



## **Incentives for Technology: a Changing LANDSCAPE**

Many southern states have recognized the value in providing incentives to start-up ventures as well as billion-dollar organizations.

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**TODAY'S GLOBAL ECONOMY** has changed the landscape in which states and communities compete for direct corporate investment. Emerging global markets in Eastern Europe and Asia have increased productivity to levels that were once only found in the developed Western nations. These lower-wage alternative locations are now on the radar screen of nearly every cost-conscious executive. Moreover, these emerging markets are competing not only for blue-collar manufacturing jobs; they are strongly competing for the highly skilled, higher-paying technology-based jobs.

Business savvy governors and economic developers realize that the cost-of-doing-business advantages (land, labor, taxes, utilities) often found in the South are only relative advantages. That is, the South may have cost-related advantages over some other states, but not necessarily over other international growth centers that now compete for direct corporate investment. In an effort to remain a healthy region of growth for technology, many Southern states have fashioned incentive programs to attract and retain employers in such high-demand industries as biotechnology, pharmaceuticals, information technology, electronics, and software.

### **The South Means Business**

A strong case can be made that certain states in the South are more aggressive than many other states in the nation when it comes to incentives for technology development. While the types of incentives may vary from state to state, and community to community, several Southern states have put together an impressive track record of creating jobs through incentives.

For any technology-related business, obtaining the maximum amount of incentives for a given project requires that negotiations be finalized early on in the process, before a final location has been announced. There are several reasons why companies benefit from a competitive situation.

First, in the case of statutory programs, many state economic development agencies require that companies produce a bona fide competing offer during negotiations. In most cases, legislation for the more lucrative statutory programs dictates that the state cannot grant the incentives unless companies have out-of-state alternatives. Such language is often referred to as a "but for" clause. In cases where competition is not legislatively required, producing an offer from a competing state may, de facto, be the only way to receive approval from all necessary parties.

Second, competition can often create the leverage necessary to successfully receive negotiated or nonstatutory incentives. By negotiating early on in the site selection process, companies are in a better position to seek creative assistance that may come in the form of free land, cash grants, fast-track permitting, infrastructure improvements, and other enticements. Southern states looking to diversify their economies with high-paying technology jobs may consider special industry-specific incentives to attract direct corporate investment. Consider the following case study:

International Sematech, a global consortium of semiconductor manufacturers, conducts R&D in a noncompetitive format to further the growth of the semiconductor industry. Although Sematech is based in Austin, Texas, the group also operates a new state-of-the-art R&D facility in Albany, N.Y. Sematech recently evaluated locations in Texas and New York for its new Advanced Materials Research Center. Both states were anxious to attract the sizable investment. In an effort to encourage future technology growth in the state of Texas, Governor Rick Perry called for the creation of the Texas Enterprise Fund for economic development.

In support of its governor, the Texas legislature approved \$295 million for the Texas Enterprise Fund. One of the funds stated purposes is to provide Sematech with an estimated \$40 million to assist with the construction of a new facility. The fund also includes an estimated \$55 million to both attract technology business and support university research. Additionally, the fund established a "deal closing fund" to be used to attract major projects such as the Toyota expansion recently announced in the San Antonio area. Perry has further expressed his commitment to provide Sematech a total of \$200 million over a period of five years, all for the benefit of the new research center. In response to the actions by the state of Texas, Sematech spokeswoman Anne Englander was quoted as saying, "My belief is that there won't be any more talk of relocating anywhere else" (Dow Jones).

Although the Sematech case is a large, high-profile project, it serves as a powerful example of the impact that incentives can have on corporate decision-making. More importantly, it demonstrates the willingness on the part of states such as Texas to aggressively lure high-paying technology jobs when faced with a competitive situation.

### **Growth for the Future**

Incentives are not for big players exclusively. Many states have recognized the need to foster growth within their borders by providing incentives to start-up firms. Many such programs form links between new businesses, academia, and venture capital. Others provide seed funding to qualifying firms to help make up for the lack of private funds.

