

## MEMORANDUM

To: All Kansans  
From: Governor Sam Brownback and Lieutenant Governor Jeff Colyer, M.D.  
Date: February 10, 2011  
Re: Our Administration's Economic Development Strategic Plan

Last year, we ran on a platform called the Road Map for Kansas, and you sent us to Topeka to grow the economy, improve education, reform government, and protect the family. As part of that platform, we committed to providing you with an Economic Development Strategic Plan for the whole state. This memorandum to all Kansans is that Plan.

### **First Steps toward Greater Prosperity**

The ultimate goal of Kansas' economic development system is the prosperity of the state's citizens. A sound economic development process enhances prosperity through enhanced business-sector productivity; it creates, sustains, and renews economic opportunity for families by creating a vibrant business sector. After decades of piecemeal growth and change, the Kansas economic development system needs to be revitalized. The overall system can better advance the prosperity of Kansans by re-coordinating the many disparate parts and policies in a manner that makes it more effective, simpler, and fairer.

The state government has two fundamental roles to play in the process of economic development. First, it must establish a business environment that motivates as much risk-taking and competition as possible in the context of a "level playing field." Second, it must steward taxpayer resources in the most effective manner possible; when the government strives to do its job well with as few resources as possible, it leaves more resources available for risk-taking and competition.

From a policy perspective, a growth-promoting business environment has three general characteristics: (1) a cost-effective operating environment; (2) the ability to execute new ideas or plans as quickly as possible; and (3) predictability with regard to the "rules of the game." The state government has a substantial influence over these characteristics. However, there are no ridged formulas to guide action. The goal of our economic development policy should be to continually (and measurably) improve each of these three features on both an absolute basis and on a relative basis compared to other states.

- A cost-effective operating environment is one in which the government provides infrastructure and services of real value for the tax money it receives for such purposes. Value is not measured by the amount of money spent. It is measured by the delivery of the highest possible quality for the least amount of money spent. Creating a cost-effective

operating environment necessarily involves the issues of taxation, government spending, and government performance in the execution of its duties.

- Taxation is a claim the government makes on the economic value created by the private sector. Taxation involves how a dollar is extracted from the private sector and how many dollars are extracted from the private sector. The more the government taxes an economic activity, the less that activity will take place. To advance economic growth, Kansas needs to minimize the taxation of activities related to risk-taking and the process of economic competition. Once such taxes are minimized, the level of taxes collected must be minimized to keep as many resources as possible in the private sector.
- To minimize taxes, state government must prioritize its spending on activities that it is uniquely qualified to do better than any other entity. It must establish performance measures around these activities so that it can continually improve the quality delivered for each dollar extracted from the private sector.

The ability for businesses to act quickly on new ideas or plans and predictability with regard to the “rules of the game” relates to government laws, regulations, and compliance procedures. State government plays a key role in public health, public safety, and environmental stewardship. In this role, state government should continually evaluate its laws and regulations to ensure that they promote as much risk-taking and economic competition as possible.

To rejuvenate the Kansas economic development system and advance the vision guiding this economic development plan, state government must engage and learn from the business community. The economic initiatives described in this document begin this process. They do this in a few fundamental ways:

- A Council of Economic Advisors will begin the process of better coordinating the actions and resource allocations of seven different economic development-related organizations that tend to operate in an uncoordinated manner—and holding them accountable through rigorous performance metrics.
- A more uniform business tax policy that treats all businesses equally rather than the current set of rules and laws that give great benefit to a few (through heavily bureaucratic programs) and zero benefit to many.
- A change in funding procedure that will allow Kansas’ universities and community colleges to become better engines of economic opportunity.
- A program for improving the economic development of rural Kansas.
- Ensuring that the state’s development of transportation infrastructure generates the best economic development return possible.

