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The Rundown podcast transcript for Performance Audit report titled **STAR Bonds Financing Program** – Released August 2021

Brad Hoff, Host and Recruiting and Training Manager: [00:00]

Welcome to The Rundown, your source for the latest news and updates from the Kansas Legislative Division of Post Audit, featuring LPA staff talking about recently released reports and discussing the main findings, key takeaways, and why it matters. I'm Brad Hoff. In August 2021, Legislative Post Audit released an economic development incentive evaluation of the sales tax and revenue (STAR) Bond financing program. I'm with Andy Brienzo, principal auditor at Legislative Post Audit who supervised the audit. Also, joining me in The Rundown studio is Dr. Daria Milakhina, LPA's audit methodologist, and one of the audit team members. Welcome to The Rundown, both of you.

Andy Brienzo, Supervisor and Principal Auditor: [00:48]

Thanks, Brad.

Daria Milakhina, Team Member and Audit Methodologist: [00:49]

Thank you, Brad.

Brad Hoff, Host and Recruiting and Training Manager: [00:51]

So, before we begin talking about the audit's findings, talk a little bit about what STAR bonds are, how do they work, and which other states have similar programs?

Andy Brienzo, Supervisor and Principal Auditor: [01:07]

So, STAR bonds are an economic development tool. They allow local governments to issue STAR bonds and then use the proceeds to finance private development. So, this is tourist attractions within development districts that the local government - so it's a city or county - has created and the proceeds from the bonds can be used to help pay for things like property acquisition, site preparation, and infrastructure and then the Department of Revenue uses part of the state and local sales tax revenue - this is where the name STAR bonds comes from - sales tax and revenue bonds - generated from the businesses in the district to repay the bonds. So, this is really a collaborative effort between the state and local governments because both state and local tax revenues are involved in retiring the bonds. So, state law generally requires that the bonds be retired in 20 years and then after that point, the attraction really should be self-sufficient and the state and local governments, once the bonds are retired, will start collecting the full amount of sales taxes that is being generated by the businesses in the district. So, we looked around for other states that have similar programs. To the best of our knowledge, Kansas created the first

STAR bonds financing program in the country. It looks like Illinois and Nevada also have programs that look like they were modeled on Kansas, but neither state appears to have used its program since at least 2010.

Brad Hoff, Host and Recruiting and Training Manager: [02:45]

How common are STAR bonds used in Kansas?

Andy Brienzo, Supervisor and Principal Auditor: [02:50]

The legislature first authorized the use of STAR bonds in 1993 and between then and November 2020, which is when we reviewed the data, 12 cities across the state have created 13 STAR bond districts, which include 20 tourist attractions. So, these 12 cities, they've issued about \$1.1 billion in total bonds, and about \$873 million in tax revenue has been used to pay off this bond debt. About 76% of that came from state sales and use taxes. and then about 24% came from local sales use and transient guest taxes. And one thing I'll point out is that I think probably the district that most people associate with STAR bonds, in other words, the one that sort of comes to mind first, when people think about STAR bonds, is probably Village West in Wyandotte county. So, that's kind of a unique district. It includes 6 of the 20 STAR bond attractions that exist across the state, and it actually accounts for 64% of the bonds that have been issued all-time under this program. So, \$726 million of the \$1.1 billion total were for Village West.

Brad Hoff, Host and Recruiting and Training Manager: [04:08]

Now state law gives Legislative Post Audit quite a bit of latitude to decide how to evaluate economic development incentives. Which approaches did you decide to use for STAR bonds?

