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# The Real Deal:

# Drivers and Measures of Incentives

Prepared for Missouri Economic Development Financing Association

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# When Are Incentives Appropriate?

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## Incentives Are Appropriate When

- External Test – There is a financing gap when competing with another jurisdiction.
- Internal Test – The project does not meet the internal Cost of Capital hurdle rate.
- Anchor Value – Incentives require maintaining job and capital investment in your jurisdiction.
- Relationship Value – Even a small offer of incentives opens the door to greater things.

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# What About Retention Incentives

- A job retained is as valuable as a new job.
- Examine the circumstances to determine if retention incentives are appropriate.
- Missouri Works Retention Incentives.
- Wisconsin and New Jersey Examples.

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# Leverage Federal and Private Incentives

- Federal New Market Credits, Federal Location Based Jobs Credits, Energy Credits, etc.
- Federal Location Based Incentives such as Renewal Community Credits and Empowerment Zones.
- Utility Incentives such as those provided by KCP&L.
- Private Foundations.

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# **What to Expect in Putting Together a Finance Deal**

# Incentive Process from a Consultant's Perspective

## 1. Preliminary Analysis

- Research existing programs and identify opportunities for new, custom programs
- Prepare incentive analysis and value proposition
- Conduct economic impact study, if necessary

## 2. Strategy Development & Negotiation

- Develop negotiating strategy and initiate discussions with officials
- Advise on potential legislative changes to existing programs / assist in crafting legislation for new programs
- Negotiate commitments with state and local officials
- Consider whether project lends itself to “Phasing”

## 3. Implementation

- Prepare and file applications
- Review terms of agreements
- Prepare a guide for client's team and document all compliance requirements

## 4. Ongoing Compliance & Tax Planning

- Prepare and file compliance documentation on deadline
- Implement strategies to mitigate the tax impact of benefits
- Review opportunities to re-negotiate agreement terms if project parameters change

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# What the Company Expects From Economic Dev

- **To be Valued:** 1) Know the multiplier, 2) Know how much tax revenue the Company generates, 3) Know the Company's charities.
- **Knowledge of the Business Climate and local Economics:** The Company needs quick access to the local economics. The Project has a time deadline and must keep moving.
- **Knowledge of the Political Environment:** The Company needs help securing cooperation and support from public officials.
- **Help Navigating the Press:** Negative press events are taken personally by Company executives and are difficult/impossible to overcome.
- **Service After the Sale:** Don't assume things are going well. Stay in contact to help with permitting, hiring, incentive compliance ext.



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# What the Company Expects In Terms of Incentives

- **A Number:** 1) A Present Value, 2) A Percent of Capital Spend, 3) An Amount Per Job.
- **Shorter Terms:** The Company has trouble seeing past the 5<sup>th</sup> year.
- **Competent Compliance Staffs:** Florida and Louisiana have struggle in this area.
- **Alignment Company Objectives:** phased approach to cash savings & tax credits
- **The Company Expects to Receive the Promised Incentives**

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# Reasons Why Incentives Are Not Realized

- The Company Fails to Performance.
- Claw backs/performance goals are too tight.
- Deadlines are missed: Reports are not filed
- Assignment of Contracts is not considered
- Attrition/Change in Staff - Hand-off is fumbled

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# **How Incentives are Measured by the Public and Private Sectors**

# Types of Incentives Available (Often they are invisible)

## Capital Investment

- Real and Personal Property Tax Exemptions
  - The most commonly available economic development incentive in the U.S. is the property tax exemption, which typically is granted for multiple years.
- Investment and Research & Development Tax Credits
  - Investment Tax credits at the state level subsidize the purchase of eligible buildings and equipment. R&D credits support research.
- Project Grants
  - Investment project grants may take the form of cash subsidies or tax credits.
- Land, Infrastructure and Real Property Grants
  - Grants of land and other property provide significant subsidies, while vital infrastructure may be provided without cost to your company.

