KANSAS LEGISLATIVE
DIVISION of POST AUDIT

The Rundown podcast transcript for the Performance Audit report titled ***Kansas Department of Commerce: Evaluating the Department's Administration of the Job Creation Fund (Limited Scope)*** – Released July 2019

Andy Brienzo, Host and Principal Auditor: [00:00]
From the Kansas Legislative Division of Post Audit, this is The Rundown your source for news and updates from LPA, including performance audits recently released to the Kansas Legislature. I'm Andy Brienzo. In July 2019, Legislative Post Audit released a limited scope audit examining whether the Kansas Department of Commerce's process to administer and distribute job creation program funds is transparent and effective. I'm with Heidi Zimmerman, Principal Auditor at Legislative Post Audit, who conducted this audit. Heidi, welcome to The Rundown. Thanks for taking the time to discuss the findings of this audit with me.

Heidi Zimmerman, Principal Auditor and Supervisor: [00:41]
Sure. I'm happy to be here.

Andy Brienzo, Host and Principal Auditor: [00:43]
Before we get into what you found, why don't you take a minute to explain what a limited scope audit is and how it differs from the standard performance audits that LPA produces?

Heidi Zimmerman, Principal Auditor and Supervisor: [00:52]
Sure. So, a limited scope audit is an audit that we conduct in 100 hours. So about 2.5 weeks from start to finish. So, in comparison, a regular performance audit usually takes us between four and six months. So, this is comparatively a much shorter process. The question that we answer limited scope audit is typically very narrow, a very straightforward question, and it's really meant to just give a very quick look into something to see if there might be something bigger that a legislator might be interested in asking for a full performance audit of.

Andy Brienzo, Host and Principal Auditor: [01:29]
So this particular limited scope audit looked at the job creation program fund or JCF. Tell me a little bit about JCF and how it works.

Heidi Zimmerman, Principal Auditor and Supervisor: [01:37]
So the Job Creation Program Fund was created in 2011 by combining two other economic development incentive programs. Its purpose is really to provide a cash award to companies to help them create jobs or to support some other economic development activity. So that could be creating new jobs or retaining jobs. It could be offering training to, to their employees or kind of a number of other economic development activities. However, a company who fails to meet these goals would be required to pay back these funds or in some cases would just forfeit some of the funds that they thought they were going to get.

Andy Brienzo, Host and Principal Auditor: [02:21]
So state law only allows the Department of Commerce to award these funds for specific purposes though, right?

Heidi Zimmerman, Principal Auditor and Supervisor: [02:28]
That's correct. The statute lays out eight purposes for which the Department of Commerce can award these funds. The Department of Commerce is the administrator of this fund. So those eight purposes range from very specific things like a major expansion of a Kansas business to very broad things like using the funds to promote a unique economic development opportunity. So even though they are enumerated in statute, there's a wide range of things the Department can use these funds for.

Andy Brienzo, Host and Principal Auditor: [03:04]
How commonly is this fund used?

Heidi Zimmerman, Principal Auditor and Supervisor: [03:06]
It's not used very commonly. We asked the department to tell us how often it's used and what they told us was of all the major projects that the department provides some sort of economic development incentive for. So out of that whole group, job creation funds are only awarded about 2% of the time...that was in 2018. We did look at a few other years and even across other years, it's in the low single digits. So, this is not a particularly commonly used program.

Andy Brienzo, Host and Principal Auditor: [03:40]
What work did you do to review the Department of Commerce's administration and distribution of JCF funds and reached the conclusions you've outlined in the report?

<u>Heidi Zimmerman, Principal Auditor and Supervisor:</u> [03:47]
So we did a couple of things and just also kind of keeping in mind that this is a limited scope audit. So, all the work we do we just do in a couple of weeks. So, we started with meeting with department staff and interviewing them and asking them about what this program is and how does it work and what kinds of things they consider when awarding these funds. We also chose a number of awards from the last five years, so we chose five [awards]. We did choose on kind of a judgmental basis. So, we looked for some awards that did seem a little odd to us and we also looked for some that seemed pretty typical for an economic development incentive program. So those five, it's not a lot. We think that those five do tell us something about the process that the department uses, but because it's just a handful and because they were not randomly chosen, they are not necessarily representative of all of the projects that the department awards funds for.

