Statutes* 2017, 116J.8731, subd. 5, so that all MIF loan repayments would replenish the Minnesota Investment Fund. State law says that funds repaid to the state's MIF revolving loan account must be used in the same manner as funds legislatively appropriated to the MIF program. If the Legislature directs all MIF loan repayments to go into the state's revolving MIF fund, the MIF program could subsidize additional projects or might need smaller state appropriations.

Chapter 3: Administration

As we discussed in Chapter 1, the laws governing the Minnesota Investment Fund (MIF) give the Department of Employment and Economic Development (DEED) considerable discretion to administer the program. In this chapter, we examine how DEED has used this discretion, drawing from our communications with program staff and our review of program files.[1] We recommend that the Legislature place more restrictions on MIF awards and that DEED generally tighten its MIF policies and procedures.

We begin with a discussion of the extent to which state law gives DEED guidance for administration of the MIF program. We then examine how the department has decided which businesses should get awards and how much they get. We conclude with a review of DEED's practices after the department has formally notified a business of its MIF award, including procedures for specifying business commitments and monitoring project outcomes.

Key Findings in This Chapter

- DEED's process for making Minnesota Investment Fund (MIF) awards is not transparent and does not use consistent criteria.
- DEED often allows businesses to pay workers at lower wage levels than those listed in their approved MIF applications.
- DEED allowed some MIF businesses to meet their commitments by counting hiring and expenditures that occurred before they received MIF awards.

Scope of Departmental Discretion

The MIF law is written very broadly. State law restricts MIF awards in only a few specific ways—it excludes retailers, casinos, and facilities for professional sports teams.[2] Other than these restrictions, almost any nonretail business could qualify under the law for almost any level of MIF funding up to $1 million for almost any increase in business activity. The law is silent on a number of key components of the program:

- **Aside from the $1 million limit and a matching funds requirement, the law provides no guidance on the size of MIF awards.** DEED is given complete responsibility to determine how much money to provide each business. There is no requirement that DEED provide similar amounts of money to businesses making similar job and investment proposals.

- **The law provides no guidance for when DEED should forgive a loan.** The law allows DEED to "forgive" MIF loans—that is, to tell a business it does not need to

[1] We systematically reviewed DEED's entire project files on 60 randomly selected MIF projects that received MIF awards in fiscal years 2012 through 2016. In addition, we less formally reviewed many other files or parts of files in the course of our evaluation.

[2] *Minnesota Statutes* 2017, 116J.8731, subds. 5-6. The restriction on retailers states that DEED may not award a MIF loan to "a store which is used solely or principally for retail sales." *Ibid.*, subd. 5.

repay the loan if it meets project goals—at its discretion.[3] As we discussed in Chapter 1, DEED agreed to forgive part or all of 74 percent of MIF loans in fiscal years 2013 through 2017.

- **The law directs DEED to consider economic vulnerability and distress when making award decisions, but does not explain how important that factor should be.** DEED uses economic distress in its scoring of potential MIF projects, but as we discuss below, this criterion does not have great impact because DEED assigns similar scores to economically strong and weak communities.

- **The law directs that money be used for "projects," but does not define what a project is.** It is unclear, for instance, how long a project can last, whether a business must apply for funding before beginning a project, whether a project can take place in multiple locations at once, or whether a project must involve capital investment.

- **The law does not limit how businesses can use the MIF funding they receive.** The law merely directs DEED to use MIF funding for "infrastructure, loans, loan guarantees, interest buy-downs, and other forms of participation with private financing."[4] Project files we reviewed showed that businesses used MIF awards for a wide variety of purposes, including real estate, construction costs, heavy equipment, office furniture, computers, vehicles, and exercise equipment.

Award Decisions

DEED staff make three key decisions about businesses seeking state assistance through MIF:

- **What businesses get state money?** Because the law's eligibility criteria are very inclusive, hundreds of businesses could conceivably be eligible (especially when the economy is strong and many businesses are considering new investments). DEED decisions about how to apply the criteria narrow the potential applicant pool.

- **How much money do businesses get?** Because the law is silent on award amounts (other than setting a maximum of $1 million), DEED must have a method of determining the size of each award.[5] For example, DEED could closely link the size of the award to the business's job and wage commitments. Alternatively, DEED could base funding amounts on factors unrelated to business promises, such as competing offers a business has received from other states.

- **Do businesses have to pay back the money they receive?** DEED decides whether to award a business a loan or a grant. Grants take the form of forgivable loans,

[3] *Minnesota Statutes* 2017, 116J.8731, subd. 3(1), and 116J.994, subd. 3(b). Under Minnesota law, the grantor of a business subsidy must require repayment with interest if the goals outlined in a business subsidy agreement are not met. *Minnesota Statutes* 2017, 116J.994, subd. 6.

[4] *Minnesota Statutes* 2017, 116J.8731, subd. 3. DEED may also use MIF funding to develop markets for renewable energy projects and to provide technical assistance to entrepreneurs.

[5] Although businesses list a projected MIF award amount in their applications, this amount has often been discussed with DEED staff before the application is sent. Thus, the amount requested in the application may or may not reflect the amount the business initially hoped to receive.

which DEED forgives only if the business meets specific goals outlined in the loan agreement.[6]

Scoring Criteria

According to DEED administrators, DEED bases the first of these three decisions—which businesses can participate in MIF—on its scoring of project proposals. Loan officers in DEED's Office of Business Finance use a four-page score sheet to score each application. As required by state rules, the score sheet is structured so that applicants can receive a maximum possible score of 600 points, with 400 points considered a passing score.[7] DEED scores applications on a rolling basis, so businesses do not directly compete against one another for MIF awards. Each application is scored on its own merits.

As we discussed in Chapter 1, state law lists many criteria for MIF project eligibility. However, the law enables a business to qualify by meeting a single criterion; it does not have to meet all of them.[8] DEED's score sheet addresses nearly all of the law's criteria, but their influence on a project's final score varies. Criteria such as job creation and the inducement of private investment can garner applications large numbers of points—up to 160 points and 150 points respectively (depending in part on interactions with other measures). However, other criteria listed in the law, such as support for microenterprises or the green economy, do little to advance a project to the 400-point threshold (a maximum of 10 points each).

DEED's application forms do not ask about some criteria DEED uses to score potential MIF projects.

Several sections of the score sheet require DEED staff to assign scores for information that is not directly requested by the application form. For example, DEED loan officers can award points to an application for "excessive public infrastructure beyond [the] means of [the] grantee" and "adds workforce skills (e.g. training, increased productivity)." Although these criteria are consistent with the statutory criteria, the application form does not ask about these possible components of a project, nor are they addressed by the required supplementary materials.[9] It is unclear how DEED staff assess whether projects meet these criteria.

DEED's score sheet also awards points for criteria not listed in the law at all. For example, applicants can earn points by establishing a local revolving loan fund or matching MIF funding with funding from local governments or nonprofit sources.

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[6] As we described in Chapter 1, local governments may keep 40 percent of a business's loan repayments up to a maximum of $100,000. Sometimes, a local government has forgiven the portion of the loan repayment it would receive while DEED requires repayment of the rest of the loan. It is also possible, although rare, for a local government to require repayment of its portion when DEED forgives the rest of the loan.

[7] *Minnesota Rules,* 4300.1901, subp. 3, published electronically January 18, 2005. As we explained in Chapter 1, businesses and local governments jointly submit applications—so "applicants" can refer to both.

[8] We noted in Chapter 1 that two of the eligibility conditions listed in the law are not sufficient by themselves; a proposed project must meet at least one other condition.

[9] *Minnesota Statutes* 2017, 116J.8731, subds. 4(1), (4), and (5).

DEED's scoring criteria for Minnesota Investment Fund applicants are easy to meet.

It is relatively easy for projects to achieve a passing score on DEED's scoring criteria. Applicants can receive many points for rather modest accomplishments. For example, applications receive 10 points for each job to be created up to a maximum of 100 points. As a result, a project proposing to create only 10 jobs gets the maximum possible points for job creation, one-fourth of the points needed to qualify for a MIF award. Another section assessing local economic needs has a maximum score of 40, but a minimum score of 32. Thus, even the best-performing local economy in the state would receive at least 32 points, or 8 percent of the points needed to qualify for a MIF award. The score sheet also gives 40 points (10 percent of the total points needed to qualify) to Greater Minnesota projects paying at least $11.00 per hour in base wages. Under the MIF law, the minimum allowable compensation for full-time employees was $13.01 per hour in 2017, so few projects with wages less than $11.00 per hour would likely be eligible at all.[10]

Some score sheet sections are based not on quantifiable measures, but rather on loan officers' assessments of claims made by MIF applicants. DEED staff have sometimes been quite generous in awarding these points to applicants. For example, we observed instances in which DEED awarded extra points for "economic vulnerability" to projects in suburban communities such as Cottage Grove, Eagan, Lake Elmo, Lakeville, Maple Grove, and Plymouth. Each of these cities has a median household income at least $20,000 higher than the statewide median household income.[11] DEED staff also award extra points for communities with a "unique situation," a scoring element intended to prioritize communities that have recently lost a large employer, suffered a natural disaster, or faced some other unusual challenge. Staff have awarded "unique situation" points to projects in communities such as Bloomington, Minnetonka, Plymouth, and Shakopee. These applications either contained no information supporting such a designation, or described hardly "unique" circumstances—such as a building that had stood vacant for several years.