## Location-Specific Benefits

- Discretionary Government Assistance
  - State and local government officials have discretion over tax and grant programs designed to stimulate the local economy. Such programs may be tapped to provide millions of dollars in annually recurring savings.
- Federal Empowerment Zones
  - Empowerment zone benefits are available to new and existing businesses in the form of income tax credits and tax exempt financing in specific geographic areas.
- State Enterprise Zones
  - Enterprise zones at the state level may offer income tax credits, property tax abatements, sales and use tax exemptions and other assistance based on the location of the business and/or residence of new hires.
- Foreign Trade Zones
  - FTZs designated by the federal government offer excellent incentive opportunities for companies doing business across international borders.

## Operational Financing

- Reduced Cost Financing
  - Interest subsidies and tax-exempt financing are available in some states. Occasionally, loaned amounts are forgiven as companies meet job retention commitments.
- Tax Increment Financing
  - Tax increment financing is used in many states to abate real and personal property taxes and reduce project financing costs. Government-issued bond proceeds may be used to reduce project costs in a variety of ways.
- Utility Discounts
  - “Economic development” projects may receive favorable rates for electricity and telecom services.
- Sales & Use Tax Exemptions
  - Government agencies may assign their tax-exempt status to project purchases, thereby eliminating the sales and use taxes.
- Relocation Cost Subsidies
  - State-level programs may be available to pay a portion of the cost of moving operations into and within a state.

## People

- Wage Subsidies
  - An increasing number of states offer cash grants or tax credits to subsidize wages as an inducement to new and existing business to create or retain jobs. The best-known of such programs include the North Carolina JDIG, the Kentucky job assessment fee, the Michigan MEGA, the Indiana EDGE and the New Jersey BEIP.
- Hiring From Targeted Populations
  - Some states and the federal government offer tax credits for hiring individuals from certain disadvantaged groups or neighborhoods.
- Recruitment Assistance
  - Grants may be available to offset recruiting costs, which can be substantial, especially in an expansion situation.
- Training Assistance
  - State tax credits and cash grants are increasingly available to offset a portion of anticipated training, both on-the-job and classroom.

# Sample Opportunity Assessment

Sample				
Business Incentives Opportunity Assessment				
	Benefit	Description	Eligibility	Estimated NPV of Incentives
I. State of Indiana				
Economic Development for a Growing Economy ("EDGE") Tax Credit	Corporate Income Tax	The Economic Development for a Growing Economy (EDGE) is a refundable tax credit program that rewards companies creating jobs and contributing to the growth of Indiana's economy. EDGE credits are calculated as a percentage of payroll tax withholding for net new Indiana jobs. EDGE credits may be awarded for a period of up to 10 years.	The Company must receive approval and enter into an agreement with the Indiana Economic Development Corporation. In addition, the Company must commit to the location and operation of the Project in Indiana for at least two (2) years after the last year in which an EDGE tax credit is claimed.	\$175,000
Hoosier Business Investment Tax Credit	Corporate Income Tax	Credit provides incentives to businesses to support job creation and capital investment. The non-refundable corporate income tax credits are up to 10% of the qualified investment and may be carried forward up to nine years. "Qualified capital investment" means the amount of the taxpayer's expenditures in Indiana for: (1) the purchase of new telecommunications, production, manufacturing, fabrication, assembly, extraction, mining, processing, refining, finishing, distribution, transportation, or logistical distribution equipment; (2) the purchase of new computers and related equipment; (3) costs associated with modernization (4) onsite infrastructure improvements; (5) the construction of new facilities; (6) costs associated with retooling existing machinery and equipment; (7) costs associated with the construction of special purpose buildings and	The Company must demonstrate that the project would benefit Indiana by increasing opportunities for employment and strengthening the economy of Indiana. Receipt of the tax credit would result in an overall positive fiscal impact to the state. The average wage per employee that would be paid by the tax payer to its employees (excluding highly-compensated employees) at the location after the credit is given would be at least equal to 150% of the hourly minimum wage (\$7.25) or its equivalent. The Company must maintain operations at the project location for at least 10 years during the term that the tax credit is available.	\$315,000

