



Incentives From the Corporate Perspective

Community relations play an important role in the site selection process. Successful negotiations benefit both the company and the community.

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LIKE ALL RELATIONSHIPS, the most successful company-community relationships are those where both parties benefit from each other. Very often this mutual benefit boils down to economics. While financial considerations are a primary factor, companies should seek to do business in a community that carries a similar set of values and possesses a pro-business attitude. When forging a new relationship, it is advantageous to start off on the right foot. In the company-community context, the site selection and incentive negotiation process is often the first step. This article is written from the corporation's perspective, and examines a few of the many issues to consider when negotiating with state and local governments and economic development organizations.

Community Relations Aggressive, pro-business communities usually have a strong sense of economic development from top to bottom. Strong pro-business governors or mayors are often the driving force behind the economic development agenda. Team up savvy political leadership with strong state and local economic development organizations and you have a winning combination. While it is difficult to find a governor or mayor who will not claim to be pro-business, not all are willing to dedicate the time, effort, manpower, and funds to be truly competitive in the economic development marketplace.

Aggressive states, communities, and economic development organizations stay competitive by accumulating the necessary political and economic capital to bid on projects. In addition to funding, the ability to accommodate their corporate prospects by being creative and flexible with their programs is essential to success. The needs of every corporate prospect are different, and economic development programs should be designed to accommodate those differences. For example, a company with a warehouse filled with high-cost electronic parts may value inventory tax abatement more than a firm with low-cost plastic bottles.

The Good Corporate Citizen Dilemma: A Case Study

Very often, companies will consider expanding in a community where they have an existing facility. In these situations, persuading the local community to put its best foot forward is not always an easy task.

Most communities claim to be dedicated to retaining their corporate citizens. They will ask to be partners in your company's future growth, willing to do whatever it takes to be your location of choice for years to come. The fact is that most communities and many states, in spite of the rhetoric, tend to take existing business for granted. Consider the following case study:

ABC Corp., located in the North, has been operating in the same town for 45 years and is the largest employer in the county. ABC must expand its operations by adding a new plant and creating 350 new jobs. ABC could consider expanding locally, or could locate its new plant in the South, where labor rates and proximity to customers would allow ABC to reduce its operating expenses. ABC approaches local officials about the possibility of local expansion and is met with a lackluster response. Local officials insist that they want ABC to grow in their area, but cannot afford to offer much in the way of assistance. ABC executives are pressured by local and state officials to make the commitment to expand locally without ruffling feathers within the community. To help make their decision easier, local officials offer \$500,000 in property tax abatement over five years. Concurrently, the same community, in conjunction with the state, offered a \$14 million incentive package to XYZ Co., an out-of-state business. XYZ Co. planned to invest \$2 million less than ABC Corp. and employs about 270 people. XYZ Co. accepted an offer from a different community.

ABC Corp. chose to locate the new plant to the South with the help of a \$22 million incentive package. The deal also included room to expand on the new site. Three years later, ABC Corp. relocated the rest of the operation to its location in the South.

Pollina Corporate Real Estate, Inc. initially represented XYZ Co. in its relocation and incentive negotiations, and was subsequently engaged by ABC Corp. The real names and exact locations of the two companies have been intentionally omitted.

Despite the fact that many of today's economic development professionals have put a premium on retention

projects, the situation described above is not uncommon. Very often, the only way to gain the attention of state and local officials is to force their community into a competitive situation. By opening up the project to other locations, companies are provided options that can be substantially more cost-effective.

Statutory Incentive Programs

There are two classes of incentives that a company may receive: statutory incentives and negotiated incentives. As the name suggests, statutory incentives are legislated programs. Common examples of statutory incentives include job-training grants, state income tax credits, sales tax exemptions on the purchase of machinery and equipment, and inventory tax exemptions.

A company will receive the benefit of a statutory incentive if the project meets all the requirements set forth by the enacting body, typically the state legislature.

Some statutory programs are easier to qualify for than others. Some programs have very general requirements, making it easy for companies to find out if they qualify. For example, there are programs where the only requirement is that a company be engaged in a certain industry (e.g., manufacturing, telecommunications, R&D). For these and other similar programs, the application process can be relatively straightforward. If a company fits the targeted profile, the company should receive the incentive without much difficulty.