DEED scoring decisions were occasionally puzzling when compared to the applications being scored. For one 2013 project in Anoka (using an older version of the score sheet), DEED awarded points for "need to attract and retain essential services" despite the city's statement in application documents that it was "a fully developed community with all essential services." DEED also awarded points for "out-migration due to lack of jobs," although the city bluntly stated that "Anoka doesn't experience out-migration due to lack of jobs." This application received exactly 400 points, meaning that any reduction in the points received would presumably have resulted in a denial.[12]

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[10] *Minnesota Statutes* 2017, 116J.8731, subd. 5. The statutorily required minimum compensation includes both wages and benefits. Thus, a business paying $11.00 per hour (or less) in base wages to full-time employees could still be eligible if it provided enough benefits.

[11] This comparison uses U.S. Census estimates based on 2011-2015 American Community Survey data. Statewide median household income was $61,492.

[12] Although DEED approved this project for a MIF award, it was eventually cancelled due to a company decision.

Provisional Award Decisions

As we discussed in Chapter 1, DEED staff usually have preliminary conversations with businesses and local governments before a MIF application is submitted. DEED staff discourage potential applicants when projects appear to be ineligible or unpromising. However, when projects appear likely to succeed, DEED staff may make actual offers of assistance.

DEED staff sometimes make provisional award decisions before receiving an application.

As part of initial conversations, DEED staff have sometimes provided businesses with award amounts and forgiveness decisions before receiving complete application materials or scoring the applications.[13] In some of these instances, DEED administrators sent formal letters advising the businesses that they were "approved" to receive a specific amount of money. In others, DEED staff suggested award amounts in meetings or e-mail correspondence. In the 60 project files we reviewed, DEED offered preliminary award decisions over a dozen times.

The letters DEED sends to businesses usually state that these preliminary award amounts and forgiveness decisions are contingent on the department's review of the completed applications. However, file documents and e-mail communications suggest that DEED staff may view these early proposals as departmental commitments. In a document from one project file, a DEED staff member, apparently writing to a colleague, tried to clarify conflicting information that had been provided to a company about its award package:

> ...the plan was for 30 jobs to be created and there would be a $150,000 forgivable loan. It was our take at yesterday's meeting [with the company and the city] that the loan was not forgivable…. There was an e-mail on June 18, 2014, from [a city representative]…referring to the loan as being forgivable…. In a letter from [Deputy Commissioner McKinnon] dated February 25, 2015, MIF is mentioned at $150,000—with no mention that it would be forgivable. Do you have any recollection that this is indeed a forgivable loan?[14]

This note, written a month before DEED scored the application, showed DEED staff trying to sort out what decisions DEED had already made and communicated to the company. (DEED eventually awarded the company a $135,000 forgivable loan.)

In another example, DEED staff proposed a forgivable loan to a business shortly after an initial meeting of representatives from the business, the city, and DEED.[15] As the city was

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[13] By "complete" applications, we mean that all components of the application were completed and DEED loan officers could formally score the project. Because DEED requires many supplementary materials to complete an application (such as a resolution of support from the local government and formal letters of commitment from other lenders financing the project), applicants may take some time to submit all application materials.

[14] Unlabeled and undated communication appearing in DEED's project file for DataBank, Ltd. (Eagan). The communication refers to a meeting "yesterday, March 17, [2015,]" that included representatives from the business, the city, and "myself from DEED."

[15] The business had contacted DEED directly to ask about business incentive programs; the city was not part of the initial conversations.

preparing the application, it notified DEED that it intended to suggest a MIF loan without forgiveness; city staff believed the business was having a short-term cash flow problem and would easily be able to repay a loan over time. A senior DEED loan officer balked, writing in an e-mail:

> It appears to me we are changing the terms of the loan and the commitment made previously…. The government entities offered to forgive the loan to encourage the business to expand.[16]

After the city protested that it would not receive any money in its revolving loan fund with a forgivable loan, another DEED staff member replied that the city could require repayment of the 40 percent of the loan that would come back to the city. However, he indicated that DEED intended to forgive the portion of the loan that could be repaid to the state. As in the previous example, this exchange of correspondence occurred before DEED had received and scored the completed application.

In a third example, DEED issued a news release about a new medical device facility to be built in Minnesota, stating in the release that "DEED provided the company with a $1 million forgivable loan from the Minnesota Investment Fund." The release was issued four months before DEED made its official award decision.

DEED's practice of providing preliminary award decisions before the application process is complete suggests that key decisions about MIF eligibility and award amounts may be made *before* the application and scoring process begins, when DEED staff encourage or discourage businesses from pursuing applications. This perception is reinforced by the fact that DEED has given a passing score to every MIF application it has formally evaluated in the past 15 years.

Transparency

DEED requires businesses and local governments applying for MIF to fill out an extensive application form and provide many supporting documents. However, DEED does not document how—or whether—it uses these forms and documents to make decisions about potential participants.

DEED's process for making Minnesota Investment Fund award decisions is not transparent.

DEED's documentation of its decision-making processes is minimal. For example, the department's project files contain no documentation of how it makes the provisional decisions we describe above. We could not determine what information the department had considered (or even what information it had received) when making provisional decisions. Although DEED does retain the score sheets it uses in making official award decisions, the score sheets frequently contain only the point values assigned by DEED staff. For components of the score sheet that are based on the judgment of loan officers, there is rarely any evidence of DEED's rationale.

[16] Brad Simenson, DEED Office of Business Finance, e-mail message to Linnea Graffunder-Bartels, City of Oakdale, "Re: proposed loan structure for Oakdale MIF," August 11, 2017.

DEED's decision-making processes regarding the size of MIF awards and whether to offer loan forgiveness are completely opaque. Our reviews of project files revealed very little documentation regarding the size or forgivability of individual awards; most files contained no documentation at all. When we asked DEED staff to review specific files and explain the reasoning behind award decisions, we did not receive satisfactory answers. For one award decision that we questioned, a written reply listed a number of qualitative factors, including DEED's concern that the company might reduce its existing Minnesota employment in favor of other locations, and concluded, "the factors noted above as well as negotiations with the company and city landed us at $400,000." The reply was simply an assertion that the final decision was the right one. DEED provided no information justifying that $400,000 was a better figure than $200,000 or $650,000 or $1 million.

The director of DEED's Office of Business Finance told us that the size of awards is based in part on DEED's scoring of MIF applications. If so, it is apparently an unrecorded process. In the 60 MIF files that we reviewed, we could not find documentation of a single instance where DEED staff referred to a score when discussing or determining the size of an award.

Similarly, DEED usually grants loan forgiveness to companies without retaining any written documentation of, or justification for, the decisions. To the extent that we found any information in DEED project files about how these decisions were made, it was generally incomplete and scattered within e-mail correspondence.

Considering that we were unable to determine how DEED makes decisions about award size and loan forgiveness with complete access to its files, it is unlikely that stakeholders understand the basis for DEED's award decisions. DEED does not publish the criteria it uses to approve applications, determine award sizes, or make loans forgivable. For example, it does not publicize its 600-point score sheet on its website or provide it to potential applicants.[17] DEED has twice changed the score sheet in the past five years without notice to applicants. We asked the program's director for written documentation of why changes were made to the score sheet and were told that none existed.

DEED's lack of transparency is inconsistent with statewide grant policies. The Office of Grants Management in the Department of Administration publishes policies for all state departments to use when making grants.[18] For competitive grants, these policies require that potential applicants be informed of the amount of money available for distribution, the award selection criteria and the weight of each criterion, and a description of the review process.[19] DEED does not publish any of this information for the MIF program.

[17] Score sheets are public documents; lawmakers or other interested members of the public could obtain them by making a request under the Minnesota Government Data Practices Act.

[18] See *Minnesota Statutes* 2017, 16B.97, subd. 4(a)(1).

[19] Staff in the Office of Grants Management (OGM) told us that MIF awards should be viewed as competitive grants or a sort of hybrid competitive grant. DEED's internal program manual states that MIF awards are sole source grants. OGM defines a sole source grant as "a type of noncompetitive grant that is awarded to an entity because it is the only provider of a particular service" (Office of Grants Management, Policy Number 08-07). Since DEED issues MIF awards to multiple companies each year, we do not see how this definition applies. OGM staff also agreed that MIF awards are not sole-source grants.

Consistency

DEED staff make award decisions on a case-by-case basis. Exhibit 3.1 displays DEED's written guidance on setting loan amounts and determining loan forgiveness. DEED loan officers use the grid at the top of the exhibit to determine a starting point for award amounts and loan forgiveness based on the number of jobs the business intends to create, the wage level for those jobs, and whether the project will be in the seven-county Twin Cities metropolitan area or in Greater Minnesota. The loan officers may then deviate from this starting point based on additional factors, such as high wage levels or competition with an out-of-state location.

DEED does not use consistent criteria to determine the size and forgivability of Minnesota Investment Fund awards.

This case-by-case approach means that decisions regarding MIF award amounts and forgiveness are largely subjective. Most of the awards in the files we reviewed deviated significantly from the grid shown in Exhibit 3.1. For example:

- DEED gave a forgivable $850,000 award to Arctic Cat, Inc., in Thief River Falls for a project that proposed to create 39 jobs paying an average hourly wage of $15.52. Using DEED's grid, this project was eligible for $5,000 per job, but DEED provided nearly $22,000 per job.