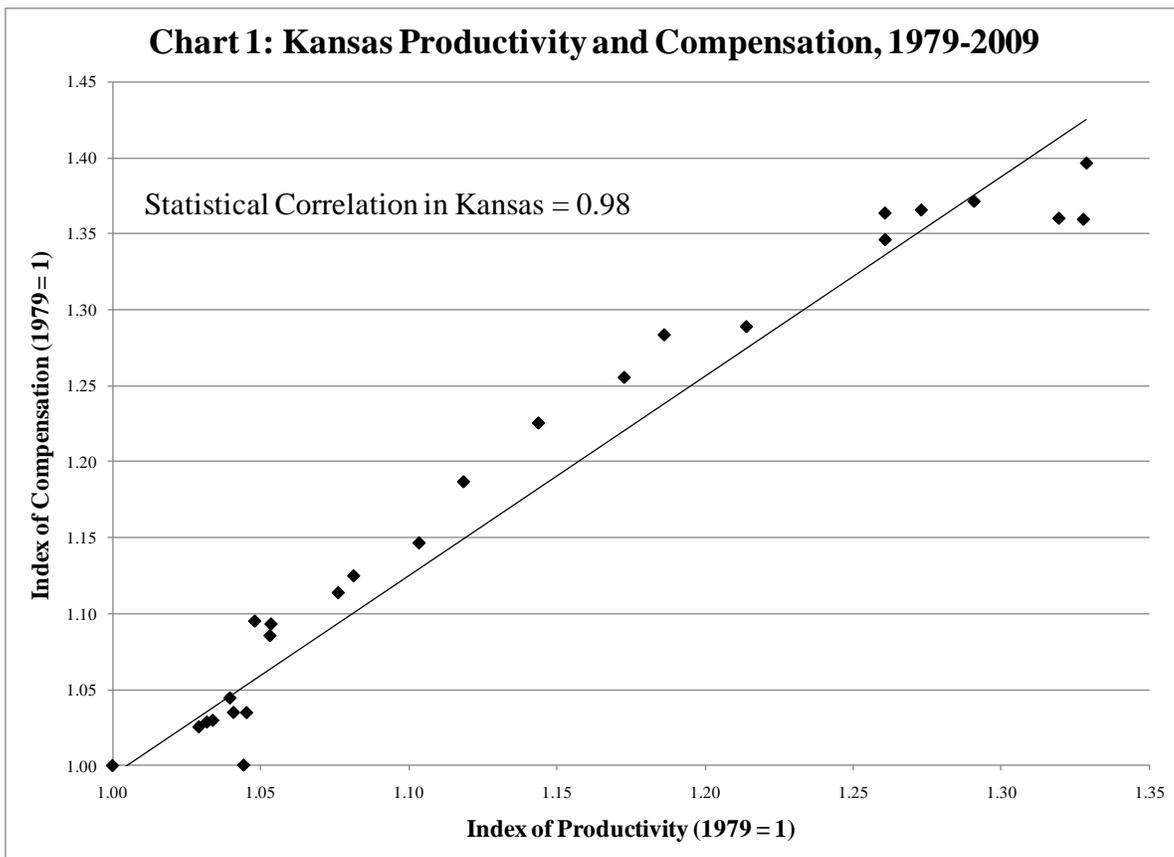
These initiatives represent a beginning. They create a focus for immediate and specific action. The first steps will form intelligent next steps as we gain experience, understanding, and insight into the interplay among current economic development programs and policies and the demands created by a new vision for economic growth in Kansas.

In any final analysis, making Kansas soil an attractive place for a broad array of people and businesses to commit their time and treasure best advances this administration’s goal of

economic development. A healthy economy is organic, not mechanistic; it resembles a healthy ecosystem, with strong patterns of stability and continuity punctuated by patterns of change. As with an ecosystem, the key to sustained economic development is to create the conditions necessary to promote as much diversity as possible through an on-going process of innovative adaption. Fostering innovative adaption means fostering business experimentation in every current and prospective Kansas business. And, as a practical matter, business experimentation requires a continual commitment of resources—human resources, financial resources, and physical resources—by tens of thousands of business units spread across dozens of unique sub-state (or regional) economies.

Economic growth is defined as a sustained increase, over a period of time, in the material goods and services produced within a specified geographic region. This definition allows for two basic sources of growth: (1) the number of people that produce; and (2) the efficiency with which the people produce over a given time period; that is, their labor productivity. The two elements can change at different rates.

The labor productivity component of economic growth drives labor compensation levels and thereby the average standard of living within an economy. Businesses cannot, on a sustained basis, pay workers more than the value of what they produce. Therefore, compensation levels should closely track increases in the average monetary value of output per worker. For the state of Kansas, over at least the past three decades, the relationship between the dollar value of output per worker (productivity) and compensation per worker is nearly exact, having a statistical correlation of 98 percent, as illustrated in Chart 1 below.



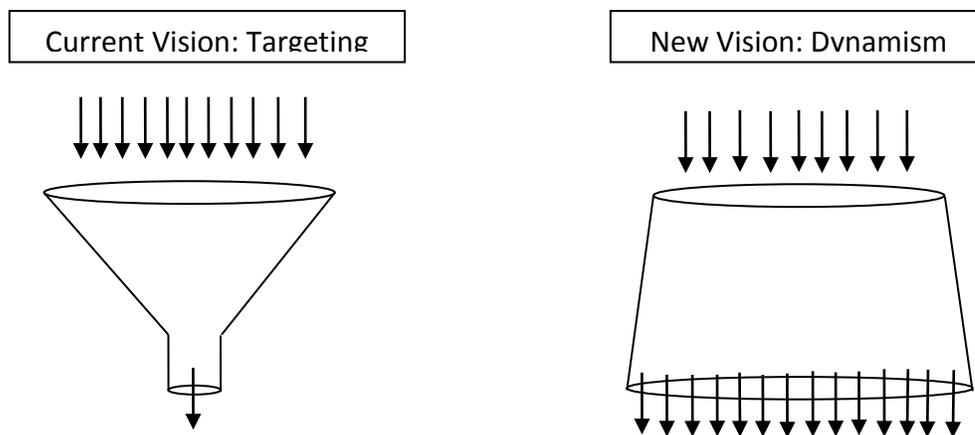
From the perspective of public policy analysis, people involved with the policy making process should distinguish between the terms “economic growth” and “economic development”. Economic growth has a concise, measurable definition. Economic development has a more amorphous meaning. Simply stated, economic development constitutes the many interrelated economic processes that culminate in economic growth—particularly the component of growth driven by improved labor productivity.