# Sample Opportunity Assessment

Skills Enhancement Fund	Training Grant	This employee training program provides partial reimbursement for a wide variety of training costs. The training grant is typically for a two-year period and is limited to a maximum of 50% of the Company's eligible training costs.	Most types of training are eligible except safety, HR/benefits orientation, and training required by law. Training expenses eligible for reimbursement include instruction, travel, and material and supply costs. Travel costs are limited to lodging and transportation expenses only (no food) and cannot exceed 30% of the total grant. Trainee wages are not an eligible training expense, although the wages paid to a staff trainer/instructor can be an eligible expense.	\$11,000
Land Discount	Land Credit	Reduction to the per acre price on county owned land based upon investment, employment level, and wages.	Locality imposes discount based on number on investment, employment level, and wages.	TBD
Property Tax Abatement	Property Tax Abatement	Local communities may offer real and personal property tax abatement as an incentive to new and expanding businesses. Property tax abatement allows a property owner to phase in payment of property taxes over a designated period. This period may be between one and ten years.	The locality may impose job creation and/or capital investment requirements. Warrick County offers the abatement up to 10 years.	\$220,000
TOTAL NET PRESENT VALUE OF INCENTIVES @ 8%				\$721,000

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# Private Sector Incentive Measurement Challenges

- GAAP accounting complicates revenue recognition and can produce “incentive losses” in the initial years.
- Tax incentives that are “below the line” are often not valued by operational executives.
- Company executives don’t manage and control incentives well because they are easily identifiable in the financial statements.
- Companies do not want to recognize contingent liabilities from claw backs. Kick the can.

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# Suggestions

- Require yearly incentive check-ups with the Company.
- Provide periodic cash basis benefit statement to Company executives summarizing incentives realized.
- Coordinate the transition from the economic development team to the less friendly Incentives compliance team.
- Projects are not complete until all incentives are actually realized by the company.

