BEYOND PLASTIC

Capital One Sticks with Plan to Buy Hibernia

On Nov. 14, 2005, Capital One Financial Corp. became the 19th-largest bank in the nation. The McLean, Va., company, known for its credit card and consumer lending business, had announced in March that it would pay $5.35 billion for Hibernia Corp. The news was not a total shock. Capital One had previously said it was interested in buying a bank for several strategic reasons.

The whole deal looked shaky on the scheduled closing date, however. It was Sept. 1, just days after Hurricane Katrina ripped through the Gulf Coast and flooded New Orleans, Hibernia's headquarters city. The parties immediately pushed back closing a week, and announced a renegotiated sale price of about $5 billion with closing set for November. Under terms of the deal, Hibernia becomes a Capital One subsidiary and gives up its name.

Capital One completed its foray into retail banking in November with the purchase of New Orleans-based Hibernia.

In a Sept. 20 conference with investors, Capital One's Chief Financial Officer Gary Perlin said that of Hibernia's more than 300 branches, 21 suffered significant damage, but that most are expected to reopen. As the largest bank in Louisiana, Hibernia is expected to play a lead role in the reconstruction effort, serving as a conduit for federal and insurance funds that flow into the region. "We've been working very closely with Hibernia to take advantage of those opportunities," Perlin said.

As for Capital One's overarching plan, Perlin said: "It's very much in line with Capital One's strategy of building and maintaining leadership positions in a number of national-scale lending businesses in the consumer space. Hibernia adds to that a local scale deposit business in Louisiana as well as growth opportunities they have demonstrated they can take advantage of in Texas."

Other advantages of getting into retail banking include the ability to sell credit cards to banking customers, who tend to be better credit risks than people without bank accounts. It's also a clear-cut survival strategy in a time when pure-play, or mono-line, credit card firms are disappearing and big banks are concentrating on the credit card business.

"The mono-lines are going out of business," says Tony Plath, a finance professor at the University of North Carolina at Charlotte. "Their operating income cycle tends to be more volatile because their business line is concentrated in just one or two businesses. They're also vulnerable because they can only grow their business in one way."

— DOUG CAMPBELL

A "DRIVER'S LICENSE" FOR WORKERS?

Virginia Leads in Issuing Employability Certificates

Matching skill supply with demand in labor markets can be tricky. Work force development and education officials in the Fifth District hope to bridge the information gap with "employability" certificates. This portable credential aims to reduce friction in labor markets.

Virginia has awarded more than 5,000 certificates since 2004. With the backing of the Virginia Manufacturers Association and other business groups, companies such as Northrop Grumman Newport News have used the certificate during the hiring process.

Virginia's Career Readiness Certificate (CRC) is designed to ensure that the recipient meets certain standards in reading, applied mathematics, and information retrieval. Those three skills meet the basic requirements of 85 percent of jobs, according to the non-profit ACT Inc., a testing firm. The certificate includes an exam score and a description of its meaning. Exams are administered at 44 local work force development centers and at the state's 23 community colleges.

Workers armed with a CRC have information on their employability that is widely understood and accepted. That can give them greater geographic freedom in the job search. On the flip side, an employer with operations in different locations could use the same CRC to evaluate workers.

PHOTOGRAPHY: COURTESY OF CAPITAL ONE

Companies have long relied on some sort of credential to signal whether an applicant has the minimum skills for a job. This credential has usually been a high school diploma, but that may not be good enough for some jobs anymore.

"More and more jobs require some postsecondary training," says Jon Erickson, vice president of educational services for ACT Inc. "At the same time, high schools have had a glut of students, teacher shortages, and a whole bunch of curriculum issues." His company's skill assessments are being used to develop a certificate equivalent to Virginia's CRC in the District of Columbia, Maryland, West Virginia, the Carolinas, and other states.

"Employers have gotten frustrated because credentials don't guarantee that people have the skills they want," adds Sondra Stein. She is program manager for a Work Readiness Credential under development at Equipped for the Future, an initiative funded by the National Institute of Literacy, several trade and nonprofit organizations, and governments in five states and the District of Columbia. (D.C. is involved in the development of two different employability certificates.)