A process known as “capital deepening” defines the core aspect of economic development. Capital deepening simply refers to the capital intensity of the production processes within an economy. However, many complex economic phenomena underlie that simple meaning—phenomena associated with increasing rates of technological innovation and technological diffusion, increasing degrees of production specialization (including the manufacture of production capital itself), increasing organizational complexity, and increasing levels of relevant knowledge within the workforce. These phenomena must come together in a mutually reinforcing way on the front lines of individual businesses—usually through a risky process of trial and error—before economic development manifests itself as productivity-driven economic growth (and the resulting higher pay per job).

That is why every business, every innovation, and every entrepreneur matters. The more that Kansas’ economic development environment motivates each entrepreneur and business to engage in the trial and error process, the more the Kansas economy will generate economic opportunity for Kansas families. The initiatives described in this plan strive to motivate all manner of people—inside and outside the state—to commit their time and treasure to Kansas soil. The initiatives seek to increase the overall volume of new business starts and business expansions.

Kansans would be hard pressed to find anyone in the state who does not share the sentiment that every entrepreneur and every business matters. Yet Kansas economic development policy tends to work as if only a small sub-set of entrepreneurs or businesses matter.

The graphic below captures the essence of the current economic development system that seeks to target specific businesses for special benefits and the new vision for creating a rejuvenated economic development system that promotes maximum risk-taking and competition—economic dynamism.



Current Vision:	New Vision:
<ul style="list-style-type: none"> <li>• Dedicate considerable human and financial resources to the difficult task of predicting the “right” technologies or businesses.</li> <li>• Determine winners based on criteria like job count or specified wage levels—criteria often at odds with the goal of inducing profitable new business starts and expansions.</li> <li>• Reward winners with special privileges or resources at the expense of non-winners.</li> </ul>	<ul style="list-style-type: none"> <li>• Dedicate human and financial resources to promoting maximum experimentation through volume and diversity.</li> <li>• Establish stable policies that treat all investments and businesses equally, thereby liberating resources from the costly and economically dubious task of targeting.</li> <li>• Focus state resources on important activities that the state can do best: supply the “public goods” parts of the economic development process.</li> </ul>

The state government of Kansas need not commit scarce resources to the enormously difficult task of predicting the outcome of competition if it focuses on the much more manageable—and appropriate—task of creating the “playing field” on which competition takes place. By way of analogy, the new vision says: The State of Kansas runs tournaments; it does not field players. Creating a playing field to host world-class tournaments will attract world-class players. The playing field will endure but players will come and go.

## Measures

Accountability for the use of taxpayer resources represents a key feature of many of the initiatives described in this economic development plan. Similarly, the plan itself must have accountability features built into it. The plan will focus on the following measures of performance. Many of these measures are inter-dependent. General improvement in a varying combination of these measures will help provide evidence that the plan is advancing the goal of a more prosperous Kansas.

### *Employment*

Jobs are a vital element of prosperous families and communities. However, job creation is a result that derives from profitable business births and expansions. If Kansas performs well in the measures below, Kansas will also perform well in terms of job count.

### *Income Growth*

State or regional income growth occurs in some combination of: (1) an increase in the number of people earning income or (2) an increase in the income earned per person. Technically, “economic growth” means a sustained increase in per-person inflation-adjusted income. However, “economic development” can encompass both measures. For example, in many rural parts of Kansas, an absolute growth in income would measure successful economic development even if income measured on a per person basis remained constant. Such an

outcome would indicate an increasing density of economic activity, which works as a precursor to the economic conditions that drive higher per-person incomes.

### *Population Density and Population Migration*

Measuring economic development strictly by income has important limitations—particularly when the measurement focuses on sub-state regions. Put in simplest terms, people often trade quality of life for income, so the growth in income or the levels of income per person may embody such trade-offs.

Measuring the change in population (or employment) density and the prevailing trend of population migration offer measures that avoid the ambiguities associated with sub-state income measures. Growing population density and net population in-migration offer clear measures of growing regional economies (and vice versa).

### *Productivity*

Productivity growth is the ultimate goal of economic development. Productivity growth—the volume and value of output per worker—drives the growth of wages and wealth. Productivity growth results from a risky trial-and-error process on the front lines of individual businesses.

### *Capital Investment*

The act of investment by Kansas businesses must precede sustainable increases in productivity. From a business perspective, expected rates of return drive investment decisions. Most of the economic development programs offered to businesses in Kansas work to help improve the expected rate of return on business investment. But these programs tend to be selective rather than broad-based.

The new vision for economic development seeks to reverse this policy situation. Every business matters. The new vision will promote and establish policies that increase the expected rate of return on investment for all businesses, without bias. A measurable increase in the rate of capital investment in Kansas offers a clear signal that Kansas has established a sound strategy related to economic development.

### *Gross Business Starts and Expansions*

On average, each year in Kansas, about 7,000 businesses start; 6,750 close; 18,750 expand; and 17,950 contract. This tight symmetry of birth-death and expansion-contraction characterizes all parts of the U.S. economy.