One of the foremost ways of accomplishing this goal is to provide public funds that can be channeled through colleges and universities to the benefit of local start-ups. For example, the state of Arkansas has several programs specifically designed to create technology development in the state. The Arkansas Science and Technology Authority (ASTA) has an investment fund that provides start-up capital for technology-based companies. ASTA also provides funding for Arkansas colleges and universities. To further encourage the transfer of ideas from labs to manufacturing, Arkansas industries may qualify to receive an income tax credit based on research and development expenditures in the state.

One of ASTA's goals is to promote the transfer of technology from academic laboratories to manufacturing plants. In the technology sector, the costs of bringing a new product to market are so high that partnerships with universities and other sources of funds become essential. Such collaboration has been the cornerstone of success for technology centers such as Austin, Texas, and North Carolina's Research Triangle.

Similarly, Tennessee has created the Venture Alliance Capital Fund (VACF), a

\$4 million fund making equity investments in new Tennessee Valley companies. The fund makes investments between \$100,000 and \$1 million and provides expert management skills to develop successful business and marketing plans. The program provides a bridge to the level where later-stage financing from private sources can be made available.

### **Direct Investment vs. Jobs**

Oklahoma's Investment/New Jobs Tax Credit offers technology companies more flexibility in the way incentives can be utilized. The program is available to qualified companies involved in areas such as high-tech manufacturing, R&D, and computer services. Companies that qualify are given the choice of electing to take the income tax credit based on the addition of new full-time employees (\$500 per new employee), or the increased investment in depreciable property (1 percent of the qualifying investment) resulting from the project. Credit amounts accumulate in the first five years of the project (cumulative benefits may equal \$2,500 per new employee or 5 percent of the investment). The credit doubles for most investments over \$40 million, or for projects locating in one of Oklahoma's state enterprise zones (cumulative benefits may equal \$5,000 per new employee or 10 percent of the investment). Unused credits may be carried forward for 15 years. Employee levels may fluctuate if the credit is taken based on investment. Job losses must not be attributable to the new investment.

Programs predicated on direct investment, rather than new jobs, are becoming more and more valuable to companies. This shift in the corporate landscape needs to be addressed by policymakers at the federal, state, and local levels. This is not to say that job creation should not be a major factor in awarding incentives. Job creation is, and always will be, a fundamental force behind incentives. With that in mind, it is important to consider changes in the international marketplace, and how incentive programs can be structured to better meet the needs of corporate users.

Manufacturing, especially high-tech manufacturing, is under extreme pressure to cut labor costs, which can be as much as 75 percent of operating costs. Corporate America's answer to this problem so far has been to locate new operations in low-wage markets overseas. The natural byproduct of this pressure is that an increasing amount of direct corporate investment is being made outside the United States.

One of the few ways companies have been able to maintain their U.S. addresses is through increased automation. By decreasing headcount and increasing the level of machine-based production, some U.S. manufacturers have been able to remain profitable in the face of stiff competition from imports. In support of these efforts, states need to put more emphasis on direct investment as a driving force for awarding incentives. When doing so, policymakers must not penalize firms for job reductions resulting from increases in automation. This is especially critical for technology-dependent industries. Technology, coupled with the knowledge-based solutions that are born in our universities and laboratories, is a major driving force behind much of the growth to be anticipated for the U.S. economy in the twenty-first century.

Many scholars agree that the U.S. has already lost its advantage in the area of low-skill manufacturing and assembly. We cannot afford to let technology and

research follow suit. Direct investment in the form of machinery and equipment, be it for manufacturing or research and development, still has a positive impact on the local economy. Incentive strategies should aim to encourage direct investment to the same extent as job creation. Programs need to be crafted that will deliver cash equivalent benefits to companies that seek to make substantial direct investment in our communities. After all, incentives are of little value if they ultimately fail to induce a firm to locate in a given area.