Many other legislated programs are very complex. These programs (which tend to offer the greatest benefits) may have dozens of requirements that a prospective company must meet. Complex programs are typically administered by a board. The board is responsible for reviewing the applications and approving or rejecting the project. Applications for complex programs can be lengthy and difficult to complete. Since the state is usually making a significant financial commitment, they often require detailed financial information on the company going back as far as five years. Some legislation requires that the board hold a public meeting to discuss the application before approval can be granted. No-growth advocates, or other opponents of business incentives, may attend these meetings. The more complex incentive programs will allow for a range of incentives, the exact amount to be determined on a case-by-case basis. Such programs require a fair amount of negotiating, usually with the board that administers the incentive.

One type of statutory incentive that has received much attention is the Enterprise Zone or Renaissance Zone program. The concept is relatively simple: To promote growth in certain designated zones, state governments will offer more aggressive benefits to companies that locate within those zones. Zones can be as large as a few thousand acres, or as small as one city block. Many of the zones are drawn around pockets of economically depressed areas where unemployment rates are high, and new business growth is highly sought.

While these areas often receive priority for zone designation, they are not the only ones to receive Enterprise Zone or Renaissance Zone status. Some such zones are located in more attractive communities with relatively stable economies. While each zone program is unique, many offer exemptions from some or all state and local taxes. Others offer large job tax credits that may be refundable as cash. Most zones last for a finite period, usually no more than 20 years.

Negotiated Incentives

The second major class of incentives is what many refer to as “negotiated incentives.” Negotiated incentives are not legislated, and therefore provide a company with more flexibility in tailoring incentives to meet their unique needs. Negotiated incentives are often very valuable to a company because they can substantially decrease the amount of capital investment required in the first year of a project.

Negotiated incentives come in many forms. They can be provided directly to the company, or indirectly channeled through local entities to the company’s benefit. Examples of direct negotiated incentives include cash grants, free land, low interest or forgivable loans, relocation assistance, temporary office space, utility rate reductions, and waiver of building permits or utility tap-on fees. Indirect negotiated incentives are often infrastructure related, including water and sewer extensions, road widenings or improvements, and construction of stoplights and turn lanes. Indirect incentives can also be off-site, such as adding water towers or utility substations.

The only way to receive negotiated incentives is to ask for them. Politicians and economic development professionals will never knock on your office door and offer you a sizeable cash grant. The process for negotiating these types of non-legislated incentives can be complicated. A strong negotiator must possess real estate and development experience, understand the political process and the motivations of the politicians involved, and be objective and independent.

Negotiated incentives are best achieved through an independent third party agent. An experienced agent will most often act as a buffer between the company and the communities involved. The agent can eliminate many obstacles (including the “good corporate citizen dilemma” discussed above), and deflect any negative attention away from the company.

What's To Be Expected

Obviously, the type of communities under consideration will greatly affect the amount of incentives a company might expect to receive. The primary factor here will be whether or not the communities selected are aggressive relative to business growth. Even if a company has selected two or three aggressive communities, success in landing a solid incentive package is not guaranteed. Timing can play a big role. If an aggressive community has just landed a big project, it is possible that they may not have the funds (especially negotiated incentives) to dedicate to your project.

The local political climate can also greatly affect the course of the negotiations. Governors facing re-election have been known to set aside funds to attract big projects at times when voters are paying special attention. Public figures who understand the impact that job creation can have on a local economy (and the well-being of their constituents) will certainly tend to be more pro-business. The only way to identify the type and amount of assistance that is available is to initiate the site selection process and commence negotiations.

During negotiations, be sure to guard against relying on verbal or qualified offers from local and even state politicians. Until a state or local offer has been memorialized in writing, it cannot be relied upon. The goal of both state and local politicians is to elicit a public commitment on the part of the company. Politicians know that corporate executives will rarely change their minds after making a public announcement. If the state or local government does put their offer in writing, check to see if the offer is subject to final approval by the city council, legislature, or economic development board. If it is, the offer is a de facto proposal. Insist that all necessary parties approve all incentives before any commitment or public announcement is made.

A Win-Win Situation

In the end, a well-negotiated state and local incentive package is a win-win for the company and the community involved. The community benefits from an infusion of investment in the local economy and the multiplier effect that comes with additional job opportunities. Long-term, incentives help the community reach its goals of establishing and maintaining a stable economic base. For the company, state and local incentives significantly lessen the short-term economic burden associated with an expansion or relocation. In the long run, incentives help companies remain competitive in the marketplace.

How Much Assistance Can We Expect?

Unfortunately, there is no matrix that can accurately determine the amount of assistance that state and local officials will offer. In most cases, incentive offers are based on the following criteria:

- The number of jobs being created
- The type of jobs
- The average wages and benefits
- The amount of investment
- The company's reputation and financial health

The more these factors weigh in the company's favor, the more aggressive a truly pro-business community can become.