A sound strategy must look beyond the failures (and, thereby, the net number of new business) and focus on the gross volume of business starts and expansions. A higher gross volume of business starts and expansion will mean more people have selected Kansas as the place to risk their time and treasure—a clear signal that Kansas has established a sound strategy related to economic development.

## **Governor's Council of Economic Advisors - Strategy Integration, Research, Coordination and Accountability**

Over the past two decades, Kansas has chosen to build an economic development model that primarily relies on free-standing agencies governed by independent boards of directors. This model offers a sound operational foundation: it provides for strong stakeholder input and offers continuity in the context of the transient executive leadership inherent in state government. However, the Governor's Office may not have a degree of influence over the operation of the overall system that corresponds with its presumed level of accountability.

The Kansas Department of Commerce holds the position in the state's model as the lead agency with regard to the implementation of economic development policy. Yet the department is the only executive agency and it has limited official means to act as the lead economic development agency with respect to the Board-directed agencies.

The Council of Economic Advisors proposed by this plan offers a response to the lack of coordination and accountability in the current economic development systems. The Council will both enhance and fill the original concept of Kansas, Inc. (which the state established in 1986 in connection with the so-called Redwood-Krider state economic development strategic plan). Kansas, Inc. was created to operate as the primary coordinating agency for research-driven economic development policy. Currently, Kansas, Inc. is the only agency in the state in which the sitting Governor is statutorily appointed to co-chair the Board of Directors. This appointment was intended to facilitate coordination across industries and agencies, and to put executive strength behind the Kansas, Inc. evaluations of other economic development agencies. Over the years, the original vision for Kansas, Inc. has yielded to the dispersed interests and agendas of the many stand-alone economic development-related agencies.

This plan seeks to dissolve the current structure of Kansas Inc. and replaced it with the Governor's Council of Economic Advisors. The Governor will chair the group, whose members will be comprised of 15 to 20 leaders and innovators of Kansas and American business. The Council members should mirror the landscape of the Kansas economy. The members could be leaders from within or outside the state. The Council will meet quarterly in conjunction with key events, such as the release of consensus revenue estimates or the Indicators of the Kansas Economy.

The Governor's Council and its staff Executive Director will work closely with the Governor to assure strategy integration, coordination and accountability across all of the state's economic development-related initiatives and agencies, including the Kansas Department of Commerce, the Kansas Department of Agriculture, the Kansas Department of Transportation, The Kansas Department of Revenue, the Kansas Department of Labor, the Kansas Bioscience Authority, and Network Kansas. It will have a comprehensive set of economic development-related responsibilities.

### *Organization of the Council*

- The Council will be chaired by the Governor of Kansas.
- The Council will be comprised of 15-20 business and industry leaders from across the state and nation.

- The Council members will serve at the invitation of the Governor for a term of three years, with possible re-appointment for one additional three-year term.
- The Council's membership will be representative of the diversity of the industries in the state of Kansas: agriculture, aviation, oil and gas, engineering, renewable resources, computer technology, information technology, health care, biological technology, finance, services, general manufacturing, and military. Consideration also will be given to industry innovators, leadership experience in the international arena, businesses with a large base of employees, and businesses with a small base of employees.
- The Council will have an Executive Director to manage the organization and oversee the implementation of the Council's directives or initiatives and shall report directly to the Governor.
- The Council will (a) be permitted to have an operational 501(c)(3) component so as to attract and mobilize private-sector funding for research; and (b) be exempt from state government procurement rules so as to promote quick and flexible operations.
- It will operate as a Board of Directors for economic development in Kansas.

### *Functions of the Council*

#### 1. Strategic Planning and Resource Coordination

- Expand and enhance—on an on-going basis—the Governor's economic growth initiatives, such that it becomes a comprehensive blueprint for all economic development-related planning and resource coordination.
- Implementation of the blueprint through a tightly-focused action plan that unifies the unique capabilities and responsibilities of all agencies tasked with duties related to economic development or economic growth. Coordination across all agencies of the Council's initiatives and directives—the details of the blueprint—is paramount. Appropriate coordination and prioritization is a deficient element of the Kansas economic development system.

#### 2. Evaluation of Policies and Agency Performance

- The Council will act to hold accountable all agencies tasked with advancing economic development in Kansas—and, by extension, the Governor's blueprint for economic growth.
- At least once each year, or at the discretion of the Governor, the Council, as part of its evaluation function and to assure coordination and progress with regard to the Council's blueprint, the Council will convene a Kansas Economic Summit with the heads of all economic development-related agencies and private sector leaders from Kansas and around the world. At such time, the various economic development agencies shall produce specific reports as prescribed by the Council.

- As directed by the Governor and Council members, evaluations will be conducted to assess the effectiveness of specific state policies and specific state agencies (including universities), as they relate to the goals of the Council’s blueprint. Evaluations will be conducted, as directed by the Governor and Council members, by (a) Council staff; or (b) outside entities under fair and unbiased evaluation designs and scopes. All findings of the evaluations will be reported to the Governor and Council members for review and potential follow-up action.

