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To: Joint Fiscal Committee

From: Joan Goldstein, Commissioner, Department of Economic Development

Date: August 31, 2021

Topic: Model to Assess the Net Fiscal Impact of Proposals for the Capital Investment Program (CIP)

Pursuant to the requirements of Act 74 of the 2021 Legislative Session which included the authorization of the Capital Investment Grant Program, the CIP Working Group has prepared the following description of the processes and procedures governing the Act's requested fiscal impact modeling for COVID projects in the State. More specifically, this description of analysis protocols and procedures is intended to meet the requirements of that authorization in Section H.18, subsection (d) which requests that the Agency of Commerce and Community Development ("ACCD") work with the Legislative Economist to develop a model "to assess the fiscal, economic, and societal impacts of proposals." Further, that Section requires ACCD to submit this model to the Joint Fiscal Committee by September 1, 2021.

The attached document describes the results of several technical sessions to develop those fiscal, economic, and societal" analysis procedures and protocols between the ACCD and its consultants (Jeffrey Carr and Robert Chase) and Legislative Economist, Tom Kavet and Nic Rockler, the principals of Kavet, Rockler, and Associates, LLC. The result is a flexible and collaborative analytic process that covers the key, quantifiable requirements of this requested impact analysis methodology. Upon approval of the Joint Fiscal Committee, this methodology will be employed to solicit and evaluate proposals under this program that we expect to receive this Fall.

Representatives from the ACCD and the Legislative Economist will be prepared to discuss the methodology with you during the September 17, 2021 meeting of the Joint Fiscal Committee. We look forward to that discussion and the use of the model to improve economic conditions in Vermont as part of our strategy to recover from the impacts of the Covid-19 pandemic.

Thank you. JG

An Economic, Fiscal and Social Impact Model to Evaluate Proposals under the Capital Investment Program

Act 74 established the Capital Investment Program (CIP) to:

> Make funding available for transformational projects that will provide each region of the State with the opportunity to attract businesses, retain existing businesses, create jobs, and invest in their communities by encouraging capital investments and economic growth.

As a part of the legislation, the Agency of Commerce and Community Development (the "ACCD"), which has chosen to work with the Administration Economist, was instructed to work with the Legislative Economist to:

> Design a data model and related methodology to assess the fiscal, economic, and societal impacts of proposals and prioritize them based on the results.

This report to the Joint Fiscal Committee ("JFC") is the response to that requirement.

The Starting Point—Overview of the Vermont Employment Growth Incentive Cost-Benefit Approach

The Vermont Economic Progress Council has used a cost-benefit model for the purpose of determining the net fiscal impact of Vermont Employment Growth Incentive ("VEGI") payments to Vermont businesses for almost 15 years. That VEGI model is based on a critical assumption that "but-for" the public investment, the incented business activity would not occur (or would occur in a substantively different manner), and the change in economic activity that is projected for a business expansion relative to a baseline. The VEGI model also assumes that the projected business expansion will not cannibalize an existing Vermont business because it incents expansion projects in export-based industries. The model includes both an economic and fiscal impact component, two-thirds of the assignment in the Legislation for the Capital Investment Program.

In the VEGI analytical process, the change in economic activity is gauged using a hybrid regional economic model in which an Input/Output model operates at the core of a partial equilibrium model that is solved annually as developed by Regional Economic Models, Inc. (REMI) of Amherst, MA. In the VEGI Cost-Benefit Model, the REMI model takes inputs such as employment changes, compensation associated with those employment changes and capital expenditures for both real property construction or improvements and equipment purchases. The VEGI model provides output for five years after business project start up, estimating changes from a baseline in thousands of variables, including:

- Personal Income
- Private sector , non-farm employment
- Capital stock (residential and non-residential real property values)
- Personal consumption in many categories
- Population, both overall and for school age children

- Consumer prices

Selected REMI outputs are then inserted into a second model, maintained by ACCD under the review of the JFC, that translates the changes in economic parameters to changes in State revenue. These include:

- Personal income, used to calculate changes in Vermont income tax revenues
- Capital stock changes, used to calculate changes in the Education Property Tax
- Consumption and price changes, used to calculate changes in the consumption taxes (Sales, Meals and Rooms, Purchase and Use)
- Population changes are a proxy for estimates in the other taxes that comprise the General Fund, Transportation Fund and Education Fund
- Employment changes are a proxy for calculating changes in the Corporate Income Tax.