<u>Andy Brienzo, Host and Principal Auditor:</u> [04:50]
Your first finding based on this work was the department's process for awarding funds is inconsistent and lacking in transparency. Talk me through this finding a little bit.

<u>Heidi Zimmerman, Principal Auditor and Supervisor:</u> [04:59]
So there were a couple aspects of this finding and a few things that kind of led us to that particular conclusion. First of all, when we went over and talked to staff, one of the first things that stood out to us was that they lacked any written policies or procedures to guide which companies received awards and even how much money to award each company. So that lack of kind of consistent process, something that they could point to and say, this is how we do things, produces kind of a lack of transparency. So that was kind of our first concern. Then there were a few other things that came up that were inconsistent that caused us a little bit of concern. So, first of all, we noticed that the department does not consistently require an application. So, some companies were required to submit an application while others were not. We also had a few additional things. So, things the department required some companies to produce jobs or other measurable economic development activity in order to receive their award, but others were not expected to do so. So for example, we noticed last year that the Kansas Business Hall of Fame, which is in Emporia, received funds with the expectation that they would just raise matching funds, but a bank here in Topeka that received job creation funds received those funds with the expectation that they would create a couple of dozen jobs. So, there was just some inconsistency in what was expected. We also noticed some inconsistency in the departments award amounts. So, we looked at it on kind of a per job created basis. So, we looked at how much money the company got and how many jobs they created and found quite a bit of variation. So, some companies got a few hundred dollars per job created, while other companies got several thousand dollars per job created. Last, we noticed that some awards seem to clearly fit the purpose of the program while others were not as clear. So, for example, the bank

that got money to create jobs, that's pretty clear that it fits, not only the statutory purpose, but also fits kind of the intent of the program. On the other hand, the Renwick School district received $90,000 to create a Future Farmers of America chapter and to create some agricultural education programs at their high school. The statute allows that under unique economic development opportunities, but it was not clear to us that that really satisfied the intent of an economic development incentive program.

Andy Brienzo, Host and Principal Auditor: [07:46]
So why is the award decision making process subjective?

Heidi Zimmerman, Principal Auditor and Supervisor: [07:49]
So we found kind of two reasons that we thought were contributing to the subjectivity of this whole process. One was the statute itself. The statute doesn't provide any criteria that the department should consider when making decisions about who to award money to, nor does it direct the department to conduct any particular analysis to make sure the award will be cost effective. The statute is also quite broad in terms of that one category of unique economic development opportunities--that's a pretty broad category. There's a lot of discretion involved there. And so, we felt that the statute itself lent to a lot of subjectivity. The second thing came from kind of the department and how they viewed the job creation fund. They tended to view this primarily as a deal closing fund that was meant to keep Kansas businesses competitive. So from their perspective, these are funds you offer a business when you're trying to keep, maybe you're trying to keep them in the state, maybe they're looking at moving to another state and you want to offer some something to help maintain Kansas' competitive edge. So from their perspective, if that's what the fund is for, then they would need to maintain some flexibility and some subjectivity in awarding those funds because each of those projects would be very different.

Andy Brienzo, Host and Principal Auditor: [09:11]
Your second finding was that the department conducts limited verification to ensure companies meet the terms of the JCF agreement. What do best practices suggest in this area and what is the department actually doing?