### 3. Research

- The Council, under the direction of the executive director, shall create and provide objective, data-driven research to inform the planning and evaluation functions of the Governor and Council members.
- The Council’s research function shall routinely conduct studies on Kansas’ basic industries, tax competitiveness, regulatory structure, along with any other topic deemed germane by the Governor and the Council members.
- The research produced under the Council’s direction shall be peer reviewed by unbiased, outside entities so that the Governor and Council members can be assured of its independence.
- The findings of all research produced under the Council’s direction will be submitted to the Governor and all Council members for their review and directives for follow-up action steps.

#### *Additional Agency Changes*

In addition to abolishing Kansas, Inc. and creating the Governor’ Council of Economic Advisors, this plan moves the functions of the Kansas Technology Enterprise Corporation (KTEC) into the Kansas Department of Commerce. KTEC came to life in the late 1980s as part of the Redwood-Krider state economic development strategy. Moving the many valuable programs that KTEC has created into the Department of Commerce will allow for better overall coordination and allow the Department, as the lead economic development agency of the state, to adopt a broader strategy for using the state’s assets most efficiently. The KTEC partnership programs shifting to the Department of Commerce for better coordination include:

- Mid-America Manufacturing Technology Center
- Biotechnology Innovation & Optimization Center (University of Kansas)
- Advanced Manufacturing Institute (Kansas State University)
- Information and Telecommunication Technology Center (University of Kansas)
- Kansas Polymer Research Center (Pittsburg State University)
- National Institute for Aviation Research (Wichita State University)

## Economic Growth Tax Reform

Tax policy plays a central role in economic development policy. Over the decades, Kansas has enacted a variety of tax policies intended to advance economic development. Many of them provide a meaningful economic incentive to make new investments and create new jobs. Almost all of the policies provide a meaningful incentive to a small number of worthy businesses to the exclusion of tens of thousands of other worthy businesses.

The initiatives in this plan seek to end the exclusion. They begin the process of fulfilling the vision that every business matters; they seek to replace the old vision of “targeting” with a new vision of “dynamism.” Every current and prospective business will have access to economic incentives to invest and create jobs—without needing permission from the state government to qualify.

Economic development efforts tend to have a big business bias. It is easy for people to comprehend large facilities and the employees that use them. However, a new data source known as Business Dynamics Statistics produced by the Center for Economic Studies of the U.S. Census Bureau with a grant from the Kansas City-based Kauffman Foundation reveals that the prevailing big business bias is the wrong focus for a jobs-focused economic development strategy. What matters most for job creation is the entire volume of new business starts and, secondarily, existing business expansions.<sup>1</sup>

In fact, research indicates that economic development strategies based on the recruitment of large employers tends to have negative effects over the long run. One of the best predictors of future economic growth for metropolitan areas is the average employment size of business establishments: larger average sizes are typically associated with slower future growth.

From 1977 to 2005 (the years of data availability from the Census Bureau), Kansas would have experienced negative net job growth in 22 of the 28 years represented in the data without the birth of brand new business establishments. The Kansas job market is in continual flux from four sources: business births, business deaths, business expansions, and business contractions. On average, Kansas businesses create about 149,000 jobs each year and eliminate about 139,500. Those numbers represent businesses with employees. Kansas has about 183,000 businesses without employees undergoing dynamic change. Many of them will become employers as the businesses mature. Over the five-year period from 2000 to 2005, brand new firms created almost all of the net new jobs. Smaller firms had a higher propensity to add net new jobs than larger firms, but the age of the firm dominates that pattern.<sup>2</sup>

This data explains the plan’s focus on all Kansas businesses, not just a targeted few. Job creation may be a key focus for many policy-makers concerned about economic development but job creation is a residual economic outcome of business dynamism. The policy challenge centers on promoting dynamism by establishing a business environment that induces the maximum amount of business birth and expansion without bias related to the size or type of business.

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<sup>1</sup> For an exposition using Kansas samples of the data, see Arthur P. Hall, “Embracing Dynamism: The Next Phase in Kansas Economic Development Policy,” Kansas Inc. Research Report, February 2010.

<sup>2</sup> *Ibid.*

The immediate tax policy strategy is to streamline the tax code and focus on a few basic incentives. The goal, within the limits of the budget, is to structure the tax incentives such that a maximum number of businesses have access to them.

### *Business Investment “Expensing”*

Expensing is a procedure related to the calculation of business income tax. Whenever a business makes a capital investment (whether equipment or structure), it is allowed to take a deduction against income tax for the depreciation of the investment. Expensing is one form of depreciation deduction. Expensing allows for an immediate deduction of the full investment amount instead of requiring a prescribed schedule of smaller deductions over multiple years.

Expensing, properly implemented, is a tax policy that treats all businesses equally. By allowing business taxpayers to capture the time value of money related to an investment, expensing results in uniform income tax treatment for investments of all types and sizes, given the tax rate faced by the business taxpayer.