In addition to revenue enhancements, the model also estimates changes in State government costs, largely based on increases in the population with a particular calculation for the Education Fund based on the change in the student age population.

The difference between the increases in revenue and increases in State government costs is a figure for net fiscal benefit that serves as the basis for determining the value of incentive payments to VEGI applicants.

A Proposed Model and Process for the Capital Investment Program

The net revenue model used for VEGI is a starting point for a model to determine the net revenues of projects applying to the Capital Investment Program. Customizing that model to incorporate a broader range of project inputs and outcomes is a part of the process proposed by ACCD and the Legislative Economist. The model customization will be performed on a consensus basis by a Technical Review Group (TRG), drawing from the technical expertise of five individuals: Jeffrey Carr, Bob Chase and Ken Jones on behalf of ACCD and Tom Kavet and Nic Rockler on behalf of the Legislature. In the event a consensus is not possible on any given issue of fiscal importance, the Joint Fiscal Committee will determine the outcome. In any such instance, a written statement of the technical differences of opinion may also be produced for use and consideration by those ultimately determining the awards granted.

The reason for the need to customize the CIP model is a recognition that the applicants for the funds under this program will be carrying out different activities that have outcomes that may require additional assumptions with respect to economic and fiscal impacts versus a straight replication of the VEGI Program's cost-benefit approach. In part, this is because the structure of these impact assessment analyses, which attempts to measure economic and fiscal impacts for invested federal COVID financial relief-assistance dollars versus a reduction in state fiscal return via an incentive—differs from the conventional VEGI analysis. In addition, other types of investment projects are also to be considered, including infrastructure projects that will facilitate the growth of a mix of businesses, some of which may not have detailed outcomes at the time of application. In other cases, a project under this modified VEGI approach may enhance human capital in terms of social supports or training opportunities.

The details of those projects will lead to the use of different inputs to the REMI model portion of the cost-benefit analysis process in order to evaluate the economic and fiscal benefits of any particular project. It is not possible, at this time, to indicate precisely all of the inputs that may be different until ACCD and the Legislative Economist review the specifics of applications.

The actual outputs from the REMI model will be similar to those used for VEGI, except we propose that we examine extension of the period of evaluation to ten years from the five-year period used for VEGI. This will allow both five-year and ten-year impact assessments, which may inform those ultimately determining the awards granted. We expect to make a consensus technical recommendation regarding the use of five or ten-year impact horizons on the statutory awards limits following review of a sample of likely applications and fiscal impact model analysis.

The translation of economic outputs to the cost benefit model for determining State government fiscal impacts will be the same as with REMI. During this process, consensus enhancements to both the VEGI Cost-Benefit Model and the CIP net fiscal impact model may be recommended. Any such major model adjustments will be presented to the JFC for review and approval.

As with the VEGI model, the model used to evaluate Capital Investment Program applications will differentiate those applicants based on their geographic location. Using counties as the geographic determinant, the model will apply higher discount rates to the benefits of projects in parts of the state that did not see the highest Covid impacts, and lower discount rates to the benefits of projects from counties that higher impacts. The result of this approach is that the net fiscal benefit determined for project applicants in more seriously affected parts of the state will be higher than for applicants in less seriously affected parts of the state.

Incorporating Social Benefits

The Legislature's structuring of the Capital Investment Program recognizes that individual projects may have both measurable economic outcomes while also generating a range of social impacts that can be difficult or impossible to measure, but which should be considered in addition to the economic and fiscal impacts incorporated in the REMI/VEGI.

If such impacts can be quantified for REMI model input through consensus TRG review of relevant academic and other literature, these estimates will be incorporated in the fiscal impact model and included in the net fiscal impact estimate. If they cannot be reasonably quantified, either quantifiable ranges of potential impacts will be presented and/or the social benefits will be described qualitatively and provided as a part of the decision matrix used in selecting projects. The social benefits to be considered and included in the application, when appropriate, include:

- Addressing issues of equity
- Providing supports to marginalized sub-populations of Vermonters
- Addressing climate change
- Public health benefits

- Possible financial and non-financial impacts on local government and quasi-governmental organizations

Full text of Section H.18 of Act 74 describing the Capital Investment Program

(a) Creation; purpose; regional outreach.