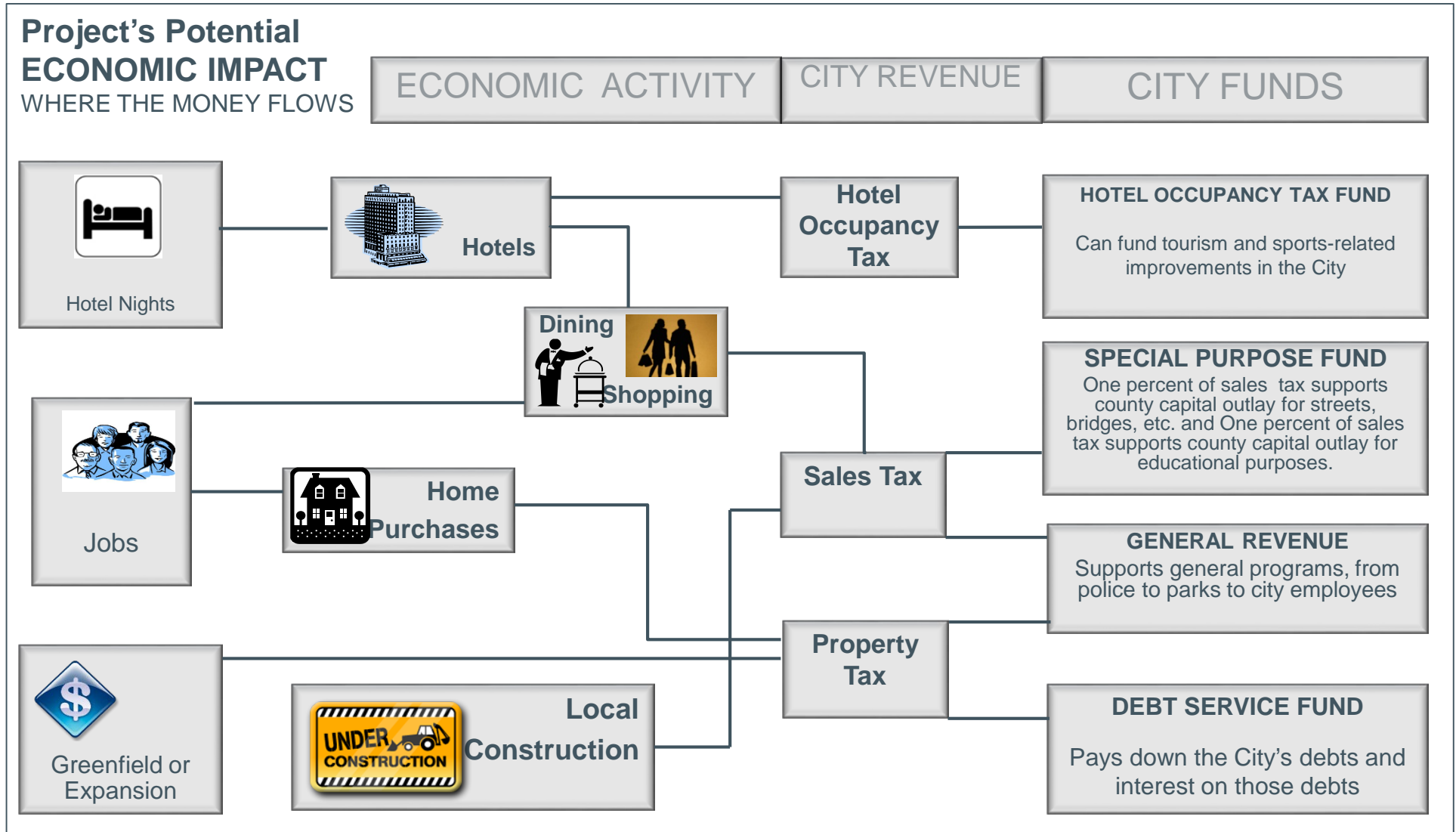


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# Economic Impact Study

Economic impact studies are used to measure the economic and fiscal impacts of new or modified economic activity in a particular geographic area. These studies can be used to assist state and local governments in determining which infrastructure investments and incentives will have positive impacts in their jurisdictions.

# Sample Economic Impact



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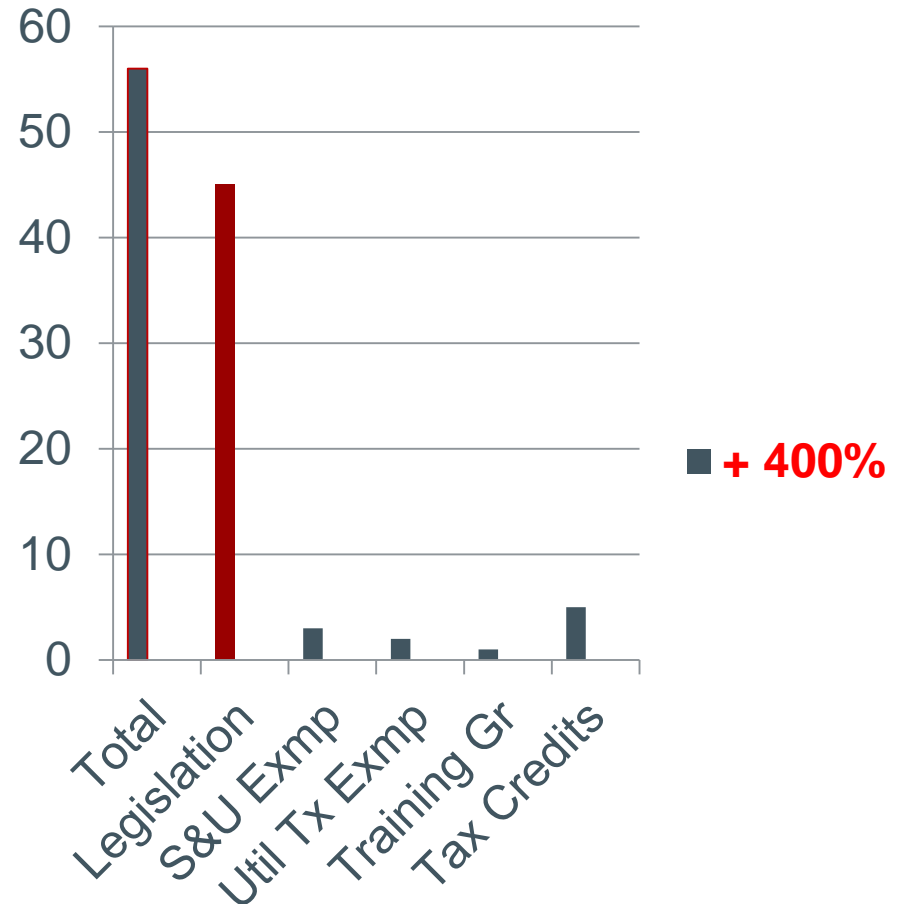
# **Innovations in Economic Development**