Andy Brienzo, Supervisor and Principal Auditor: [04:23]

That's right. So, the state law that establishes our economic development incentive evaluation function that requires us to do these evaluations gives us quite a bit of latitude, as you say, to determine how to estimate the incentives economic and fiscal impact. So, for this evaluation, we decided to evaluate STAR bonds tourism. We also looked at a break-even analysis or conducted a breakeven analysis for three particular STAR bond attractions to get a sense of their fiscal impact. I'll get into that later on, but one of the primary analyses that we did for this evaluation was, as I said, looking at tourism. So, that's because we think generating tourism is really the primary purpose of the program based on our review of state law, legislative testimony, [and] program guidance put out by [Department of] Commerce. The STAR bonds financing act identifies the program's purpose pretty broadly. So, it says it's the promotion, stimulation, and development of the general and economic welfare of the state, including Kansas communities. But it also makes it pretty clear that tourism is an important component of STAR bond projects. So, for example, state law lists potential tourist attractions as the areas eligible for STAR bond financing. It requires a market study for each attraction. That's being proposed to determine its ability to gain local, regional, and national market share, and determine the attraction's ability to maintain its status as a significant factor for travel decisions. State law also requires feasibility studies for proposed STAR bond attractions, which should identify their visitation expectations. Now the broad

statutory purpose that the legislature has created for this program gives the secretary of Commerce discretion to select STAR bond attractions and in addition to tourism, Commerce officials said, they look at other things when considering proposed attractions like job creation, effects on local quality of life, and the ability to attract compatible industries. Now, current attractions likely have value from a purely local perspective. They enhance local quality of life by providing new amenities and they may stimulate local jobs, capital investment. They may increase local government tax revenues, but the thing that really sets this program apart from other economic development programs that also are intended to do similar things- to improve the economic and general welfare of the state is the tourism focus. And so we wanted to look at that in particular when we did this evaluation. Now that doesn't mean that these other possible approaches looking at these other things like job creation or capital investment wouldn't be valid. We think those would be valid ways to look at them at this program, we didn't do them. That doesn't mean we think it's not important. It's just that we have limited time and we felt this was a good first cut at this program because it really hones in on the thing that makes it unique among economic development incentives.

Brad Hoff, Host and Recruiting and Training Manager: [07:35]

Now that the Department of Commerce has a couple of tourism related goals for proposed STAR bond attractions. Talk a little bit about what these goals are and why they're important.

Andy Brienzo, Supervisor and Principal Auditor: [07:49]

So, the state law establishing this program doesn't include any requirements related to tourism. So this, these might be things like how many visitors a STAR bonds financed attraction might draw where they might be coming from how far away, things like that. But Commerce has established a couple of tourism related goals for proposed STAR bond attractions. So, when they're reviewing a proposed attraction, their guidance says that each attraction should draw 20% of visitors from outside Kansas and 30% of visitors from at least 100 miles away.

Daria Milakhina, Team Member and Audit Methodologist: [08:25]

And out-of-state visitors are important because those are new money for the state of Kansas that the state would not have gotten if they didn't come to Kansas. For example, if you have a family in Kansas thinking, "What are we going to do this weekend?" We can go to this STAR bond district that is close by or we can do something else, like go to the zoo. Those visitors probably would have spent this money anyways in Kansas. From the state's perspective, it doesn't matter. The state would still get these sales tax dollars, but if you have a family in Nebraska and they're thinking, "Okay, we want to drive somewhere." Suppose we can drive four or five hours. And this family would choose to spend their money in Kansas. Otherwise without STAR bonds, they would not have spent this money in Kansas. And that would be new, additional sales tax dollars that the state is gaining from out-of-state visitors

Brad Hoff, Host and Recruiting and Training Manager: [09:27]

Now to evaluate whether these current attractions are meeting these goals, the team spent some time looking for comprehensive and reliable tourism data for them. What did you end up using?