(1) The Agency of Commerce and Community Development shall use the $10,580,000 appropriated to the Department of Economic Development in Sec. G.300(a)(12) of this act to design and implement a capital investment grant program consistent with this section.

(2) The purpose of the program is to make funding available for transformational projects that will provide each region of the State with the opportunity to attract businesses, retain existing businesses, create jobs, and invest in their communities by encouraging capital investments and economic growth.

(3) The Agency shall collaborate with other State agencies, regional development corporations, regional planning commissions, and other community partners to identify potential regional applicants and projects to ensure the distribution of grants throughout the regions of the State.

(b) Eligible applicants.

(1) To be eligible for a grant, an applicant shall meet the following criteria:

(A) The applicant is located within this State.

(B) The applicant is:

(i)(I) a for-profit entity with not less than a 10 percent equity interest in the project; or

(II) a nonprofit entity; and

(ii) grant funding from the Program represents not more than 50 percent of the total project cost.

(C) The applicant demonstrates:

(i) community and regional support for the project;

(ii) that grant funding is needed to complete the project;

(iii) leveraging of additional sources of funding from local, State, or federal economic development programs; and

(iv) an ability to manage the project, with requisite experience and a plan for fiscal viability.

(2) The following are ineligible to apply for a grant:

(A) a State or local government-operated business;

(B) a municipality;

(C) a business that, together with any affiliated business, owns or operates more than 20 locations, regardless of whether those locations do business under the same name or within the same industry; and

(D) a publicly-traded company.

(c) Awards; amount; eligible uses.

(1) An award shall not exceed the lesser of $1,500,000.00 or the estimated net State fiscal impact of the project based on Agency modeling.

(2) A recipient may use grant funds for the acquisition of property and equipment, construction, renovation, and related capital expenses.

(3) A recipient may combine grant funds with funding from other sources but shall not use grant funds from multiple sources for the same costs within the same project.

(4) The Agency shall release grant funds upon determining that the applicant has met all Program conditions and requirements.

(5) Nothing in this section is intended to prevent a grant recipient from applying for additional grant funds if future amounts are appropriated for the program.

(d) Data model; approval.

(1) The Agency shall collaborate with the Legislative Economist to design a data model and related methodology to assess the fiscal, economic, and societal impacts of proposals and prioritize them based on the results.

(2) The Agency shall present the model and related methodology to the Joint Fiscal Committee for its approval not later than September 1, 2021.

(e) Application process; decisions; awards.

(1) (A) The Agency shall accept applications on a rolling basis for three month periods and

shall review and consider for approval the group of applications it has received as of the conclusion of each three-month period.

(B) The Agency shall make application information available to the Legislative Economist and the Executive Economist in a timely manner.

(2) Using the data model and methodology approved by the Joint Fiscal Committee, the Agency shall analyze the information provided in an application to estimate the net State fiscal impact of a project, including the following factors:

(A) increase to grand list value;

(B) improvements to supply chain;

(C) jobs impact, including the number and quality of jobs; and

(D) increase to State GDP.

(3) The Secretary of Commerce and Community Development shall appoint an interagency team, which may include members from among the Department of Economic Development, the Department of Housing and Community Development, the Agency of Agriculture, Food and Markets, the Department of Public Service, the Agency of Natural Resources, or other State agencies and departments, which team shall review, analyze, and recommend projects for funding based on the estimated net State fiscal impact of a project and on other contributing factors, including:

(A) transformational nature of the project for the region;

(B) project readiness, quality, and demonstrated collaboration with stakeholders and other funding sources;

(C) alignment and consistency with regional plans and priorities; and

(D) creation and retention of workforce opportunities.

(4) The Secretary of Commerce and Community Development shall consider the recommendations of the interagency team and shall give final approval to projects.

(f) Grant agreements; post award monitoring. If selected by the Secretary, the applicant and the Agency shall execute a grant agreement that includes audit provisions and minimum requirements for the maintenance and accessibility of records that ensures that the Agency and the Auditor of Accounts have access and authority to monitor awards.

(g) Report. On or before December 15, 2021 the Agency shall submit a report to the House Committee on Commerce and Economic Development and the Senate Committee on Economic Development, Housing and General Affairs concerning the implementation of this section, including:

(1) a description of the implementation of the program;

(2) the promotion and marketing of the program;

(3) an analysis of the utilization and performance of the program, including the projected revenue impacts and other qualitative and quantitative returns on investment in the program based on available data and modeling.