Exhibit 3.1: DEED Guidelines for Minnesota Investment Fund Award Size, 2017

	Size of MIF Award per Job Created	
Location of Projects and Wages of Proposed Jobs	If Loan is Nonforgivable	If Loan is Forgivable
Outside the Twin Cities Area		
Jobs paying wages of $11 to $12.99 an hour	$16,000 per job	$4,000 per job
Jobs paying wages of at least $13 an hour	$24,000 per job	$5,000 per job
In the Twin Cities Area		
Jobs paying wages of $14 to $18.99 an hour	$16,000 per job	$4,000 per job
Jobs paying wages of at least $19 an hour	$24.000 per job	$5,000 per job

Deviation from Guidelines and Forgiveness Factors

- Capital Expenditures – Significant levels of capital expenditure
- Wage Levels – Relatively high wage levels for area
- Job Creation – High levels of job creation
- Local Conditions – Economically distressed area or other mitigating factors
- Competition – Likelihood of business expanding outside state

NOTES: We have edited many of the labels for greater clarity (for example, substituting "Capital Expenditures" for the original document's "Cap Ex.") We have also omitted two sections detailing statutory requirements for minimum compensation and prevailing wage. Other than those changes, the grid and bullet points above constitute DEED's entire written policies on MIF award size and loan forgiveness.

SOURCE: Department of Employment and Economic Development.

- DEED gave a nonforgivable $200,000 award to AlixaRX in Eden Prairie for a project proposing to create 66 jobs that would pay an average hourly wage of $22.65. Using DEED's grid, this project was eligible for $24,000 per job, but DEED provided about $3,000 per job.[20]

The director of DEED's Office of Business Finance defended such wide variations in an e-mailed response to questions from our office:

> It is essential to emphasize that given the complexity of each business transaction, it is impossible to develop a standard algorithm or formula to arrive at an award. We have guidelines, but state and local economic conditions, wage levels, interstate competition, current and future operations are just a few of the factors that need to be considered when developing a proposed award.[21]

Exhibit 3.2 illustrates how DEED has made different decisions for similar projects. While we cannot reproduce comprehensive information on each project, the exhibit presents the summary information given to the DEED commissioner at the time of final approval of three different MIF awards. Because the DEED commissioner has final authority, we assume that all key information relevant to the award decisions was included in these summaries.[22]

The first two projects in the exhibit (Entrust Datacard Corporation and Olympus America (Gyrus ACMI)) were very similar, each proposing to create 100 jobs at an average wage close to $24.00 per hour. Under DEED's grid from Exhibit 3.1, each would be eligible for a forgivable award of $500,000. However, DEED awarded Olympus America twice that amount, providing the maximum amount allowed by law. The major differences between the two projects appear to be that Olympus America was prepared to commit much more money to its project and that its project involved manufacturing.[23]

However, if these distinctions were the deciding factors, then DEED's award to Viracon (the third project shown in Exhibit 3.2) is not easily explained. Although it was also a manufacturing project, Viracon was not spending as much money as Olympus America and its wages were much lower. Further, the Viracon narrative does not contain the same hints of additional jobs beyond the 100 promised that appear in the Entrust Datacard Corporation and Olympus America narratives. Yet Viracon also received $1 million, the maximum amount possible.[24]

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[20] This project was later cancelled.

[21] Bob Isaacson, DEED Office of Business Finance, e-mail message to Joel Alter, David Kirchner, and Madeline Welter, Office of the Legislative Auditor, "Follow-up," September 29, 2017. In a further communication with our office, Mr. Isaacson noted that such factors may not be well documented in DEED's files.

[22] In addition to the written summaries, DEED staff discuss all MIF awards with the commissioner in person.

[23] After reviewing a draft of this report, DEED staff noted that another reason for the Olympus America award amount was that Minnesota was competing with another state for this project. If so, DEED staff did not mention the competition in the documentation provided to the commissioner at the time of the award decision. Further, there is no mention of competition with another state in the project application or the e-mail correspondence DEED retained in its files. The company eventually decided not to accept the subsidy due to discomfort with certain program requirements. However, it proceeded with the project in Minnesota anyway, suggesting that the MIF award had not been a crucial factor in the company's decision to locate the project in Minnesota.

[24] Viracon was also eligible to receive $500,000 based solely on the grid shown in Exhibit 3.1.

Exhibit 3.2: Summaries for Three Minnesota Investment Fund Projects

The projects below each promised to create 100 jobs. The information provided is taken from the summary information DEED staff provided to the DEED commissioner for her final approval.

Entrust Datacard Corporation

Location: **Shakopee**
Award: **$500,000 (forgivable)**
Year: **2015**

"The project includes the expansion and remodeling of a 400,000 sq. ft. corporate office building. Upon completion, the business will relocate all 680 permanent FTE employees from their current Minnetonka location, as well as 100 new FTEs. Additionally, the business will locate its MultiWeb operations and employees, as well as an external third-party warehousing operation to the new location…. The project will create 100 new jobs in the City of Shakopee (on top of the 680 existing jobs being relocated from Minnetonka), with the average hourly wage of these new jobs being $23.58 per hour plus a minimum of $4.79 per hour in employer paid benefits. These new 100 jobs will have a cumulative payroll and benefits of approximately $6,522,880 per year."

Project Total Cost	$15.2 million
Other Financing	—
Base Employment	680
Jobs To Be Created	100
Average Wage	$23.58
Average Benefits	$ 7.78
Average Total Comp.	$31.36
Lowest Wage	$13.74
Lowest Benefits	$ 4.54
Lowest Total Comp.	$18.29
Subsidy Per Job	$5,000

Olympus America (Gyrus ACMI)

Location: **Brooklyn Park**
Award: **$1,000,000 (forgivable)**
Year: **2014**

"The first phase consists of the construction of a 181,000 sq. ft. building. The high tech facility includes research and manufacturing/assembly (86,000 sq. ft), warehouse (38,500 sq. ft), and office (55,900 sq. ft.). The facility will include an innovation center for new product development. The project team has created a site plan that showcases the building and also minimizes the parking and loading dock views. The landscape plan has been designed to help enhance the building's architecture. The site is being planned for possible expansion that includes an additional 100,400 sq. ft. building and another 122 parking stalls…. Project will create 100 new jobs in the City of Brooklyn Park at an average cash wage of $24.54 per hour plus $8.19 of employer paid benefits."

Project Total Cost	$37.2 million
Other Financing [city]	$1 million
Base Employment	265
Jobs To Be Created	100
Average Wage	$24.54
Average Benefits	$ 8.19
Average Total Comp.	$32.73
Lowest Wage	—
Lowest Benefits	—
Lowest Total Comp.	—
Subsidy Per Job	$10,000

Viracon

Location: **Owatonna**
Award: **$1,000,000 (forgivable)**
Year: **2016**

"The project consists of Viracon investing $25 million in equipment and creating 100 new jobs in Owatonna. MIF financing is necessary for this project so Viracon can grow to keep pace with the highly competitive glass fabricating market and design a larger size specification than currently available to Viracon to compete in the global market to offer alternative to the growing depend of fabrications and size [sic]. The financing will enable [the company to] purchase equipment, hire and train a significant number of new employees."

Project Total Cost	$26 million
Other Financing	—
Base Employment	1,387
Jobs To Be Created	100
Average Wage	$15.00
Average Benefits	$ 3.00
Average Total Comp.	$18.00
Lowest Wage	$12.80
Lowest Benefits	$ 3.00
Lowest Total Comp.	$15.80
Subsidy Per Job	$10,000

NOTES: Corporate overviews and DEED's assessment of the companies' financial health are omitted from the narratives. Quotations include minor grammatical corrections. The different benefit amounts in the table and narrative above for Entrust Datacard Corporation appeared in the original document.

SOURCE: Department of Employment and Economic Development, "review summaries" contained in MIF project files.

DEED's decisions regarding loan forgiveness have been somewhat more consistent than its decisions regarding award size—because DEED has recently forgiven most loans. In fiscal years 2014 through 2017, for example, all but two businesses proposing to create more than 75 jobs were granted full forgiveness (the two exceptions received $1 million awards and partial forgiveness).

For projects proposing to create fewer jobs, DEED's forgiveness decisions have varied for unclear reasons. For example, in 2015, DEED made forgivable all of a $700,000 award to Price Mechanical, Inc., in Maple Grove for a project proposing to create 31 jobs at an average wage of $26.97 per hour. But DEED required full repayment of a $750,000 award to Sil-Pro, LLC, in Delano for a project that would create 32 jobs at an average wage of $22.40 per hour.

Recommendation

DEED has provided MIF loans and grants to businesses with only broad legislative guidance since the program was instituted in 1996. For many years DEED's award decisions were constrained by lack of funding. As we showed in Chapter 1, legislative appropriations for MIF were less than $5 million per year throughout the 2000s and early 2010s, and in several years the Legislature appropriated no money at all.

The Legislature's renewed commitment to funding MIF starting in Fiscal Year 2014 has enabled DEED to increase both the number of MIF awards and the amount of money distributed to businesses. In our view, this increased funding should be accompanied by increased scrutiny of the department's decision making.

RECOMMENDATION

The Legislature should require DEED to publicly specify:

- **The criteria that determine which businesses will receive MIF awards.**
- **The criteria that determine the amount of money a business will receive.**
- **The circumstances under which DEED will forgive MIF loans.**

In general, expenditures of state money for any purpose should be transparent, consistent, and governed by explicit policies. These expectations are especially important when the state spends money to directly benefit private businesses. Further, the benefit conferred by a forgivable loan is substantially greater than the benefit from a loan that must be repaid. Thus, the need for transparency and policy-driven decisions regarding loan forgiveness is even greater.

DEED's current decision-making process raises significant questions. DEED's authority is very broad, its awards vary widely, and its documentation is inadequate. The Legislature should require DEED to set clear criteria governing its MIF award decisions. The criteria should be specific enough that a person knowing sufficient details about a project would be able to predict the approximate award DEED would provide and whether the loan would be forgivable.

DEED should not only set these criteria, it should publish them. The Office of Grants Management requires that state entities making competitive grants publicly describe their application review processes and list the criteria used to evaluate applications. Whether or not MIF formally fits the definition of a "competitive" grant program, we believe these are reasonable guidelines to ensure transparency, and DEED should follow them. The basis for MIF award decisions should be clear to businesses, legislators, and the general public. For individual awards, DEED should retain in its project files clear rationales for why it made an award, why it awarded the amount it did, and (if applicable) why it made the loan forgivable.