Andy Brienzo, Supervisor and Principal Auditor: [09:44]

So, the Department of Commerce created these two goals. So, 20% of visitors from outside Kansas, 30% of visitors from at least 100 miles away, but it didn't collect sufficient or reliable data to evaluate whether attractions are meeting these goals. So, Commerce officials said they received visitation projections as part of a feasibility studies, I mentioned just a few moments ago, but they get these years before attractions are built. Commerce officials told us that they're sometimes overly optimistic. And then prior to the 2021 legislative session, Commerce didn't have the authority to require visitation data from existing STAR bond attractions. So, as a result, some attractions hadn't given Commerce visitation data. By the time we conducted our audit, others had provided rough estimates or percentage changes over time, things like that, but we didn't have the ability to get from Commerce - comprehensive, reliable visitation data. So, we spent some time looking around and we settled on a company called Streetlight, which estimates visitation to various areas in the United States using cell phone and vehicle GPS location data and they typically work with transportation agencies, but their data are statistically representative of the US and Canadian populations, and we thought they were sufficiently reliable for our analysis. The other advantage to using Streetlight data is that it's a third party. So, it's data are inherently more likely to be objective than the data that STAR Bond attractions are self-reporting to Commerce.

Daria Milakhina, Team Member and Audit Methodologist: [11:24]

And because Streetlight data is representative of the US population and the composition of this population, we can rely on it to calculate the percentages of the tourists that came out of state to the attraction and also from a hundred miles away to the attraction.

Brad Hoff, Host and Recruiting and Training Manager: [11:44]

Based on Streetlight's data, it looks like only a few STAR bond attractions met the Department of Commerce's tourism goals in 2018 and 2019. So, which attractions met these goals and what does this tell you about the types of attractions that might attract tourists more successfully?

Andy Brienzo, Supervisor and Principal Auditor: [12:12]

So, we ended up evaluating 16 of the 20 STAR bond attractions. We looked at calendar years 2018 and 2019. We excluded 2020 due to the COVID-19 pandemic, which of course affected the tourism industry particularly badly. We also wanted to only include attractions that were complete and open to the public by early in the year 2018, so this left 16 attractions, as I said. Now of those 16 attractions, only three, according to the Streetlight data met both of Commerce's goals in one or both years we reviewed. So, the Kansas Speedway and Topeka's Heartland Park met both goals in both years and the Hutchinson Underground Salt Museum met both goals in 2019

and one of the two goals in 2018. And I just want to caveat our analysis of the Speedway. So, the Kansas Speedway didn't meet both tourism goals when we looked at visitation for the entire year, so 365 days out of the year, but Commerce officials told us to Speedway was built largely to host only a few major races each year. So, these are mostly NASCAR races. These are the big race weekends that the Speedway hosts. And during those days isolating those days, it did meet the tourism goals during 2018 and 2019. So, it met them during its major scheduled events, which are primarily what it was built for. And I think what we can draw from this conclusion is that really it's unique attractions that are most likely to meet Commerce's goals. So, as I said Heartland Park, Kansas Speedway and the Underground Salt Museum were the only ones that successfully met the goals. And we think they probably drew visitors from out of state and from far away because they're not available in many other places.

Andy Brienzo, Supervisor and Principal Auditor: [14:05]

So, the Speedway, of course, it's a major racing venue. and there's only so many of those in the United States. Heartland Park during the years that we reviewed 2018 and 2019 hosted national level racing events and of the states near Kansas, only Colorado and Illinois had had similar events in these years. And then the Underground Salt Museum is actually the only museum of its kind in the western hemisphere to our knowledge. I believe you'd have to go to Europe to get a similar experience. So, these are more likely to meet Commerce's goals in our mind because they're pretty unique attractions that are more likely to draw people from outside Kansas.

Brad Hoff, Host and Recruiting and Training Manager: [14:42]

The second question the team answered in this evaluation is how long it take the state to break even on the sales tax revenue it forewent for the three selected STAR bond attractions. Why did you decide to focus on this question as part of your evaluation?