Stein says that public schools devote more time to developing core academic skills at the expense of "soft" skills like communication and cooperation that are highly valued in the workplace. At the same time, employers have raised the bar for what they need in a worker.

That's why some firms look for employees with an associate degree from a community college or a professional certification. But even this information may be inadequate.

While working as chief economist at the State Council of Higher Education for Virginia, Fletcher Mangum held focus groups to find out more about the intersection of education and economics. "One of the things we commonly heard from business owners was that a degree didn't really tell them what skills a person had," says Mangum, now a Richmond-based consultant. He worked on the taskforce that developed Virginia's CRC. "A degree was too generic and the quality of the information it conveyed about the person's skill sets and educational level varied from institution to institution."

Mangum says it's more efficient for government to administer a single statewide assessment rather than use many tests individually provided by employers. "Employability certificates remove a lot of uncertainty from the [hiring] process," he notes. Skeptics of the approach, though, note that a decentralized certification system has served many companies well, and are reluctant to see any single system crowd out competitors. — Charles Gerena

Edison Schools in the Fifth District

	Elem.	Middle	High
Allendale, SC	2	1	1
Baltimore, MD	3	0	0
Charleston, SC	5	2	1
Washington, D.C.	2	1	1
TOTAL	**12**	**4**	**3**

SOURCE: Edison Schools Web site

PRIVATE ENTERPRISE, PUBLIC SCHOOLS

Three Baltimore Schools Improve Test Scores

Three Baltimore public schools under for-profit management since 2000 have made progress, according to federal academic standards. And two of the three schools have made it off Maryland's "needs improvement" list.

From the beginning, the decision to pay the private firm, Edison Schools, to manage three failing inner city elementary schools was controversial.

"When they first came in, everyone was in an uproar because someone was taking over their neighborhood school," says Zelda Holcomb, Edison's operations vice president and general manager for the Baltimore region.

Edison's contract has been renewed through 2007. The state pays the firm and then subtracts the total cost for running the three schools from the city school system's funds. In the 2003-2004 school year, the most recent for which data is available, Edison received $8,880 per pupil to operate three Baltimore schools, according to Mary Clapsaddle of the Maryland State Department of Education's accounting office. Money for Edison employees' retirement comes from the city school system. Edison is the nation's biggest for-profit manager of public schools, with 136 schools in 19 states and the District of Columbia in 2005-2006. The firm earned an after-tax profit of $700,000 on revenues of $411 million for the fiscal year ending June 30, 2005. It was the first profitable year for Edison, which opened its first four schools in 1995.

Jim Foran of the Maryland State Department of Education likes Edison's work. "The professional development, community involvement, the inviting environment when you go into one of these schools — it looks very different than when you go into one of these [other] urban schools," Foran says.

All three of the schools made "adequate yearly progress," a benchmark established by the federal government. Before Edison assumed management, the three public schools in question were among the worst in the city. "AYP [adequate yearly progress] is a measure the federal government established for schools showing sufficient progress not to be put into an improvement activity," he says. "It's an assurance to parents that schools are operating well, academics are serious, and children on average perform well enough on that benchmark."

Edison Schools aims to raise achievement through curriculum changes, technology, professional development, and parental involvement. Holcomb says the Edison model works. "These are the research-based techniques for professional development, the structure of the school, and behavior management," she says. "It's data-driven accountability."

For example, the schools have encouraged various adult groups to help out. A group of volunteers, calling themselves the Mighty Men of Montebello, works with Montebello Elementary School, a school of nearly 1,000 students, 84 percent of whom receive a free or reduced-price school lunch, an indicator of poverty. A grandparents' club also has been formed at that school. "We have some people on the board at Furman-Templeton [another Edison school] from the local church," Holcomb adds.