# Advocating for Incentive Legislation

For significant investment and job creation/retention, explore potential legislative action to add value to an incentive package by restructuring or developing customized provisions within existing State incentive laws.

During a prior project, we developed new legislation, which supported a major corporate headquarters relocation. The legislation included customized incentives for the particular relocation, which would not have been available through existing incentive laws.

The chart to the right itemizes the incentive package and the additional value, highlighted in red, that the legislation provided.

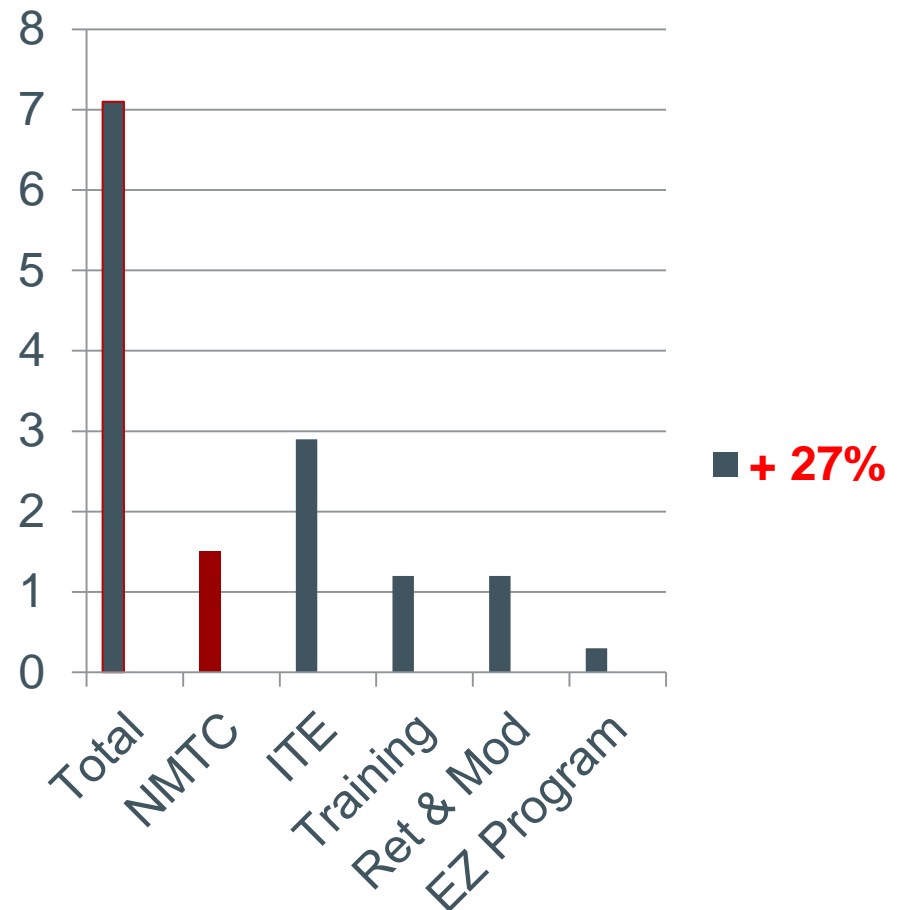


# Adding Federal incentives

For sites located within eligible census tracts, explore using a holistic approach to add value to the incentives package by tapping low-interest loans or equity through New Market Tax Credit financing structures.

During a prior project we accessed Federal New Market Tax Credits, and routed our client's investments through a Community Development Entity (CDE). By doing so, we were able to increase the value of the client's incentives package by 27%.