Andy Brienzo, Supervisor and Principal Auditor: [15:07]

So, in addition to analyzing how well 16 STAR bond attractions drew tourists from out-of-state and from a hundred miles away, we also conducted a break-even analysis. So, we wanted to get a sense of the fiscal impact that three selected STAR bond attractions had on the state. So, the state gives up significant tax revenues to help repay STAR bonds. Since the program started, about \$668 million in state sales and use taxes have been used to help retire STAR bonds. So, we wanted to see whether the state might recoup this investment within a reasonable timeframe and to get at that, we looked at three particular attractions. Now, we didn't look at all of the attractions and we didn't include enough analyses in our work like return on investment, job creation, numbers, some of the indirect and induced economic effects, that we would need to look at to conclude on whether the program as a whole is successful or not. So, we're not commenting on whether STAR bonds is a successful program. We're not commenting on whether it is worth the money, but what we're trying to do here is get a sense of how three particular projects are fiscally impacting the state and get the audience for our report to start thinking about these things in maybe a new way. Maybe we start thinking about some of the

opportunity costs that come along with foregoing significant amounts of tax revenue that take several years to make up, thinking about whether some of these projects might've happened anyway, even without STAR bonds, thinking about different types of economic activity, new versus moving economic activity around. And just sort of thinking about this program and these projects in a way that maybe they haven't been before in addition to looking at how well they're attracting tourists and kind of give people a new look into STAR bonds as a program without necessarily concluding on the success or failure of the program as a whole.

Brad Hoff, Host and Recruiting and Training Manager: [17:21]

Okay. So now I want to shift a little focus and talk to Dr. Milakhina now over here and talk a little bit about the attractions and the methodology that you used. So, which three attractions did you select for review and how did you go about analyzing them?

Daria Milakhina, Team Member and Audit Methodologist: [17:42]

Right. We picked three attractions that are diverse enough to maybe cover different areas. Salt museum in Hutchinson, Prairie Fire in Overland Park and Sports Forum in Wichita. They are different in the sense that we have a sports arena in Wichita and we have two different museums. There's a smaller museum in Overland Park that has also a shopping area around it. And there is a bigger, and probably more unique museum in Hutchinson. Our analysis was a little bit different for each particular district. First, uh, we calculated the sales tax that the state was giving up and it was based mostly on, uh, what we think would have happened or would not have happened, without STAR bonds and, here it's, as I said, different for every district. For example, for Hutchinson, we knew that there was some development in the area besides the museum that now is included in the STAR bonds area. They have some shops and restaurants that were there and after the bonds were issued, the sales tax from this already existing development was given up by the state. So, we took this initial development that was there before STAR bonds and we calculated it until the STAR bonds are paid off, how much the state lost that the state would have been getting without STAR bonds. In Wichita, there was initial developments, but when the STAR bonds were issued, that was taken into account and the state was still getting sales tax from that initial development. However, this amount was not adjusted for inflation and because it takes a lot of years to pay out STAR bonds, it adds up if you adjust for inflation. For Overland Park, when we talked to the officials, it was clear that the area was going to still be developed with something similar because it's in the corridor or kind of the attraction corridor in Overland Park. And it would not have been just a field in the middle of the corridor and other things that were developing there. So, we assume that some of that would have been developed without the museum. So, we calculated how much the state is given up, because something would have been developed anyway. So, it was developed, but it was not adjusted correctly. Then we compared it to the benefits of the state. Once the STAR bonds are paid out, the state is getting additional sales tax. Now we made a couple of assumptions there and they're important. We talked before that the tourist money out of state are important because those are new money to the state. The money that come from the Kansas visitors are not necessarily are not necessarily new money to the state. I want to add though that's the tourist money from out of

state are also not necessarily, would not have happened to the state. For example, if the family comes to the wedding and then they go to the Salt Mine Museum, they were there already in the state so they they're spending money that they spend for the restaurants and hotel. They would have spent them anyways. They're just, if this museum was not there, they would not spend money in the museum. Because we try to choose our assumptions conservatively, we still assumed that every tourist that came to the state came there because of the STAR bonds museum. At the same time, we're probably a little bit under-estimating the expenditures that come from the Kansas residents, because maybe they increased their entertainment budget to go to these particular STAR bonds attractions. And otherwise, they would not have spent this money, but maybe save this money. So, they (money) would not come to the state in the form of the sales tax revenue. Now we calculate the benefit to the states, this additional sales tax revenue, after the STAR bonds were issued by taking the percentage of the out-of-state tourists and applying it to the projected sales tax revenue for the years after the STAR bonds issued. We calculated these benefits year by year, and then for every year after the STAR bonds were paid off. We compared this amount to the amount that was given out by the states during the STAR bonds time periods. And we ended up calculating when these two amounts are going to break even.