The Legislature may wish to consider tightening the criteria for MIF awards that currently appear in law. It is appropriate for the Legislature to set broad criteria and delegate administrative details to state agencies. However, as we noted at the beginning of this chapter, the current statutory criteria for MIF awards are so broad that an award can be justified for almost any increase in business activity. The Legislature may wish to specify that certain criteria should have more weight than others, for example.

The Legislature may also wish to place some restrictions on DEED's discretion. The Legislature could specify ranges or thresholds—for example, stating that a business cannot receive more than a certain amount of money per job created, or that a business must create a minimum number of jobs at a certain wage threshold in order to receive loan forgiveness. Alternatively, the Legislature could place limits on the number, size, or type of awards that DEED makes. For example, the Legislature could limit DEED to a total dollar amount of forgivable loans in a single fiscal year. Some policymakers have questioned the appropriateness of forgivable loans altogether; the Wisconsin Legislature outlawed loan forgiveness by that state's counterpart to DEED in 2017.[25]

Procedures Following Award Decisions

After DEED makes a formal MIF award decision, DEED and local government staff perform various tasks to guide the business through the program and ensure that it meets state requirements. These tasks include, for example, developing legal contracts, monitoring businesses to ensure compliance, and reviewing invoices and receipts submitted by businesses for reimbursement. We have a number of concerns about these activities.

Legal Documents

Because MIF is structured as a state-local program (as described more fully in chapters 1 and 2), DEED and local government staff prepare two key legal documents following an award: (1) a grant contract between the state and the local government that outlines the conditions under which DEED will transfer money to the local government, and (2) a loan agreement between the local government and the business that outlines the conditions under which the local government will loan money to the business. Although DEED is not a party to the loan agreement, the grant contract tightly restricts its content. Further, DEED

[25] 2017 Wisconsin Act 59, section 1771, codified in *Wisconsin Statutes* 2017, 238.124. DEED staff noted, however, that the Wisconsin Legislature simultaneously expanded other forms of business subsidies.

provides local governments with loan agreement templates and approves all loan agreements before they are signed.[26]

Wage and Benefit Levels

MIF loan agreements state that businesses must create a specified number of new jobs (or in some instances, retain a specified number of existing jobs). The agreements also detail the minimum wages and benefits employees in these new positions must earn.

DEED often allows businesses to pay workers at lower wage levels than those the businesses proposed in their MIF applications and on which DEED based its award decisions.

DEED staff rely on the hiring and wage proposals in a project application when making decisions regarding project approval, award amount, and loan forgiveness. For example, proposed wage levels are a part of the project summary that DEED staff present to the commissioner for final approval of MIF award decisions.

However, after DEED makes its award decisions based on the wage levels proposed in applications, it often allows businesses to pay workers at lower wage levels and still meet their MIF hiring obligations. Of the 104 projects between fiscal years 2008 and 2017 where a loan agreement was signed, DEED allowed 62 businesses (60 percent) to commit to lower wages in their loan agreements than the wages on which DEED staff had based their MIF award decisions. In many instances, DEED scored the application and made an award decision based on the *average* wages a business expected to pay new workers—but it then held the business accountable for keeping all wages above a much lower *minimum* threshold.[27] As we show in Exhibit 3.3, these differences have often been quite substantial.

For example, DEED awarded Geringhoff in St. Cloud a $500,000 forgivable loan based in part on the business's proposal to pay new employees average compensation (wages and benefits) of $26.23 per hour. However, the company's DEED-approved loan agreement with the City of St. Cloud only required the business to pay its employees at least $12.45 per hour in wages and benefits.[28]

[26] The 2013 Legislature gave DEED the authority to make MIF loans directly to businesses instead of working through a local government, in which case DEED would be a party to the loan agreement. *Laws of Minnesota* 2013, chapter 85, art. 3, sec. 4, codified in *Minnesota Statutes* 2017, 116J.8731, subd. 2(a). However, as of December 31, 2017, DEED administrators reported that the department has not yet used this authority.

[27] DEED staff noted that in some instances, businesses also received assistance from other DEED programs—such as JOBZ—and wage levels may have been based on the requirements of those programs.

[28] Geringhoff eventually had difficulty meeting its hiring goals and had to repay a portion of its MIF award to DEED. DEED allowed the business to keep a prorated portion of its MIF award based on the employees it did hire. According to DEED records (drawn from self-reported information from the business), all of those employees met the minimum $12.45 threshold for total compensation. The average compensation, however, was $24.25, below the original average wage proposed by the company at the time DEED made its award decision.

Exhibit 3.3: Proposed and Required Compensation Levels for Selected Minnesota Investment Fund Businesses, Awards Made Fiscal Years 2012-2016

Business	Location	Proposed Average Hourly Compensation for New Jobs	Proposed Minimum Hourly Compensation (if listed)	Minimum Hourly Compensation Required by Loan Agreement
C4 Welding, Inc.[a]	Sauk Rapids	$24.85		$17.32
Cytec Engineered Materials, Inc.	Winona	25.97	$25.00	12.45
Entrust Datacard	Shakopee	31.36	18.29	18.29
Geringhoff	St. Cloud	26.23		12.45
Corvida Medical, Inc. (J&J Solutions)	Eagan	41.23	17.70	17.50
The Kraft Heinz Company	New Ulm	30.00	25.00	23.00
Link Snacks, Inc.[a]	Minneapolis	52.48		24.00
Louis Industries, Inc.	Paynesville	17.70		12.45
Acucraft Fireplaces (The Maxson Company)	Big Lake	25.85	20.00	18.00
NatureWorks, LLC	Minnetonka	48.50	35.00	24.00
Northland Process Piping	Mora	19.72	16.44	14.04
Price Mechanical, Inc.	Maple Grove	36.00		24.00
Prime Therapeutics, LLC[a]	Eagan	36.43		13.00
Rosemount, Inc.[a]	Shakopee	36.70		14.50
Sil-Pro, LLC	Delano	25.35		14.50
Smiths Medical	Plymouth	56.19	16.88	16.88
Tata America International Corporation	Bloomington	22.00		13.00
The Toro Company	Bloomington	34.50		13.00
Verndale Custom Builders	Verndale	20.08	18.00	12.82

NOTES: Compensation includes wages and benefits. Proposed compensation levels were those DEED considered when making award decisions. However, companies were legally bound to the requirements in loan agreements between the local government and the business; DEED approved all agreements. A few loan agreements we reviewed required businesses to meet both minimum and average compensation levels. The agreements listed above only required minimum compensation levels except the Corvida Medical agreement, which required that the business pay employees an average of $20 per hour in total compensation.

[a] These businesses received more than one MIF award at this location during this time period. Only one of the awards is shown.

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

RECOMMENDATION

DEED should require businesses to meet the employee wage and benefit levels the department considered when making MIF award decisions.

DEED's current application process creates an incentive for businesses to list highly optimistic wage and benefit levels in their applications. All other things being equal, a project with high wage levels is likely to receive a larger award, and is more likely to receive loan forgiveness. Once DEED has committed to a sizeable award, the business can instead meet the lower wage thresholds DEED has demonstrated it is willing to accept.

DEED should ensure that loan agreements list the wage and benefit levels that were used by the department in making the award decisions.[29] DEED should detail the business's expected obligations in the formal award letter that it sends after making award decisions. If a business is no longer willing to commit to those wage and benefit levels when the loan agreement is finalized, DEED should reassess the award amount and any loan forgiveness (and possibly the award itself) based on the wages the business will actually agree to pay in a binding contract. Any changes should be documented in a new award letter and in the project file.

The statutory language requiring assisted businesses to pay employees at or above a minimum threshold is ambiguously worded.

The MIF statute requires that participating businesses "pay each employee total compensation, including benefits not mandated by law, that on an annualized basis is equal to at least 110 percent of the federal poverty level for a family of four."[30] The U.S. Department of Health and Human Services sets the federal poverty guidelines; for a family of four in 2017, the poverty guideline was $24,600.[31] Thus, 110 percent of this amount was $27,060. An employee working 2,080 hours per year would have to earn $13.01 per hour to reach this threshold.[32]

This requirement is ambiguous in three distinct ways.

First, the law requires that participating businesses pay "each employee" the minimum compensation threshold. MIF loan agreements typically apply the minimum compensation threshold to new jobs that the assisted business agrees to create. DEED staff told us that the department interprets the threshold to apply to all new employees associated with a MIF project.[33] However, the plain wording of the statute—"each employee"—could apply to *all* employees of the MIF-assisted business, including existing employees.

Second, the phrase "on an annualized basis" is open to multiple interpretations. It could mean that the Legislature intended that individuals working for MIF businesses should receive no less than 110 percent of the federal poverty guideline over the course of a year—that is, an employee earning less than $27,060 in 2017 would be below the threshold. In this interpretation, employees working full time, or 2,080 paid hours annually, would have to earn a minimum of $13.01 per hour to meet this threshold. However, part-time

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[29] In grant contracts and loan agreements, DEED should consider specifying median wage levels rather than averages. Averages can be disproportionately affected by one or two highly paid employees, such as plant managers or other executives.

[30] *Minnesota Statutes* 2017, 116J.8731, subd. 5.

[31] Technically, the thresholds published by the U.S. Department of Health and Human Services are called the "U.S. Federal Poverty Guidelines," not the federal poverty level. See U.S. Department of Health and Human Services, Office of the Assistant Secretary for Planning and Evaluation, "Poverty Guidelines," https://aspe.hhs.gov/poverty-guidelines, accessed October 23, 2017.