Expensing shifts the time value of money from the state government to businesses undertaking investment. That shift explains the economic development “incentive.” It improves the expected rate of return on every investment. (Every investment-related tax credit works as an “incentive” for the same reason—they work to improve the expected rate of return on the investments they target.) This initiative seeks to make the investment-related tax incentive logically consistent and universally available rather than ad hoc.

The implementation of expensing in this plan is somewhat unique from a tax practitioner’s perspective. It seeks to provide the full value of expensing to each Kansas business investor that is not provided by the depreciation procedures allowed by federal tax law. For that reason, the tax deduction generated by the Governor’s expensing plan is not the equivalent of “full expensing” as practitioners would interpret it in a federal tax context.

### *P.E.A.K. – Promoting Employment Across Kansas*

PEAK is a new program that is consistent with the new vision and this plan. Expensing is the investment-related component of the tax program and PEAK forms the foundation for the labor-related component of the tax program.

PEAK allows qualified for-profit companies that are relocating jobs from outside Kansas or an existing Kansas business that is expanding and creating new jobs to keep up to 95% of payroll taxes over a period of five years or more. To qualify the company must meet certain criteria in number of jobs created, wages paid, and employee health insurance coverage.

### *Department of Commerce Job Creation Fund*

The Kansas “IMPACT” program, along with savings from the elimination of certain tax credits, will be converted to a multi-million dollar fund that can be used to close economic development deals. The “Job Creation” or contingency fund is designed to strengthen state incentive programs and give the Secretary of Commerce and Governor flexibility to make prudent decisions to close a deal on a prime economic growth opportunity without adding additional debt to the state.

## Universities as Engines of Economic Development

From an economic development perspective, universities should be evaluated as key elements of a “critical infrastructure”—infrastructure that supports the economic development process. State government has a fundamental role to play in the creation and maintenance of critical infrastructure. Few other entities have the incentive and resources required. Businesses will come and go but infrastructure is an element of on-going continuity that enables change and progress.

While innovation can happen anywhere, it tends to thrive in places characterized by “agglomeration,” which means geographies with dense commercial activity and populations. Density promotes a high volume of experimentation through commercial trial and error, which, in turn, promotes a co-evolution of mutually reinforcing economic activities based around experiments that succeed and lessons learned from experiments that fail.

Research suggests that universities can simulate the virtues of agglomeration found in big cities. Universities help in this regard for two reasons. First, the overall stock of knowledge acts as a springboard for further knowledge. A cumulative impact emerges from knowledge generation. Second, small firms in particular can often utilize universities for access to research and development. However, universities also can foster technological innovation throughout more mature industries. The university-related economic development strategy of this plan focuses on three of Kansas’ core strengths:

### *Wichita State University – National Institute for Aviation Research (NIAR)*

NIAR will help a vital element of the Kansas economy – aviation - remain competitive in world markets in the 21st century. Two critical components necessary to ensure continued aviation-sector growth are research and training. Wichita State’ National Institute for Aviation Research is the one of the nation’s top aviation research facilities. To complement NIAR, industry and local units of government have created in Wichita the National Center for Aviation Training which will train thousands of Kansas for high-paying aviation jobs.

#### 1. National Institute for Aviation Research

- The FY2012 budget report includes \$5,000,000 from the state general fund for NIAR. This funding will be administered by the Department of Commerce and will require Wichita State University to match these dollars one-for-one in either repurposed funds or funds raised privately.
- Wichita State University will be required to provide return-on-investment metrics the progress toward which is to be evaluated periodically by the Governor’s Council of Economic Advisors and the Department of Commerce.

#### 2. National Center for Aviation Training Funding

- The FY2012 Budget Report includes \$5,000,000 for the National Center for Aviation Training from the Economic Development Initiatives Fund.
- The Center will be required to provide return-on-investment metrics the progress toward which is to be evaluated periodically by the Governor’s Council of Economic Advisors.

### *University of Kansas –National Cancer Institute Designation*

An exciting opportunity for future economic growth in the state resides in the University of Kansas' initiative to secure National Cancer Institute (NCI) designation from the National Institutes of Health (NIH). Continued support for NCI designation is a smart state investment and it will spur the ascendancy of the University of Kansas as a medical center of national significance, improving its ranking and reputation, and having a positive impact on the state's health care economy.

- The FY2012 budget report includes \$5,000,000 from the state general fund for the University of Kansas-NCI Designation initiative. This funding will be administered by the Department of Commerce and will require the University of Kansas to match these dollars one-for-one in either repurposed funds or funds raised privately.
- The University of Kansas will be required to provide return-on-investment metrics the progress toward which is to be evaluated periodically by the Governor's Council of Economic Advisors and the Department of Commerce.

### *Kansas State University—Animal Health National Bio and Agro-Defense Facility Dividend Initiative*

The selection of Kansas State University as home to the National Bio and Agro-Defense Facility (NBAF) provides a rich opportunity to build an integrated, private-sector animal health economic growth dividend for Kansas. In order to secure this dividend, an intense private sector collaboration/commercialization initiative is required.