Andy Brienzo, Supervisor and Principal Auditor: [22:44]

I might just add that conducting this break-even analysis required us to predict what these three districts might have looked like in an alternative scenario where STAR bonds don't exist and it also required that we predict the choices that people would make in these alternative scenarios. So, we are making assumptions that are based on economic research and our own professional judgment, but these assumptions are necessarily uncertain because they don't reflect reality but using simplifying assumptions like this is common in economic analysis. So, we think it's a reasonable way to go about doing this work. Other people may have made different assumptions, doing the same analysis that would yield probably different outcomes, but that might also reflect different understandings of how people might behave under the alternative scenarios that we were thinking about.

Daria Milakhina, Team Member and Audit Methodologist: [23:40]

There is much more details to our analysis and assumptions that you can read in a longer version of the methodology in appendix B.

Brad Hoff, Host and Recruiting and Training Manager: [23:52]

It looks like the team estimated it will take decades for out-of-state visitor revenues to make up for the tax revenue the state gave up for these three attractions. Tell me more about this finding.

Daria Milakhina, Team Member and Audit Methodologist: [24:12]

So, when we estimated how many years it will take to break even we use the ballpark with less strict assumptions and more strict assumptions. We calculated that for Hutchinson it will take from somewhere from 43 to 118 years to break even, the costs to the state to the benefits. Their results for Hutchinson are mostly driven by the fact that this they did not exclude the existing development from the STAR

bond. So, they were initially losing a lot of sales tax revenue because of the STAR bonds and this is true for all three districts. The out-of-state visitations is not exactly really high. So, that was also contributing to all of the three results. Now for Overland Park, it would take 13 to 71 years to break even and for Overland Park, the thing that is driving the results is that a lot of this development would have happened anyways. So, the state is not getting new dollars because of the STAR bonds. And for Wichita, we found that it will take somewhere from 5 to 49 years to break even and it is a combination of some development existing there and not being adjusted to the inflation, but also not having enough out-of-state visitations.

Brad Hoff, Host and Recruiting and Training Manager: [25:50]

Finally, what's the main takeaway of this audit report?

Andy Brienzo, Supervisor and Principal Auditor: [25:55]

So, as I mentioned before, we're really looking at just a few aspects of this program. We can't conclude on whether overall it's a success or a failure, but we think we're looking at some of the big, the big elements here, tourism and the fiscal impact on the state because it's giving up a lot of tax revenue to support the three districts that we reviewed and we think these are important ways, new ways to look at this program. Our results suggest that really only a few attractions are generating the out-of-state tourism that we think legislators probably originally intended for this program. And although STAR Bond projects are likely benefiting their local communities in concrete ways, through things like job creation and capital investment and, you know, amenities that improve local quality of life and maybe bring in people from different areas, most of these attractions are not drawing in a lot of out of state visitors, which really significantly limits their ability to generate new revenue for the state. And as a result, legislators and Department of Commerce will have to consider the extent to which, these are the right types of projects to finance using STAR bonds and the extent to which they're willing to continue having them supported through this program.

Brad Hoff, Host and Recruiting and Training Manager: [27:15]

Andy Brienzo is a principal auditor and Dr. Daria Milakhina, is an audit methodologist at Legislative Post Audit. They worked on an evaluation of the STAR bonds financing program. Thanks to both of you for joining me today.

Andy Brienzo, Supervisor and Principal Auditor: [27:28]

Thanks, Brad.

Daria Milakhina, Team Member and Audit Methodologist: [27:29]

Thank you, Brad.

Brad Hoff, Host and Recruiting and Training Manager: [27:30]

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