The chart to the right itemizes the incentive package and the additional value, highlighted in red, that these tax credits provided.

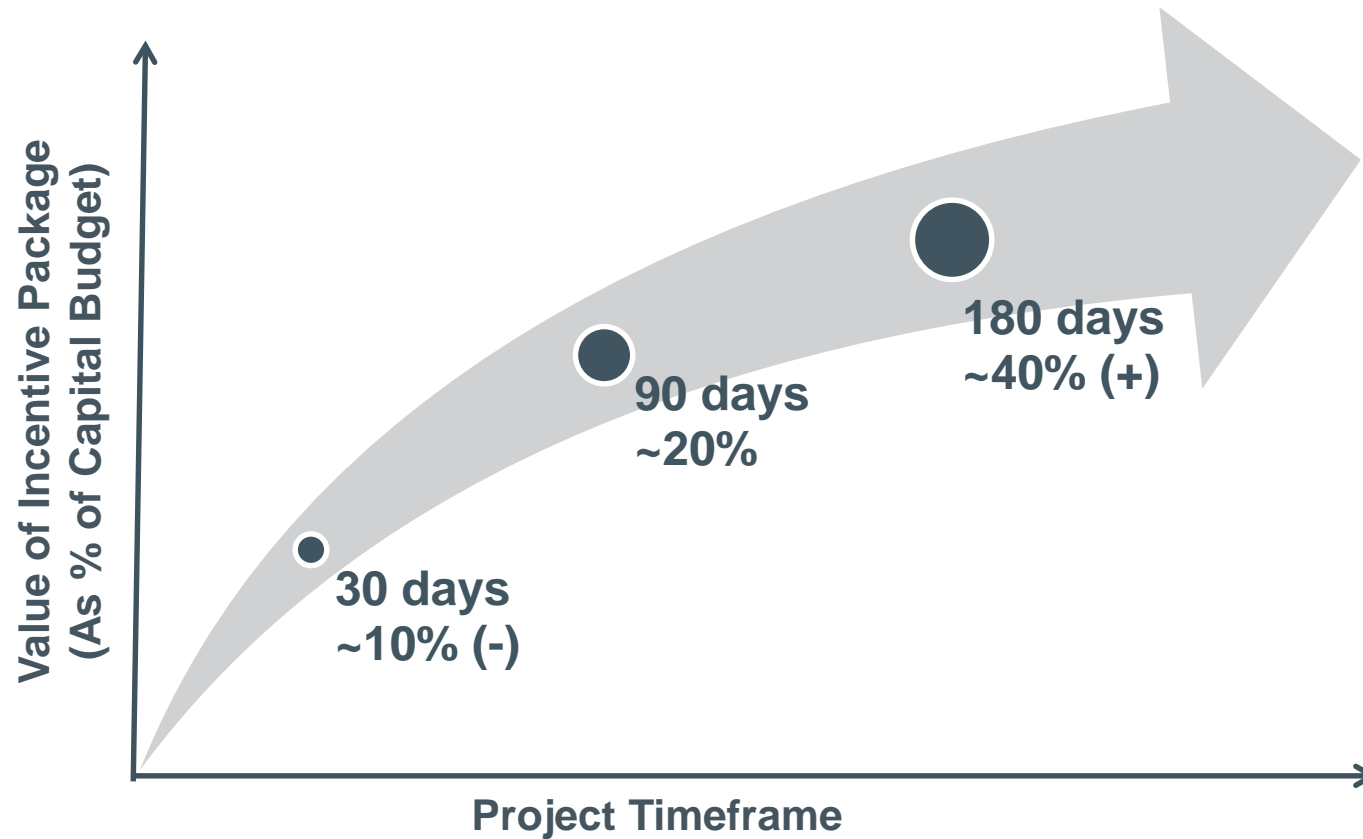


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# Other Innovations

- States and local jurisdictions with limited incentives using phased approaches.
- Leveraging retained incentives to increase offers for new projects and expansions.
- Innovative use of training incentives:
  - Match making
  - Co-development efforts
  - Supplier relationships

# Time and leverage drive value



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Thank You

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Advice You  
Value