



GOVERNMENT INCENTIVES FOR NORTH AMERICA

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As more European corporations look at the vast North American market, the competition for these corporate manufacturing, distribution, research and regional headquarters facilities has increased. Canada, the United States and Mexico are all vying to attract new companies to their respective country. Many state, provincial and local governmental bodies in Canada, Mexico and the U.S. have developed incentive programs into a highly competitive method for luring and keeping existing corporations. Incentives are not limited to the much publicized giant auto assembly plants. For example, Pollina Corporate represented a major foreign corporation with a smaller project involving a manufacturing facility with only 80 initial employees. The company was offered a full range of incentives by a number of U.S. states including payment of all employee salaries during an on-the-job-training program lasting 8 weeks; an 80% abatement of personal property taxes for a period of 10 years, which amounted to over \$800,000 per year; a decrease in real estate property taxes of over \$100,000 per year; and low-interest forgivable loans of over \$10,000,000 for building improvements. Forgiveness of the loan was based on employment growth (e.g., for each employee added over the initial 80, a significant amount of the loan was forgiven).

There is no simple formula for picking the right country, much less the best location within a particular country. Every company's requirements are different and while, for example, low cost Mexican labor may sound attractive, it must be weighed against other potential disadvantages of a Mexican location that may outweigh the labor cost advantage. The weakness of the North American economy today has caused all three countries and their local governments to intensify their efforts to attract new jobs and investment and they all view European companies as a major source for future growth.

Mexico

Assembly plants in Mexican cities along the U.S. border (maquiladora industries) are beginning to show more promise for companies in search of lower cost operations. The maquiladora industries are able to take advantage of the lower wage rate of Mexico for relatively low-skilled assembly operations. The Mexican maquiladora industry has had its difficulties in recent years due to the North American economic downturn. According to *BusinessMexico*, 237 maquiladoras closed in 2001 in Baja, California. In the Monterrey region manufacturing vacancies went from 4.5% in 2000 to 8.9 percent in 2002 and will likely rise further by year end 2003. Unemployment in the major maquiladora markets of Tijuana, Mexicali, Nogales, Monterrey and Juarez has been rising. In the recent past manufacturers struggled with high turnover, find that with rising unemployment, this problem has eased somewhat.

Mexican officials are becoming more aggressive in seeking employers with new offers of tax breaks, reduced real estate costs and new recruitment efforts. Federal and state incentives for investment can include up to \$500 for each new job created for training and developing facilities. Some states offer extra incentives for specialized industries as does the Yucatan for aerospace, agribusiness, medical, furniture, textile/apparel and information technology. A special "Sectoral Promotion Program," has been announced by the Mexican government to offset the imposition of tariffs on raw materials from non-NAFTA countries.

While most manufacturers have historically clustered in border cities, there is growing interest in interior Mexican locations. Interior locations, such as Tlaxcala and Queretaro provide lower-cost, less transient labor and a more centralized location to serve growing Latin American markets. Care must be taken in site selection, as the availability, quality, and delivery of utilities and infrastructure can vary considerably throughout the country.

Canada

The Canadian government has helped to encourage corporate success through a new regime of lower taxes, skilled available labor and lower business costs. Canadians are fortunate to share with the U.S. the largest and most comprehensive trading relationship in the world. Facilitated by the North American Free Trade Agreement (NAFTA) signed by Canada, United States and Mexico, billions of dollars of products cross the borders of these countries every year.

An aggressive timetable for reducing federal and provincial corporate tax rates, which have been relatively high, will bring the average to a point that is more competitive with the U.S. rates. Even as tax rates have fallen, Canada has managed to maintain a balanced budget for the past five years. Canada's tax credit program for research and development has encouraged companies to tap into Canada's highly educated and highly competitively priced work force. The cost of Canadian technical and professional workers is about sixty-five percent of the cost of comparable U.S. workers. Nearly two-thirds of investment in R&D can be recovered through tax credits and other incentives. In general, for manufacturing, Canadian incentives do not compare to those offered in many U.S. states and communities. In manufacturing sectors, Canada, like the U.S., is characterized by a highly skilled work force.