Heidi Zimmerman, Principal Auditor and Supervisor: [09:24]
So best practices in this area emphasize the importance of requiring companies to submit relevant data and then review that data and then verifying the accuracy of that data. So basically, you want to do something to independently verify that the data they submit is in fact accurate and true. So, in terms of what the department was doing, there's a few things. So, first of all, the companies are required to create jobs and they have to submit information saying this is the number of jobs we created. We found that the department did verify job counts so when they asked the business to submit the number of jobs they also compared it to a Department of

Labor report and so we felt that was a good step and a good way of verifying that when a company said we created these jobs to make sure they did in fact exist. But there were a couple of other areas where the department didn't go quite as far as we felt that they should and as far as best practice would indicate that they should go. So, for example, a number of the projects we reviewed required the company to make specific capital investments or to raise matching funds. And you had to do those things as the terms of getting the funds. We found that although the companies often did report that information to the department, the department didn't take any steps to verify that that data was in fact accurate. Last, most of the awards that we looked at required the company to spend those job creation funds for very specific purposes--so to build a building or to implement a program. But we found that the department didn't even ask those companies to submit information about how they spent those funds and they weren't doing any other steps to verify it either. So companies are required to spend these dollars in very specific ways in order to get the money, but then the department isn't doing any verification that those funds were actually spent on the allowable purposes and so we felt that was a little problematic.

Andy Brienzo, Host and Principal Auditor: [11:35]
So based on your findings, what recommendations did you make to the Department of Commerce? And since this is a limited scope audit, as we mentioned before, what outstanding issues remained that might be worth evaluating in more detail in the future?

Heidi Zimmerman, Principal Auditor and Supervisor: [11:48]
We made three recommendations to the Department of Commerce. So, first of all that they should establish some criteria that it will use to evaluate job creation fund awards and then also a process for determining how much money it will award. We think that recommendation will address that first finding. Second of all, we recommended that the department should verify the data that companies submit to them is accurate. And then we had a third recommendation related to the department's annual report. In terms of issues for further consideration, as we mentioned earlier, this is a limited scope audit, so it's a very brief look into the program and so there were a couple of questions that we just didn't have the time to go into in detail. So, the first one was kind of what criteria do other states use to determine who receives funding for programs that are similar to the job creation fund? The department told us that most states do have a similar program. And so, understanding what criteria they use to evaluate awards could help the department establish their own criteria. So, the second issue involved something we talked about at the beginning where companies who didn't meet their goals are required to pay back money. So, we were not able to look in-depth at that payback provision. We were able to look at it very briefly, but it did prompt a question regarding, does the department use that function consistently and in accordance with the terms of the award agreement?

Andy Brienzo, Host and Principal Auditor: [13:22]
Finally, what's the main takeaway from this report?

Heidi Zimmerman, Principal Auditor and Supervisor: [13:25]
Currently, the funding that flows into this program is capped at $3.5 million annually. So, the department gets around $3.5 million or no more than $3.5 million every year to administer this program and to award funds. However, in 2021, that cap is going to be lifted and at that time the Division of Budget has estimated that when that cap is lifted, around $33 million is going to flow into that fund annually. So that's a pretty decent chunk of money. It's certainly a lot of money for the department to be overseeing with sole discretion in terms of how to distribute that money. So, in light of that, I think it becomes even more important that this program be administered in a transparent manner. That it treats all businesses in a consistent way and especially that it holds companies accountable so that taxpayer dollars are used effectively.

Andy Brienzo, Host and Principal Auditor: [14:29]
Heidi Zimmerman is a Principal Auditor at Legislative Post Audit. She completed a limited scope performance audit examining whether the Department of Commerce has process to administer and distribute job creation program funds is transparent and effective. Heidi, thank you for taking the time to walk me through your findings.

Heidi Zimmerman, Principal Auditor and Supervisor: [14:46]
Thank you Andy.

Andy Brienzo, Host and Principal Auditor: [14:47]
Thank you for listening to The Rundown. To hear more podcasts, subscribe on Spotify or Apple podcasts. For more information about Legislative Post Audit and our audit reports, visit our website kslpa.org and follow us on Twitter @ksaudit