[32] DEED uses 2,080 hours per year in its definition of a full time equivalent in its standard loan agreement.

[33] Despite stating that this was the department's interpretation, DEED staff acknowledged that they did allow businesses to pay some new employees below the threshold in a few projects we reviewed—for example, because they were seasonal or part-time employees that the business did not intend to count towards its hiring goals.

employees, who work less than 2,080 hours, would have to earn more per hour in order to meet the requirements of the law.

DEED interprets “on an annualized basis” differently, taking it to mean that any position paying at least $13.01 per hour in 2017 is acceptable, regardless of whether the position is part time or full time. In this interpretation, the hourly wage is “annualized” by calculating what the employee would receive if she or he worked full time for an entire year.

In our detailed file reviews, we encountered two instances where DEED allowed businesses to count part-time employees towards their MIF obligations who would not have earned at least 110 percent of the federal poverty guideline if interpreted as an annual—rather than hourly—amount.[34] In a third instance, file correspondence showed a DEED loan officer allowing a business to count seasonal workers for the purposes of meeting its MIF requirements; again, these workers would not have earned the statutory minimum if interpreted as an annual amount. In the same file, a related e-mail from a DEED administrator commented that MIF could “work with” seasonal jobs.[35]

Third, the law is ambiguous in that it does not explicitly state whether MIF businesses that are paying their employees at the minimum threshold should increase their pay rates as the federal poverty guideline changes. Each year, the Department of Health and Human Services adjusts the poverty guidelines to account for changes in the cost of living. Thus, the minimum compensation threshold has steadily risen since the law was passed, from $17,160 in 1996 to $27,060 in 2017.

The law states that a business “receiving [MIF] grants or loans” must pay each employee an amount “equal to at least 110 percent” of the federal poverty guideline. This could mean that a business must pay at least 110 percent of the federal guideline the entire time that it is in the MIF program, increasing its wages as necessary to stay at or above the threshold. On the other hand, it could mean that the business must pay at least 110 percent of the federal guideline in place at the time the business reaches the deadline to meet its hiring obligations. Yet another possible interpretation is that the business is only required to pay its employees at least 110 percent of the federal guideline at the specific point in time it receives the MIF loan.

Under DEED’s interpretation of the law, businesses do not have to continuously pay employees at or above the statutory threshold starting with their entry into the MIF program. Instead, they are only required to show their compensation meets the threshold at the point they reach the hiring deadline listed in their loan agreements. However, the threshold that DEED uses is not 110 percent of the poverty guideline in place at the time DEED enforces the requirement, but rather 110 percent of the guideline that was in place at the time DEED made the award decision.

For example, DEED awarded a $107,500 MIF loan to Ice Castle Fish Houses (American Surplus and Manufacturing) in Pine River, providing formal notice in January 2014. The loan agreement, dated a month later, required the business to create 20 new full-time-

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[34] In one of these cases, DEED staff agreed to count part-time employees but then discovered they had misunderstood the business’s self-reported data. The business had no part-time employees—the business was reporting full-time employees that had worked for only part of a year.

[35] DEED’s willingness to allow seasonal workers has varied. Less than two weeks after this e-mail, a DEED representative e-mailed a different MIF applicant that it could not count seasonal workers. Currently, DEED’s standard loan agreement prohibits businesses from using seasonal workers to meet MIF hiring obligations.

equivalent jobs paying at least $12.45 per hour in wages and benefits. This compensation level was consistent with the statutory threshold using the 2013 federal poverty guideline ($12.45), but was already below the statutory threshold using the new 2014 federal poverty guideline ($12.61) released in January 2014.[36] When DEED checked the business's progress at the end of the project's reporting period in 2017, increases in the federal poverty guideline had moved the statutory threshold to $13.01 per hour.

However, when DEED reviewed the project at the end of the reporting period, it did not require the business to pay its employees at least 110 percent of the 2017 poverty guideline for a family of four. Instead, it enforced the loan agreement—which required that the business pay employees at least 110 percent of the poverty guideline *from four years earlier*. In fact, Ice Castle Fish Houses was not paying this lower level of compensation for all its new employees, leading to DEED sanctions.[37]

Most businesses in the MIF program have promised in their loan agreements to pay substantially more than 110 percent of the federal poverty guideline. However, a significant minority only promised to pay at least the minimum amount required by DEED's interpretation of the law. From fiscal year 2008 through 2017, 104 businesses both received MIF awards and signed loan agreements with local governments before December 31, 2017. In over 20 percent of these loan agreements, the minimum compensation threshold listed in the agreement was set at or below the minimum amount required by DEED's interpretation of the law.[38] In recent years, however, loan agreements have required higher wage levels. For all projects with award decisions in fiscal years 2016 and 2017, loan agreements listed minimum compensation levels at least $1.00 per hour higher than DEED's interpretation of the statutory minimum.[39]

RECOMMENDATION

The Legislature should clarify the minimum compensation threshold in the MIF statute.

When DEED monitors business compliance with MIF loan agreements, it interprets the law as establishing a minimum compensation provision for new employees only, not existing employees. The Legislature may have originally intended the provision to apply to new employees only, but the plain language of the law creates potential confusion. We recommend that the Legislature amend the statute to clarify which employees are affected by the statutory threshold.

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[36] Annual Update of the HHS Poverty Guidelines, 79 *Federal Register*, p. 3,593 (2014). For the purposes of discussion, we use DEED's interpretation of "annualized basis" in this example—that is, the minimum threshold is an hourly amount, not an annual one.

[37] DEED gave the business a choice; it could (1) increase wages to $12.45 retroactive to the date of its hiring deadline for some of its new employees that were earning less than that amount or (2) immediately repay part of its MIF loan. The business chose to increase employee pay as DEED suggested.

[38] Similar to the Ice Castle Fish Houses example, we found two other instances where DEED set the minimum compensation threshold based on the federal poverty guideline for the year prior to the date of the award decision. Additionally, for two 2008 MIF projects, the minimum compensation thresholds in the loan agreement were far below the statutory requirement.

[39] For some projects in this time period, loan agreements had not yet been completed as of December 31, 2017.

The Legislature should also rewrite the ambiguously worded phrase "on an annualized basis" to more clearly express its preferences regarding the minimum compensation threshold. The law should clearly state whether DEED should enforce the minimum threshold based on minimum *hourly* compensation ($13.01 per hour in 2017) or minimum *annual* compensation ($27,060 per year in 2017).

Finally, the Legislature should explicitly specify at what point in the MIF process the minimum compensation threshold takes effect and for how long it should be enforced.

Part-Time Jobs

As implied by the discussion above, we found that some businesses have used part-time workers to meet the obligations in their MIF loan agreements.

DEED permits MIF businesses to use part-time workers to meet their job creation obligations.

DEED administrators told us that providing state assistance to businesses to create some part-time jobs is consistent with DEED policy and an appropriate use of the MIF program. DEED's standard loan agreement explicitly defines the new jobs a business must create in terms of full time equivalents. Thus, a business that has promised to create 40 full time equivalents can meet its obligations by creating 80 half-time jobs.

We make no recommendation with regard to this finding because the MIF law is silent on whether businesses may use part-time jobs to fulfill job creation goals. However, we note that the relevant sections of the MIF law have not been changed since they were originally written in 1996. Conversely, the 2013 law creating the Job Creation Fund, a program with similar purposes, explicitly required DEED to use that business subsidy program to support the creation of full-time positions only.[40]

Timelines

Participation in the MIF program is designed as a *quid pro quo*. The state provides money to a business in return for job creation and financial investment. As we discuss in Chapter 2, there is no reason to provide money to businesses if they would create jobs or make investments without receiving public funds. However, DEED has sometimes awarded businesses MIF funding for hiring and investment that have already taken place.

DEED allowed some MIF businesses to meet their obligations by counting hiring that occurred before DEED made its award decision.

The legal contracts DEED has prepared or approved often have not specified a starting date when a business could begin hiring in order to meet its job creation commitments. For many years, the vast majority of loan agreements did not contain a provision specifying the earliest allowable hiring date.[41] Further, the monitoring documents that DEED retained have not always shown when new employees were hired—occasionally, businesses simply

[40] *Minnesota Statutes*, 116J.8748, subds. 1(h) and (j). DEED administrators noted that the department supported this provision at the time the Job Creation Fund was established.

[41] DEED has now added such a provision to its standard loan agreement.

reported they had the required number of employees at the hiring deadline. As a result, we do not know how many businesses have counted positions that were filled before DEED formally notified the business it would receive a MIF award.

However, we did identify 13 loan agreements completed in the last five years in which DEED explicitly allowed businesses to count positions that were filled before DEED had made award decisions. In some instances, shown in Exhibit 3.4, DEED allowed businesses to count hires made months earlier. A few businesses were even allowed to count hires made before they had completed their MIF applications.

Exhibit 3.4: Selected Minnesota Investment Fund Projects Where Hiring Date Preceded Award Date, 2014-2017

Business	Location	Award Date	Date from which DEED Allowed Business to Count Hiring	Days Before Award
Acucraft Fireplaces (The Maxson Company)	Big Lake	Dec. 18, 2015	Jul. 1, 2015	170
American Logistics Services	Cottage Grove	Aug. 12, 2015	Apr. 17, 2015	117
Capital Safety (DB Industries)	Red Wing	Aug. 29, 2014	May 23, 2014	98
Entrust Datacard Corporation	Shakopee	Mar. 13, 2015	Sep. 3, 2014	191
Uponor, Inc.	Apple Valley	Mar. 25, 2016	Jan. 1, 2015	449
Zierke Built Manufacturing	Fairmont	Jan. 4, 2017	Nov. 16, 2016	49

SOURCE: Office of the Legislative Auditor, analysis of DEED program documents.