Canada has a world class infrastructure located with the majority of its population along the border with the U.S. There are four major clusters of business in Canada with others emerging. The major clusters are financial services in Toronto, oil and gas in Ottawa, bio/pharma in Montreal, and auto in southwestern Ontario. Generally, the cost of doing business can be ten percent or lower than in comparable U.S. cities. Canada's favorable exchange rate with the U.S. and lower employee benefit costs, which is linked in large part to the national health care system along with NAFTA, have helped open the country to new investment from abroad.

United States

Many U.S. local and state governments have recently inaugurated new mayors and governors. With these changes, there are changes occurring in how these states and local governments can be ranked relative to being pro-business. Just as is true in Canada and Mexico, most state and local officials will speak highly of their pro-business attitude but not all are willing to back up the rhetoric with financial assistance.

There are dramatic differences between states and communities in the U.S. relative to incentives offered to employers. For example, on a recent project, negotiating with two Midwestern states on behalf of a manufacturer with 400 employees, one state offered \$22,500,000 in incentives and an adjacent state only offered \$2,800,000. While there can be substantial variations in what state and local governments will offer, there are also considerable geographic variations in labor as well as other costs including taxes, utilities and the cost of living in the U.S.

Frequently, many European companies opening new operations in the U.S. are drawn to major metropolitan areas which, depending on the company's requirements, can prove to have overall operating

costs 10%-20% higher than other, less urban locations, which still can provide excellent market accessibility and often better, lower-cost labor. When it comes to transportation and infrastructure including utility availability and reliability, the U.S. is excellent, with few areas having any shortcomings.

Statutory and Negotiated Incentives

There are basically two categories of incentives offered in North America. First are the statutory incentives, which are those pre-approved by state, provincial and local governmental bodies and made available to all eligible companies who request them. The second category is negotiated incentives, which are limited solely by the needs and imagination of the relocating corporation, its negotiators and the ability of political leaders to accept and approve them. Granting of incentives is not limited to governments. Many utility companies also can offer significant incentives, such as reduced rates, low cost or free equipment (e.g., energy efficient light fixtures, backup generators), dual sources of power, free technical assistance in evaluating utility capability for existing facilities and for designing the utility requirements of new facilities.

Generally, incentives can be categorized as follows: (1) tax related - e.g., personal property tax abatement, corporate tax reductions, real estate tax reductions, payroll tax reductions; (2) employment related - e.g., pre-employment screening, subsidized job training, employee relocation assistance; (3) financial incentives - e.g., free or low cost property (land and buildings), waiving of development fees, publicly financed infrastructure, low interest or forgivable loans, cash grants; and (4) fast tracking - e.g., streamlining of the construction and environmental permitting process.

Funds may be available in many areas to pay part of qualified new or existing employees' wages during specified training periods or to reimburse the company for the cost of conducting in-house training. Other incentives include matching jobs with potential candidates, screening and interviewing preliminary applicants on behalf of the company, and making recommendations of qualified candidates. Free-site, free-building or other direct subsidies to persuade a business to relocate into a community are not uncommon. The most effective incentives are those that address the specific needs of the corporation and can even include cash grants to help pay for relocation costs.

The details of any incentives offered are essential to understand the specific use to which the incentive can apply. Formulas for calculating the incentives and restrictions on them can make an incentive that sounds very attractive of little or no value to the corporation. Program applications, or fine print on criteria for eligibility, can be so overwhelming that companies give up in frustration or find that they do not qualify for

programs. Once a company announces its intent to relocate to a specific community, the eagerness and “willingness to be flexible” on the part of state or local government can wane rapidly. Before committing to a specific location, all details of programs offered (particularly statutory incentives) must be examined in detail. Prior to committing to a location, a company can often negotiate the details of a program offering to make it more palatable to the company. The best incentives are typically those that are negotiated to meet a company’s specific needs. Because they are custom-designed for the company, policies and procedures for their use are negotiated with the company’s needs in mind.

Corporations often find it difficult negotiating in a political arena. It is very unlike the negotiations that take place between companies where executives can make decisions, give written commitments and will stand behind their individual decision. In a political arena, public officials often will make verbal commitments but when asked to put them in writing, are reluctant to do so and if they do so, will make the commitments contingent on city council or legislative approval. This process often becomes very frustrating for business leaders if they do not have the assistance of an experienced incentive negotiator.

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