The contract will automatically terminate in 2007 because the federal No Child Left Behind Act supersedes the state legislation under which the state assumed control of the failing schools. Foran says that even though the state no longer has the ability to take over individual schools under the act, the city could become a partner with Edison Schools or form charter schools, deregulated public schools that are designed to deliver on goals stated in the charter.

It is difficult to compare achievement results in Edison Schools with other schools. A RAND Corporation research brief, commissioned by Edison, examined Edison schools and reports: "Edison results relative to comparison schools improve in years four and five, but whether those improvements ultimately yield net positive effects is the key question." — Betty Joyce Nash

NATIONAL FLOOD INSURANCE

Henderson County, N.C., Joins the Crowd

County officials in Henderson County, N.C., balked at joining the National Flood Insurance Program for years. They figured that by not passing a flood ordinance, one of the requirements for joining, they were doing the county's heavily developed landscape a favor: People couldn't get loans to build in flood areas without insurance and so they just wouldn't build in risky places. (See "After the Flood" in the Winter 2004 issue of *Region Focus*.)

Wrong. Rocky Hyder, Henderson County's coordinator of emergency management services, says that demand for property in the scenic mountain county had gotten so high that the cost didn't discourage developers from filling in properties that were technically in flood-prone areas. And, on top of that, the county was ineligible for most types of federal disaster assistance after Hurricanes Ivan and Frances, which hit the county hard in 2004. So, after four months of controversy, Henderson County commissioners finally passed the county's flood ordinance in July 2005.

"Due to the current regulations both at state and federal level with regard to participation in the National Flood Insurance Program, and limitations implemented by state and federal government for disaster assistance funds, the staff felt like we had to adopt some type of flood damage prevention ordinance and participate at some level," Hyder says. Two enforcement officers were added to the staff. The law prohibits development in the flood way, the most vulnerable land near rivers and streams. About 10 percent of the county's land lies in a flood-prone area.

"It also prohibits most development in about 80 percent of the flood fringe, an area mapped on the flood insurance rate maps," Hyder says. "The commissioners basically said if you had an existing lot at the time the ordinance was passed, then 20 percent of the lot in flood fringe could be modified, but no more than 20 percent, so as not to transfer flood storage to a neighbor." When flood-prone areas are filled in one place, typically land elsewhere along the stream will be affected. After all, floodwater has to go somewhere.

The National Flood Insurance Program, under the Federal Emergency Management Agency (FEMA), allows homeowners to buy flood insurance from private insurers who are paid to administer the program. The U.S. Government Accountability Office has found that while FEMA has kept the program financially sound in general, the floods of 2004 and 2005 have required FEMA to borrow $300 million, as of August 2005, from the U.S. Treasury to help pay an estimated $1.8 billion in flood insurance claims. After Hurricane Katrina, Congress increased FEMA's borrowing power from $1.5 billion to $3.5 billion. As of August 2005, the NFIP had about 4.6 million policyholders in about 20,000 communities. Since it began in 1968, the program has paid out about $14.6 billion in claims, mostly through premiums.

The program, though, is not actuarially sound — about 29 percent of policies were subsidized, the GAO reported in 2003. "As a result of these subsidies, some policyholders pay premiums that represent about 35 percent to 40 percent of the true risk premium." — Betty Joyce Nash

WINNING TICKET?

Lottery Coming to North Carolina

North Carolina is set this spring to become the 42nd state nationwide — and last in the Fifth District — to operate a lottery. State lawmakers last summer narrowly voted in favor of adopting a lottery, and Gov. Mike Easley signed the North Carolina State Lottery Act into law on Aug. 31. Tickets are tentatively set to go on sale April 5.

As is the case with many other state lotteries, proceeds from North Carolina's are chiefly to go to education. The state expects to reap $425 million for educational purposes in fiscal 2006. Easley has been pushing for a lottery since 2001, arguing in part that the state was losing potential revenue to neighboring states with lotteries. His goal is to use the money to reduce classroom sizes. North Carolina's move into state-sponsored lottery follows South Carolina, which joined the ranks in 2002.

Cashing In

About one-fourth of the U.S. lottery proceeds go to government coffers.