DEED reimbursed some businesses for expenses incurred before DEED had decided to give them MIF awards.

Of the 45 projects we reviewed that involved reimbursements by DEED, we identified at least 8 projects for which DEED reimbursed businesses for expenses incurred before DEED had made their MIF award decisions. The amount of time elapsed between the earliest expense and the decision date ranged from 22 to 227 days.

For example, a Texas-based company (DataBank, Ltd.) applied for MIF funding for a project to build a new data center in Eagan and create 18 positions. The company submitted its earliest MIF paperwork in April 2014, but did not submit its final application materials (together with the city) until March 2015. On April 23, 2015, DEED formally notified the company it would receive a forgivable MIF loan of $135,000. In October 2015, DEED and the city signed a grant contract to provide the city with the funds to loan to DataBank (the contract's effective date was backdated to April 21, 2015). Meanwhile, the city and the company had reached a loan agreement on April 7, 2015.[42] The loan agreement specified that the MIF loan would be used to purchase two large pieces of specialized equipment. However, the invoices that the company eventually submitted to DEED for reimbursement showed that the company had ordered the equipment in September 2014—seven months

[42] The city and the business signed a loan agreement two weeks before DEED's award decision and six months before DEED and the city signed a grant agreement specifying the required terms of the loan agreement. DEED approved this loan agreement.

before DEED's award decision—and paid it off in three payments in October 2014, January 2015, and March 2015. DEED provided the reimbursement in April 2016.

The practice of allowing businesses to receive reimbursement for expenses incurred before funding was awarded was intentional, not a result of record-keeping errors. According to documents in DEED's files, at some point in early 2015 the practice came to the attention of DEED fiscal staff, who raised concerns. After interdepartmental discussions, DEED's Office of Business Finance stopped allowing such retroactive reimbursements, though it permitted a few additional businesses to receive reimbursements that had already been informally authorized by DEED staff.

Monitoring

DEED relies on local governments to collect monitoring information on businesses that participate in the MIF program. DEED provides businesses and local governments a standard form for listing expenditures and new positions. On the reporting form, an official of the business must assert that the reported data are "true and correct." Not all businesses use the standard form; some instead provide printouts from accounting or payroll software containing similar information.

Although DEED expects local governments to address any issues that they find when collecting monitoring data, it conducts its own review of the information that businesses submit.[43] DEED makes its own determination of whether a business has met the terms of the loan agreement and enforces sanctions if appropriate.

New Employees

The monitoring information contained in the project files we examined usually consisted of information self-reported by businesses. This reporting has not always provided complete information, and it is difficult to verify.

DEED's project files do not contain sufficient documentation to show that businesses have met their hiring commitments.

In a majority of the files that we reviewed that included monitoring reports, information about hiring consisted of a simple list of employees or positions with wage and benefit information for each individual.[44] In many instances, these lists contained information about hiring, but no information about departures—that is, whether any employees had left the company during the period between the original award and the business's hiring deadline. Particularly for larger companies, it is unrealistic to assume that no workers leave employment over a two-year period. Such departures should be accounted for in order to gain an accurate count of increased employment.

Other files contained more comprehensive information. Some included both a list of employees on the date from which DEED and the business had agreed to count hiring and a list of employees on the hiring deadline. In these instances, it was clearer how many new workers the business had added. Some files containing both DEED's reporting form and

[43] DEED staff also conduct site visits to businesses that receive larger awards.

[44] Sixteen of the 60 case files we reviewed were cancelled projects. Of the remaining 44 project files, 43 included at least one monitoring report.

printouts from payroll software had comprehensive information—for example, such a printout might show number of hours worked, rate of compensation, total earnings since the start of the year, and original hiring date.

Since DEED staff conduct monitoring site visits to many MIF businesses, it is possible that DEED staff obtained additional information from businesses that did not appear in project files. For this reason, we cannot conclude from the file record alone that DEED's monitoring was insufficient. However, many project files lacked the documentation to show that DEED's monitoring was rigorous.

DEED lacks sufficient information to independently verify self-reported business data on jobs and wages.

DEED officials told us that they compare the end-of-project monitoring reports against each company's unemployment insurance filings.[45] All Minnesota employers must file quarterly reports with DEED's Unemployment Insurance Division that show (1) total employment by business and (2) each employee's hours worked and total wages.[46] DEED officials told us that these unemployment insurance data are imperfect for assessing the accuracy of a company's MIF reports, but that DEED uses them to determine whether the MIF self-reports are "in the same ballpark."

We, too, found that it was difficult to use these data to independently verify reports of job growth at MIF businesses. We examined DEED's unemployment insurance data for businesses that had received MIF funding in the last ten years. However, we observed that businesses' filings often contained incomplete information on each employee's number of hours worked. Without data on employee hours, it was impossible to determine whether employees worked full time or part time or to compute their hourly wages.

Additionally, unemployment insurance filings are supposed to specify an employee's work location when a business has multiple locations. Inconsistent compliance with this requirement also hampered our ability to verify employment data reported by MIF businesses.

As a result, we did not have adequate data to assess the actual hiring for a majority of businesses that had participated in the MIF program in the past ten years. For the minority where we felt able to draw some conclusions, we found that businesses in the program generally increased hiring in the two years after their award decision dates.

[45] In most instances, we were unable to verify that such checking occurred because DEED staff have not routinely documented this process. We found very few written references in DEED's project files to the use of unemployment insurance data to monitor business compliance with MIF requirements. After we made inquiries, DEED staff were able to provide us with a few instances of additional documentation.

[46] *Minnesota Statutes* 2017, 268.044, subd. 1.

RECOMMENDATION

As a condition of receiving MIF funding, DEED should require that businesses report complete information on employees' locations and hours worked in their unemployment insurance filings.

The limitations of using unemployment insurance data to verify business self-reporting are long-standing. We reported similar difficulties in 1996 and 2008.[47] Similar to a recommendation we made in 2008, DEED should require businesses receiving subsidies to file unemployment insurance information in a way that makes the data more useful for verification of employment growth. In particular, DEED should include provisions in MIF loan agreements mandating that businesses report complete unemployment insurance data on hours worked and business locations.

Businesses are already required to accurately report this information in their unemployment insurance filings. However, DEED's unemployment insurance division places a low priority on enforcing compliance because these data are primarily gathered for research purposes and do not affect businesses' unemployment insurance payments or workers' benefit calculations. Thus, we propose that DEED's Office of Business Finance, which administers the MIF program, take its own steps to ensure more complete reporting of unemployment insurance information by participating businesses.

Expenditures

In contrast to the monitoring information related to hiring, the documentation regarding the use of MIF funds contained in DEED's project files was generally comprehensive. Almost all project files we reviewed involving reimbursements contained copies of invoices showing how businesses had spent the MIF funding they received.

However, as we described above, DEED sometimes allowed businesses to use MIF funding to pay for expenses incurred prior to their MIF award date. Further, we identified two questionable uses of state funds. Because these were isolated occurrences, we make no related recommendations.

DEED gave one business a $750,000 MIF reimbursement even though the business did not provide either the statutorily required matching amount or appropriate receipts.

State law limits MIF financing to one-half of a project's cost, at most.[48] However, DEED's 2015 award of $750,000 to Post Holdings, Inc., in Lakeville appeared to be simply a state payment to the company, without any matching amount provided by the company. As we discussed in more detail in Chapter 2, this award related to a corporate merger that was finalized months before the business applied for MIF funding. There was no evidence in the file that the company or a third-party lender provided any funding to the project—indeed, there was no "project" at all. DEED's file on this award indicates that it

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[47] Office of the Legislative Auditor, Program Evaluation Division, *State Grant and Loan Programs for Businesses* (St. Paul, 1996) and *JOBZ Program* (St. Paul, 2008).

[48] *Minnesota Statutes* 2017, 116J.8731, subd. 3(1). This requirement does not apply to renewable energy projects.

"reimbursed" the city for its payment to the business, but there is no documentation of how the business used the money.

DEED allowed one business's owners to use MIF funds to pay themselves $70,000 for equipment transfers without sufficient documentation.

File documents demonstrated that the owners of Verndale Custom Builders in Verndale used funds from a 2015 MIF award to pay themselves $70,000 for two large pieces of equipment (a truck and a crane) that they owned through a sister company. The file contained no appraisal or other information showing that the equipment was appropriately valued or that the transfer actually occurred. Although this transaction may have been appropriate, we believe further inquiry was warranted.

It is not surprising that DEED staff did not notice that the transaction involved companies with the same ownership. The person reviewing invoices probably did not read the entire file from beginning to end (as we did) and would have been unlikely to connect the invoice with biographical information about the business's owners in its application. However, we were troubled that the director of DEED's Office of Business Finance found no fault with the transaction after we pointed it out.

Program Documentation

In this chapter, we have relied heavily on data found in DEED's internal project files. In addition to the issues raised above, we also had concerns about the files themselves.

DEED does not adequately identify not public documents in its project files.

DEED's project files contain a mix of public and not public information on businesses and individuals. Much of the information DEED collects is public information under state law, including application forms, legal documents, and most of the correspondence between state officials, local governments, and businesses.[49] However, some of the information that businesses have provided to DEED to supplement their applications is not public by law, including income tax returns and business plans.[50] In addition, some businesses have provided not public information about employees as part of DEED's monitoring process, including individual payroll records and income amounts.

DEED places all of this information into the same electronic files.[51] Many files do not segregate public and not public information, and not public documents are often not marked in any way. It is impossible to tell whether files contain not public information without carefully examining the information on each page.