### **More Programs**

Following are some examples of incentive programs offered in other Southern states:

**Alabama:** Site Preparation Grant Program authorizes the state to sell bonds and use the proceeds to make development grants to local entities. Grant funds may be used by local government to do site improvements for company facilities. Eligible companies must be in specific target industries, including computer software and R&D. Companies may own or lease the subject facility.

**Florida:** Qualified Target Industry Tax Refund provides refunds on taxes of \$3,000 per net new full-time job created in Florida. Among the eligible targeted industries are pharmaceutical manufacturers, computer and electronic manufacturers, information services, telecommunications, and research and development. The refund may be based on a variety of taxes paid by the approved business, including corporate income, sales, ad valorem, intangible personal property, insurance premium, and other selected taxes. By locating in one of Florida's enterprise zones, the amount of the refund may increase to \$6,000 per net new full-time job. To be eligible for approval, a company must be in a targeted industry, demonstrate the need for the refund (usually by considering an out-of-state location), and create at least 10 net new full-time jobs. Other requirements include paying at least 115 percent of the average annual state, MSA, or local wage.

**Georgia:** Job Tax Credit Program makes companies in select industries — including telecommunications, computer software, data processing, and R&D — eligible for income tax credits ranging in value from \$750–\$4,000 per job, depending on the tier ranking of the county where the project is located. Companies locating in least developed counties, or Tier 1 counties, may apply the tax credits against 100 percent of corporate income taxes, and any remainder against the employer's quarterly or monthly withholding taxes. Eligibility requirements vary according to county classification.

**Kentucky:** Kentucky Jobs Development Act credits are for new and expanding service and technology-related projects, including data processing and R&D. KJDA projects may receive a 100 percent credit against the state income tax arising from a project, and may collect a job assessment fee of up to 5 percent of the gross wages of each employee whose job is created by the project and who is subject to Kentucky income tax. Benefit amounts are capped at 50 percent of project start-up cost plus 50 percent of annual facility rental cost or rental value for up to 10 years.

**Louisiana:** Custom Computer Software Sales Tax Exemption makes custom computer software purchases exempt from sales tax. The exemption is being put into effect in four phases. Phase one, which went into effect on July 1, 2002,

excluded 25 percent of the sales price of custom computer software from the definition of tangible personal property. The exclusion is 50 percent in 2003 and will rise to 75 percent on July 1, 2004. Effective July 1, 2005, all custom computer software becomes nontaxable.

**Mississippi:** Research and Development Jobs Tax Credit provides a five-year tax credit of \$1,000 per year for each new R&D job created by new or expanding businesses, effective for years two through six after the creation of the job. There is no minimum number of R&D jobs required to be eligible for this credit. To qualify, a business must first meet Mississippi State Tax Commission regulations defining eligible R&D jobs. The credit is limited to 50 percent of the company's corporate income tax liability.

**North Carolina:** Credit for Technology Commercialization provides eligible companies with a credit (either 15 percent or 20 percent) for investing in machinery and equipment used in production directly related to technology that is developed by and licensed from a research university. The credit is a percentage of the eligible investment. Companies must invest a minimum of \$10 million in a given year.

**South Carolina:** Job Tax Credit Program is reserved for specific industries and users, including R&D and other technology-intensive companies. Companies that qualify for the program earn income tax credits valued between \$1,500 and \$8,000 for each new full-time job created in the first five years of the project. Credits earned can offset corporate income taxes in the following year, up to 50 percent of the company's total liability. Unused credits may be carried forward for 15 years.

**Virginia:** Technology Zones can be established by communities to encourage new technology business to develop. Presently, 13 localities have created zones throughout the state. Qualifying companies locating or expanding in a zone may receive permit or fee waivers, local tax incentives, zoning variances, and other benefits. Zones extend for a 10-year period.