	Lottery Sales (mil.)	Profit (mil.)
DC	$245	$76
MD	$1,395	$458
SC	$950	$290
VA	$1,262	$408
WV	$1,303	$512
US	$48,801	$13,902

SOURCE: North American Association of State & Provincial Lotteries; Fiscal Year '04

Lotteries in the United States generated total sales of $48.8 billion in fiscal 2004, according to the North American Association of State & Provincial Lotteries, with "profits" — or the amount transferred to state coffers — of $13.9 billion.

In adopting lotteries, states face controversial trade-offs. With the windfall of revenue come questions about propriety of depending on gambling to fund education. After all, the chance of winning many lotteries is worse than one in 135 million. Additionally, as argued by the nonprofit Tax Foundation, lawmakers can sometimes "shuffle other funds so that lottery tax revenue supplants, rather than supplements, existing funds for education."

Some economists describe lotteries as a de facto excise tax, in which the cost is borne by those paying for the product. This feeds the problem that a small percentage of players accounts for more than half of all lottery sales, and that those with household incomes of less than $10,000 represent nearly 10 percent of the heaviest players. (See "The Revenue Game" from the Fall 2002 issue of *Region Focus*.)

Additionally, publicly run lotteries tend to have very high operating costs. So if you aren't opposed to them for normative reasons — that is, you think it's just wrong for the government to sanction this activity — then you still might want to consider having the state turn the operations over to a private firm. This would yield a higher share of "profits" to the state, even after the private firm takes it cut.

The regressive nature of lotteries is problematic in the sense that low-income households aren't just substituting expenditures on lottery tickets for other forms of gambling; they are spending less on necessities such as food and clothing. That's according to a recent study by Brookings Institution economist Melissa Schettini Kearney published in the *Journal of Public Economics*. Kearney concluded that the average household reduces consumption by $41 a month in response to the introduction of a state lottery. This finding also weakens the argument that states are losing revenue to neighbors who offer lotteries; most of their residents weren't gambling in the first place until the new lottery came along.

Lawmakers can mitigate the regressive nature of the lottery, Kearney says. Low-income lottery players tend to buy instant "scratch-off" tickets rather than the bigger jackpot "lotto" games. "If you want your state lottery to be less regressive, then you should focus on the bigger jackpot games or limit how many instant games you offer," Kearney says. — Doug Campbell

A DANVILLE TRADITION NO MORE?

Indian Firm Buys Dan River Inc.

Dan River Inc., based in Danville, Va., was sold in January to an Indian firm, GHCL Ltd. The price has not been officially disclosed, but Indian media and other sources place the number at about $17.5 million, along with the assumption of about $80 million in debt. Dan River emerged from Chapter 11 bankruptcy in February 2005.

The company, rooted in Danville since 1882, currently employs about 1,700 workers in the United States, including roughly 1,100 in the Danville region. Nearly 500 of those people will lose their jobs in March due to planned cuts in production near the company's headquarters.

The company has been shedding workers and facilities for some time. "It is not a new thing," says Calvin Barnhardt, vice president of human resources at Dan River. "We have, since 2002, closed probably 14 facilities." In early December 2005, for instance, the firm announced a plant closing in Morven, N.C.

The firm expects to remain a separate corporate entity to keep its brand names and licenses. "We certainly will be looking to capitalize on that very important asset and that's the name Dan River," says Barnhardt. "If the name Dan River all of a sudden went away, then you lose that continuity and you lose that establishment you have in the marketplace. We want to preserve that and use it as a springboard to offer a wider range of products."

North Carolina State University economist Michael Walden predicts that the decline in textiles jobs will continue. Those firms remaining in the United States will likely concentrate on niche production of "specialized textile outputs, where proximity to the U.S. market is important," Walden says.

The news of further textile consolidation comes on the heels of Vaughan Furniture Co.'s recent announcement to close one of its two factories in Galax, Va., about 100 miles west of Danville. The closing is due to cheaper Chinese imports, according to company officials, and will result in about 200 job losses. — Betty Joyce Nash