- The FY2012 budget report includes \$5,000,000 from the state general fund for Kansas State University—Animal Health NBAF Dividend initiative. This funding will be administered by the Department of Commerce and will require Kansas State University to match these dollars one-for-one in either repurposed funds or funds raised privately.
- Kansas State University will be required to provide return-on-investment metrics the progress toward which is to be evaluated periodically by the Governor's Council of Economic Advisors and the Department of Commerce.

It is our clear intent to evaluate these university-related initiatives so they produce a measurable return on investment. Universities represent a form of "critical infrastructure" for the state, but the mere provision of this infrastructure is not enough. We must demand results that drive economic development for the State of Kansas.

One key result that must emerge, one that is easily measured, is the generation of new research funding. In the United States, the federal government, primarily in partnership with universities and colleges, dominates basic research funding. Industry essentially takes over once research and development reaches an applied stage. Industry performs almost 70 percent (and funds almost 60 percent) of the applied research; the federal government funds about one-third. Industry dominates both the performance and funding of research and development that has reached a mature stage—the stage, which, over the past decade, has

absorbed more than double the financial resources dedicated to basic and applied research combined—the stage most likely to have direct implications for productivity increases.

Kansas handicaps itself with regard to technology-based economic development by not attempting to leverage as much federal research and development funding as possible. Nationwide, about 15 states control about 75 percent of federal research and development funding. Kansas commands less than one percent that funding. An operational focus that tightly links Kansas' state funding to federal funding offers substantial benefits.

Because Kansas commands such a small share of federal research and development funding, it is enrolled with 18 other under-performing states in a federal program known as the Experimental Program to Stimulate Competitive Research (EPSCoR). The program requires state matching funds and is designed to help escalate university-industry partnerships in states that receive a disproportionately low per capita average of federal research dollars.

This plan entrusts the Kansas Board of Regents with this program. The Council of Economic Advisors will evaluate the Regents' performance to ensure Kansas universities substantially improve their performance in acquiring federal and industry funding. We must demand that Kansas universities meaningfully leverage their capabilities into measurable performance in the realm of private-sector partnerships—partnerships with both emerging and mature companies.

## **Rural Growth**

Kansas is caught up in a century-old trend related to population shifts in the Great Plains. From an economic development perspective, the Great Plains region has experienced urbanization while the remainder of the country has experienced de-urbanization (relatively speaking).<sup>3</sup> This transformation process had a direct economic influence on the declining populations of rural counties. We must take a keen interest in promoting the prosperity of the rural regions of Kansas. Initiatives in this area act as a complement to the broader initiatives.

Research on the economic development of rural areas has produced some consistent findings:

- Income support payments to farmers do not spill over to the nonfarm sector. Counties that have a higher share of income from farm sources grow more slowly. Furthermore, higher farm incomes are associated with slower nonfarm population and income growth. Counties with a higher share of farm income derived from farm support payments also grow more slowly.
- Rural areas grow faster when they have a diversified economic base.
- Businesses that form in rural areas tend to have longer life spans than businesses that start in urban areas. However, entrepreneurs must perceive the potential for higher after-tax profits in rural areas to compensate for the additional risk of business failure in rural areas.

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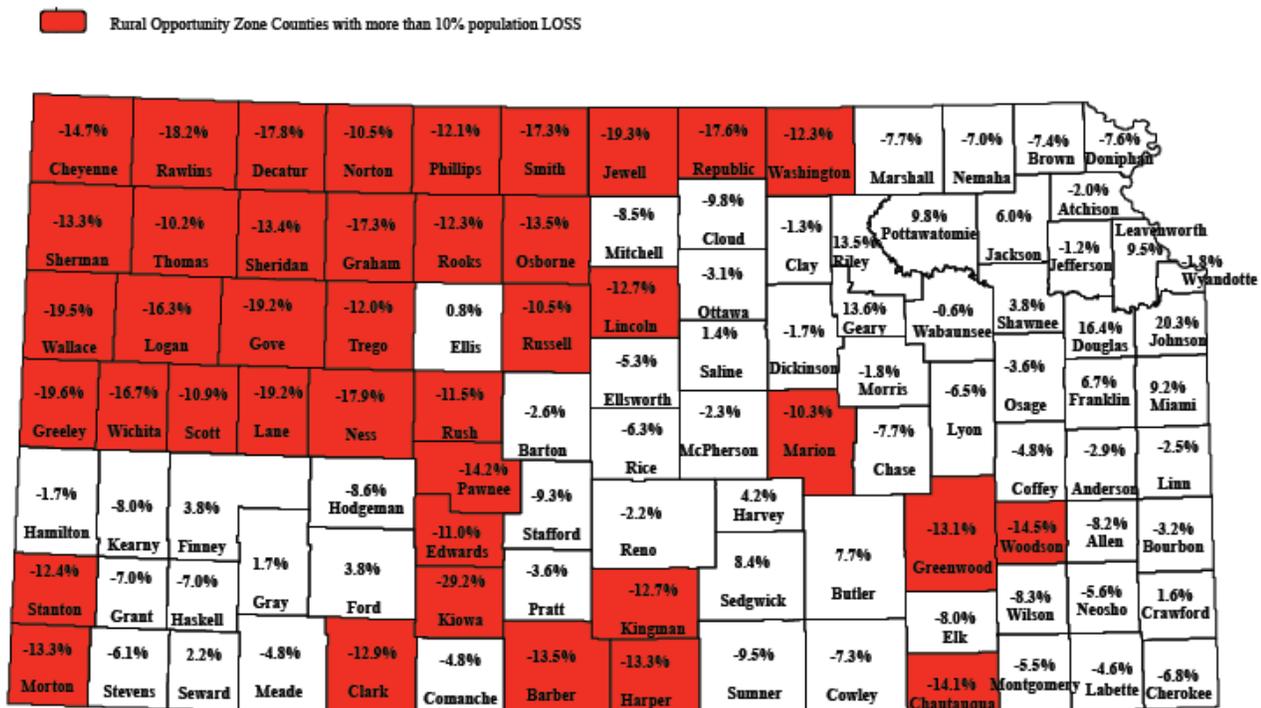
<sup>3</sup> For evidence, see Arthur P. Hall, Scott Moody, and Wendy P. Warcholik, "The County-to-County Migration Patterns of Taxpayers and their Incomes, 1995-2006," Technical Report 09-0306, March 2009, Center for Applied Economics, University of Kansas School of Business.