[49] *Minnesota Statutes* 2017, 13.591, subd. 2.

[50] *Ibid*.

[51] Although the files contain "public information" as defined in law, the files are not immediately accessible. A person wishing to view project files would have to follow DEED's procedures for requesting information under the Minnesota Data Practices Act.

Recommendation

DEED administrators told us that the department has already addressed some of the lax procedures we encountered. For example, DEED has ended the practice of reimbursing businesses for expenses incurred before issuance of an award letter, and it now includes a starting date for new hires in its standard loan agreement. However, the department can and should do more.

RECOMMENDATION

DEED should tighten its administrative procedures.

DEED should not allow businesses to count hiring towards their goals until after an award letter is sent. Additionally, the award letter should be changed so that it clearly spells out a business's obligations as a condition of receiving the MIF award.

DEED should adjust its monitoring of business hiring to ensure that it gathers sufficient documentation to show that MIF businesses are actually adding the number of employees they claim. Although we did not identify instances where businesses counted new hires without taking departures into account, the documentation that DEED collects should be sufficient to rule out that possibility. DEED should make sure that it either receives a list of all worker departures in addition to all new hires, or it should receive a listing of all employees at the hiring deadline date that can be compared to a listing of all employees at the date DEED made the award. Although some files contained such information, many did not.

Finally, DEED's failure to identify the not public information it retains in its files is a poor management practice. It is the responsibility of every state agency to safeguard not public information it stores about businesses and individuals. We do not see how an agency can confidently meet this responsibility without clearly identifying not public information within its records.

List of Recommendations

- The Department of Employment and Economic Development (DEED) should improve the usefulness and accuracy of its public reports on the Minnesota Investment Fund (MIF). (pp. 26-27)

- The Legislature should require stronger assurance that use of MIF is essential for a business project to proceed. (pp. 29-30)

- The Legislature should consider restructuring the MIF program so that loans are made directly by DEED to participating businesses. (pp. 42-43)

- The Legislature should consider amending state law to discontinue the practice of directing a portion of MIF loan repayments to local governments. (p. 43)

- The Legislature should require DEED to publicly specify:

  - The criteria that determine which businesses will receive MIF awards.

  - The criteria that determine the amount of money a business will receive.

  - The circumstances under which DEED will forgive MIF loans. (pp. 55-56)

- DEED should require businesses to meet the employee wage and benefit levels the department considered when making MIF award decisions. (pp. 58-59)

- The Legislature should clarify the minimum compensation threshold in the MIF statute. (pp. 61-62)

- As a condition of receiving MIF funding, DEED should require that businesses report complete information on employees' locations and hours worked in their unemployment insurance filings. (p. 66)

- DEED should tighten its administrative procedures. (p. 68)


THE GREAT SEAL OF THE STATE OF MINNESOTA
L'ETOILE DU NORD
1858

Appendix: Past Research Regarding Business Incentives

In Chapter 2, we briefly discussed research literature regarding the impacts of business incentives. We said that researchers that have summarized past research have questioned whether public business incentives are cost-effective. However, this broad conclusion may not be applicable to all individual economic development programs.

States have tried to influence economic development in various ways. They have provided (1) direct financial assistance to businesses, such as grants and loans; (2) business tax incentives, such as tax abatement or credits; and (3) nonfinancial incentives, such as construction of infrastructure to facilitate business development.

There has been a large amount of research on economic development incentives, spanning many decades. This research has evaluated a range of programs, in many different settings, using a variety of methods. This appendix provides a broad summary of this research, rather than an exhaustive discussion of individual studies.

Business Location Decisions

Thirty years ago, the U.S. Government Accountability Office (GAO) summarized previous research about factors that affect business location decisions. GAO said:

> Surveys that specifically asked employers about [business] location decision factors have found that financial incentives were secondary factors. Primary factors were product markets, raw materials, labor, transportation, energy, and perhaps "business climate," which is sometimes defined as tax and regulatory factors. Researchers hypothesize that once these primary factors determine the region in which a business will locate, secondary factors such as financial incentives can play a significant role in determining specific business location.[1]

Based on its own survey of employers, GAO said "financial incentives are relatively unimportant influences on [business] location decisions…. These findings are generally consistent with the results of other studies."[2]

A 2001 academic review of research said that past surveys of business officials regarding why they make business location decisions have yielded "highly disparate results."[3] It said this likely reflects that different types of businesses consider different factors. For example, a business's age, economic health, and state of development may affect its decisions about where to locate or expand. This research summary suggested that manufacturers' location

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[1] U.S. General Accounting Office, *Enterprise Zones: Lessons from the Maryland Experience* (Washington, DC, December 1988), 43.

[2] *Ibid.*, 44.

[3] Terry Buss, "The Effect of State Tax Incentives on Economic Growth and Firm Location Decisions: An Overview of the Literature," *Economic Development Quarterly* 15, n. 1 (2001): 98.

decisions might take taxes into account more than the decisions of nonmanufacturers, but it said:

> Tax literature, now in hundreds of publications, provides little guidance to policy makers trying to fine-tune economic development. Taxes should matter to states, but researchers cannot say how, when, and where with much certainty.[4]

To address the concerns referenced above about how different types of businesses make decisions, a 2013 study examined business location factors for several categories of businesses.[5] Based on a national survey of commercial real estate experts, the study found that the availability of labor and employee parking were among the top three considerations in decisions regarding manufacturing and office projects. Taxes and public financial incentives were important factors, but they were ranked a little further down the lists.

Recently, our office surveyed Minnesota companies that claimed a state research tax credit, and we inquired about the tax credit's impact on business location decisions.[6] Among companies that received a refund through the tax credit, 57 percent of respondents said the credit was "very important" or "moderately important" in allowing the company to expand in Minnesota. Thirteen percent of respondents said the credit was "very important" or "moderately important" in allowing the company to relocate business activities to Minnesota.

Economic Impact of Business Incentives

In the words of one literature review, the amount of research that has addressed whether business incentives induce job growth or business investment is "massive."[7] While this appendix cannot convey the diversity of study methods and the details of individual studies, we present below a selection of comments from prior research summaries. We have included statements from researchers at various times from the past 15 years. In general, the statements indicate significant skepticism about the impact of business incentives, while noting that some studies have reported positive results. In addition, researchers have expressed a desire for continued analysis with improved data that may shed additional light on the effects of business incentives.

> **Bartik (2017):** "Preliminary work suggests that a state's incentives are not highly correlated with a state's fortunes. Incentives do not have a large correlation with a state's current or past unemployment or income levels, or with future economic growth….
>
> The existing research on incentives is that in some cases they can affect business location decisions, but that in many cases they are excessively costly and may not have the promised effects. The new research suggests

[4] *Ibid.*, 101.

[5] Shelley Kimelberg and Elizabeth Williams, "Evaluating the Importance of Business Location Factors: The Influence of Facility Type," *Growth and Change* 44, n. 1 (March 2013): 92-117.

[6] Office of the Legislative Auditor, Program Evaluation Division, *Minnesota Research Tax Credit* (St. Paul, 2017), 37.

[7] Alan Peters and Peter Fisher, "The Failures of Economic Development Incentives," *Journal of the American Planning Association* 70, n. 1 (Winter 2004): 29.

that much of this consensus is justified. On the other hand, some signs show that there is some improvement toward reining in incentives so that they are less costly and targeted in a more effective manner. But this improvement is limited. In other words, the glass is partly full and partly empty, but more empty than full."[8]

Jensen (2017): "Economic development incentives target individual firms for financial or non-financial benefits to induce capital investment or job creation. Previous studies have found a mixed impact of incentives on economic development, with numerous studies pointing to no impact of incentives on economic growth or job creation…. My main finding is that [the flagship economic incentive programs in Virginia and Maryland] had essentially zero impact on job creation when they are compared to a control group of similar firms."[9]

Bartik and Erickcek (2014): "Most [economic development] incentive studies suggest that incentives are not cost-effective, either having no statistically significant effects or large costs per job created. However, there are some exceptions."[10] The review identifies customized job training and manufacturing extension services as approaches for which research has shown some positive impacts.

Ellis, Hayden, and Rogers (2014): "To summarize, the empirical research does not provide evidence that development incentives serve as engines of growth for communities…. [T]here are compelling reasons to think that, in general, economic development incentives *do not work* to induce business behavior that will pay off—in terms of jobs, sales, and ultimately tax revenues—for the community that offers them."[11]

Gorin (2008): "The use of refined approaches and better data sets has improved researchers' ability to evaluate the effectiveness of specific incentive programs. But fundamental concerns remain, and some researchers have begun to write off economic development incentives as ineffective or inefficient for a host of reasons."[12] The author says these concerns include whether public incentives (1) are large enough to affect business behavior, (2) distort allocations of private resources by encouraging firms to invest in suboptimal places, (3) displace government

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[8] Timothy Bartik, *A New Panel Database on Business Incentives for Economic Development Offered by States and Local Governments in the United States* (Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 2017), 4-5 and 116-117. The author cautioned that his preliminary research from a large, new database (referenced in the first quoted sentence) is subject to change as more variables are analyzed.

[9] Nathan Jensen, "The Effect of Economic Development Incentives and Clawback Provisions on Job Creation: A Pre-Registered Evaluation of Maryland and Virginia Programs," *Research and Politics* (April-June 2017): 1.

[10] Timothy Bartik and George Erickcek, "Simulating the Effects of the Tax Credit Program of the Michigan Economic Growth Authority on Job Creation and Fiscal Benefits," *Economic Development Quarterly* 28, n. 4 (2014): 315. The "manufacturing extension services" referenced in this review are public-private partnerships that are intended to help transfer technology and expertise to small- and medium-sized manufacturers.

[11] Steven Ellis, Grant Hayden, and Cynthia Rogers, "A Game Changer for the Political Economy of Economic Development Incentives," *Arizona Law Review* 56, n. 4 (2014): 958 (italics in original).

[12] Dan Gorin, "Economic Development Incentives: Research Approaches and Current Views," *Federal Reserve Bulletin* (October 2008): A69.

spending on other public goods, and (4) result in a zero-sum game, in which gains in one location are offset by losses elsewhere.

Peters and Fisher (2004): "On the three major questions—Do economic development incentives create new jobs? Are those jobs taken by targeted populations in targeted places? Are incentives, at worst, only moderately revenue negative?—traditional economic development incentives do not fare well. It is possible that incentives do induce significant new growth, that the beneficiaries of that growth are mainly those who have greatest difficulty in the labor market, and that both states and local governments benefit fiscally from that growth. But after decades of policy experimentation and literally hundreds of scholarly studies, none of these claims is clearly substantiated. Indeed, as we have argued in this article, there is a good chance that all of these claims are false."[13]

[13] Alan Peters and Peter Fisher, "The Failures of Economic Development Incentives," *Journal of the American Planning Association* 70, n. 1 (Winter 2004): 35.

February 8, 2018

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St. Paul, MN 55155

Dear Mr. Nobles:

Thank you for the opportunity to review and provide comments on the revised draft of the Office of the Legislative Auditor's (OLA) evaluation report regarding the Minnesota Investment Fund (MIF). The Department of Employment and Economic Development (DEED) appreciates your staff's efforts to understand and assess the complexity and impact of MIF. Since 2011, MIF has provided funds to more than 100 businesses – helping them add a projected 8,400 quality jobs throughout the state. Generally, we view the report as a valuable assessment of MIF and we intend to strongly consider the recommendations. This letter is a response to a number of the points raised in the report that we believe are due to an incomplete or inaccurate understanding of MIF and its critical role in supporting economic development in Minnesota.

While Minnesota's incentive programs, like MIF, are modest relative to finance programs available in other states, they remain critical components for community and business competiveness and play a key role in business expansion and relocation decisions, especially in Greater Minnesota. Businesses have many location options when considering new or expanded operations. MIF serves as a necessary incentive to compete against offers from other states and spur investment in Minnesota. This is especially true when comparing Minnesota to locations with similar attributes such as workforce skills, infrastructure, supply chain, and quality of life. There is no question that MIF is viewed as a valuable tool by businesses, economic developers, and local communities throughout the state and by those businesses interested in establishing a Minnesota location.

The MIF awards have had measurable impacts to Minnesota's tax base and reflect our commitment to assisting our communities who, unlike those in many other states, do not have many resources outside of the tax base to accomplish economic development. The economic impact ratio is high for this program, which directly results in increased tax revenues that often offset a project's MIF investment in as few as one or two years. This is true even without taking into account the indirect benefits to the community or state that happen as a result of the MIF project.

As the report notes, the Department continues to do a good job managing the program's finances and there is little risk to state funds. We continue to have sound internal controls and ensure that funds are managed properly with well-constructed legal documents and effective clawback processes when businesses do not meet performance commitments. As a loan program, MIF is also an important complement to the Job Creation Fund program, which provides financial assistance to businesses as performance thresholds are achieved. MIF also provides important flexibility to assist businesses in unique circumstances in rural and urban areas needing financing to add or even retain jobs.

The Department has made important improvements to tighten program administration and improve transparency, including investment in new technology to better manage transactions. These improvements include the development of:

- enhanced "but for" and "no harm" provisions
- online award map with project information
- tool kits for local officials
- Unemployment Insurance data utilization
- program processes and procedures
- conflict of interest forms
- enhanced monitoring guidelines
- improved invoice tracking
- legal document templates
- timelines for business hiring and spending

The Department is disappointed the OLA does not highlight these improvements or recognize our commitment to continuous improvement. Moreover, many of these improvements address this report's recommendations, some of which were based on project activity occurring prior to implementing these improvements.

Many of the issues identified in this report have been addressed by the Department or could be solved with minor adjustments and this perspective has been ignored or minimized. For example, if we remove the misclassified leverage from the Post Holding project, the program still results in a leverage of more than 28:1. More importantly, the business established its headquarters in the state and has doubled their workforce to more than 400 employees since receiving MIF funding. Furthermore, Exhibit 3.2 on page 54 of your report identifies three projects that represent over $78 million of private investment, or a leverage ratio of 31:1.

We are also surprised that the report makes conclusions on the value of MIF assistance to individual expansions without discussing the transactions with the individual businesses or DEED. Any project file on its own cannot provide the personal insights and dynamics on the value of MIF that are gained only through discussions with all participants. We often spend months, if not over a year, working with businesses and communities prior to applications. Hundreds of communities and businesses are strong supporters of the program – yet the report minimizes these perspectives and highlights views from a small number of interviews with local government officials.

The Department has the following responses to the List of Recommendations listed on page 69:

1. DEED should improve the usefulness and accuracy of its public reports on the Minnesota Investment Fund.

The Department implemented online Annual Program Summaries several years ago and an online Business Awards Map in 2015. These initiatives were not required but were important steps to improve the transparency of the Department's program and activities. Moreover, these transparency efforts are not common among agencies inside or outside Minnesota and reflect the Department's commitment to program award transparency. It should be noted that press releases are another great way to communicate program activity to stakeholders. Press releases on program awards increased from an average of six per year between 2011 and 2013 to more than 17 per year between 2014 and 2017. Likewise, the report notes inaccuracies on our website. We admit, there was one typo and some information on our website had not recently been updated. We have corrected the error and are making an effort to update our website's information in as timely of a manner as possible moving forward. The balance of the information available on our website was accurate and transparent. Nevertheless, we appreciate the report's recommendation and are taking steps to further improve the usefulness and accuracy of all reports related to program activity.

2. The Legislature should require stronger assurances that the use of the Minnesota Investment Fund is essential for a business product to proceed.

Although not required in statute, the Department implemented provisions several years ago to address not only this recommendation, but also concerns that any assistance might provide an unfair advantage to another Minnesota business. We appreciate the recommendation and will continue to enhance these requirements.

3. ***The Legislature should consider restructuring the Minnesota Investment Fund program so that loans are made directly by DEED to participating businesses.***

MIF is a program grounded in a partnership between local and state governments with a generally successful track record. In the early years of the program, many cities had capacity to manage the program. Today, while that capacity has somewhat diminished, many communities still have the necessary capacity and others use outside consultants to manage the administration. The Department, in partnership with its local partners, has managed to administer this program with limited state staff. We value the work done at the local level, require their approval for assistance, and ultimately need capacity at the local level to work with business prospects and build the relationships. If the Legislature were to eliminate our local partners, DEED would need additional staff to manage the MIF process.

4. The Legislature should consider amending state law to discontinue the practice of directing a portion of MIF loan repayments to local governments.

Many communities view MIF as a key financing tool given their limited resources outside property tax-related approaches. Most communities with revolving loan funds seeded by MIF repayments have used the funds to assist businesses in their communities. The report relies on a few outlier comments for their criticism of the local component of MIF. It is the department's opinion that the partnership between local and state governments is a critical component of this program and we strongly disagree with the suggestion to eliminate the role of our local government partners without their approval.

5. The Legislature should require DEED to publicly specify:

- ***The criteria that determine which businesses will receive MIF awards.***
- ***The criteria that determine the amount of money a business will receive.***
- ***The circumstances under which DEED will forgive MIF loans.***

The Department has made strides in establishing award criteria as noted by the award guidelines included in the report. The Department will implement additional transparency, although our efforts will be somewhat limited due to the competitive economic development environment and the reality that each award uses a unique collection of factors because projects and communities are all different.

6. ***DEED should require businesses to meet the employee wage and benefit levels the Department considered when making MIF award decisions.***

We agree with this recommendation and have begun implementation. The modified wage levels did not affect the project eligibility and modifications were made generally in response to changes in the project specifications or to streamline reporting challenges in conjunction with other assistance. The actual average wage typically exceeded the projected average wage noted in the application. Still, moving forward the Department will document reasons for any modified wage levels to enhance program transparency.

7. The Legislature should clarify the minimum compensation threshold in the MIF statute.

The Department believes the intent of this provision was to require all new employees to receive the minimum compensation as noted in statute. The 2018 hourly compensation level, which is equivalent to 110% of the federal poverty level for a family of four, is $13.27 per hour or $27,610 per year. Most jobs created through the program far exceed this minimum level. We look forward to discussing the pros and cons of this policy with the Legislature.

8. *As a condition of receiving MIF funding, DEED should require that businesses report complete information on employees' locations and hours worked in their unemployment insurance filings.*

The Department has used the State's Unemployment Insurance records as a third-party verification tool for job creation for several years. Although the information is not perfect, it is the most accurate available and has been a useful practice. We will continue to work with DEED's Unemployment Insurance Program to further improve the data to better meet program requirements, including job creation verification.

9. DEED should tighten its administrative procedures for the MIF program.

Although the Department has implemented a variety of steps to tighten program administrative procedures (as noted above), there is always opportunity to further improve. The Department has already improved administrative procedures around reimbursements, the starting date for new hires, and has worked to improve our business monitoring. The Department will be implementing additional actions, including better documenting data within our internal database that is considered "not public" information.

Thank you again for the opportunity to review the report and provide comments. We appreciate the recommendations and look forward to improving program operations using this report as we have used other OLA reports in the past. This remains helpful feedback as we continue to help businesses grow and create jobs for Minnesotans utilizing important tools such as MIF.

Regards,

Shawntera Hardy
Commissioner

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