- Rural economic development is best executed in the context of a region-specific focus—an execution that effectively leverages state and local resources in a manner that acknowledges the unique resources, opportunities, and market knowledge of each region.

One of the nation’s true challenges is how to effectively enhance prosperity in rural America. For the purpose of these programs we will define rural as an incorporated community of less than 10,000 people. The goal is to improve the quality of life in rural Kansas.

### Rural Opportunity Zones

- Offer an income tax rebate for a period of five years to residents who move from out-of-state into Kansas Rural Opportunity Zone (defined as counties that have suffered double-digit percentage population decline over the past decade).
- Offer state-county partnerships for paying down student loans of residents who move to a participating Rural Opportunity Zone from out of state.
- The Governor’s Council on Economic Advisors will monitor program effectiveness through established return-on-investment metrics.
- It is anticipated that because the incentives inherent in the rural opportunity zones are targeted to new business and the migration into the state by persons previously living in other states, there will be minimal fiscal impact.
- Counties eligible for Rural Opportunity Zone designation must have experienced a population loss of 10 percent or more over since the 2000 Census. Based on that criterion, the following map shows the Kansas counties immediately eligible to participate in the program.



## **Kansas Department of Transportation – Full Economic Growth Partner**

Transportation infrastructure is a vital component of economic development. Yet not all projects are “good” projects from an investment perspective. The need for prioritization is made more important not less by the success of the three major transportation plans Kansas has implemented over the past two decades. Every new project increases the total available transportation infrastructure available to Kansans and thereby makes the incremental value of the each new project less important to the overall economy—an economic concept known as diminishing marginal returns.

The state government of Kansas spends more than \$1 billion annually on transportation-related projects. Coordinating and evaluating these expenditures as investments requires a healthy—and objectively demonstrable—economic development rate of return. The state government’s prioritization of transportation will benefit from rigorous methods of prioritization. The Kansas Department of Transportation must be a full economic growth partner with the Governor and have a prominent seat at the table of prosperity enhancement.

The Governor’s Council of Economic Advisors will include KDOT in all economic growth deliberations and meetings. Additionally, the Council will collaborate with KDOT to determine a proper model for analyzing relative economic benefit of each new project and to also create a mechanism to test return-on-investment achieved on select past projects to test economic growth impact.

### *Wichita Fair Fares*

The Fair Fares program is used to motivate low cost air carriers to provide services to the Wichita market. The Center for Economic Development and Business Research at Wichita State University has consistently found that the Fair Fares program passes a cost-benefit analysis and makes a positive contribution to the economic performance of the state’s south-central economy. This program is one important element of an overall transportation-related strategy. Convenient and cost-effective access to one of the state’s primary business centers is consistent with the goal of expanding commerce to increase economic growth.

### *Wichita Fair Fares Funding*

- The FY2012 budget report includes \$5,000,000 from the economic development initiatives fund.
- Wichita will be required to provide return-on-investment metrics, the progress toward which is to be evaluated periodically by the Governor’s Council of Economic Advisors.

## **Economic Development is an On-Going Process**

The specific initiatives described in this document represent the beginning—not the end—of a long-term transformation process. Implementation and measurement related to the specific initiatives of this plan will set up the necessary starting points for an on-going process of evaluation and learning.

We have seen in recent years that state budgets decline when economic growth lags. The best way to ensure that our schools are fully funded is to grow the state and local economies. The best way to ensure that there are resources for necessary social services to our most vulnerable citizens is to have a growing economy. To achieve this, Kansas needs to be competitive both nationally and internationally. This can only happen if our state keeps its taxes and regulations down, improves the playing field for all businesses, and maintains world class university programs and transportation infrastructure.

We can do it.

We will do it.

Our Strategic Economic Development Plan is only the beginning. We look forward to working with all Kansans to make our state the best place in the country to live, work and raise a family.

Please join us in this effort.