Sweet land of subsidy

The downturn has forced states to be savvier and more careful about providing tax incentives to business

ON NOVEMBER 14th 2012, before an audience of elected officials and assorted local dignitaries, voestalpine Metal Forming, a division of an Austrian steel company, broke ground on a manufacturing facility in Bartow County, around 50 miles (80km) north-west of Atlanta. Voestalpine supplies parts to European carmakers, and hopes to expand further. Mercedes-Benz has its only American plant near Tuscaloosa, Alabama, while Volkswagen has one in Chattanooga, Tennessee, just over the Georgia border. Car-manufacturing factories dot the south-east, a region of low-tax states without strong unions and offering relatively cheap land. Voestalpine looked at many sites across the region, and finally narrowed the contenders down to three states.

Georgia boasts the world's busiest airport, America's fourth-busiest container port, several interstate highways and a well-respected workforce-training programme. To sweeten the deal, however, the state's economic development team gave voestalpine an array of tax credits and incentives: $3.3m in job-creation credits and $1.4m in port-tax credits over five years, $4m in sales-tax exemptions on machinery and equipment, $3m in local-tax abatements and a grant of $275,000 towards site developments—in all, over $14m in credits and cost exemptions.

If that seems steep, consider that Voestalpine will invest $62m in the facility, which is scheduled to open later this year. Not including the jobs and the economic activity generated during its construction, it will eventually employ 220 people directly and could generate hundreds more jobs for its suppliers and vendors. Those 220 jobs will pay employees an average annual salary between $30,000 and $40,000—right around the Bartow County average of $37,000 a year, and particularly welcome these days, when the county's unemployment rate stands at 9%, well above the national average of 7.6%. Much of that money will find its way back into the community as employees buy houses, food, cars and so forth—and as they spend they will pay sales and property taxes, which means more government revenue and so more money for social services.

If voestalpine fails to meet 80% or better of its promised investment and job-creation targets in five years, Georgia can claw back whatever portion of the $14m in credits and

grants has not been claimed or spent. Chris Cummiskey, who heads Georgia's Department of Economic Development, says that companies such as voestalpine "are putting far more into the community than they are taking out".

Not everyone agrees. Opposition to incentives is a rare issue that can unite progressives and "tea-party" types. Greg LeRoy, who heads an economic-development watchdog group called Good Jobs First, suggests that states would be better off making investments that benefit everyone, rather than showering big companies with dollars. He calls subsidies aimed at luring or, worse, retaining companies that say they are thinking of moving (see chart) "a race to the bottom" that "wastes a lot of money on a microscopic fraction of employees". Instead he suggests that governments should fund "training programmes, cluster training, investments in infrastructure or fibre-optic networks or [school] education. These are much safer investments…benefiting lots of different employers." Mr Cummiskey believes that given Georgia's infrastructure, even with no incentives, "We'd pick up most of the business in the south-east."

That is easy to say from a comfortable perch in a big, rich city such as Atlanta. But incentives can give scrappier, hungrier places a way to compete for business. They keep dominant cities from getting too comfortable. They help businesses keep costs down and hedge their expansion risks. The cash crunch that followed the downturn led some states to spend more on economic development in order to lure businesses. It has led others to save precious funds by tightening economic-development budgets. Putting even a rough dollar figure on the number of incentives offered is difficult, but all states and many cities and counties have them, and they have become an accepted and largely beneficial aspect of competition.

They take a variety of forms: credits for creating jobs, taxpayer-funded workforce training, property-tax abatements, assistance with land acquisition (land is often just given away) and site development, credits against expenses for research and development, sales-tax refunds on machinery or energy used in manufacturing, credits for redeveloping brownfields or opening a business in a poor district.

Some are statutory; they are available to any company that meets a predetermined requirement. The $3.3m in job-creation credits that voestalpine will receive, for instance, comes from a credit available to any company in Georgia that creates jobs in one of seven sectors, including manufacturing. A company gets $3,000 per job per year for five years as a credit against its total tax liability. Voestalpine's port-tax credits are also available to any company in Georgia that increases imports or exports through Georgia's ports by at least 10% over the previous year. Around half of all American states have some sort of job-creation tax credits. Some target wages, as Georgia's does; others target types of businesses: in 2010 California and Connecticut both enacted credits for small businesses that hire full-time workers.

Easy money

Largest relocation and retention subsidies

	Year	Value $m	Origin	Destination
Sears Holding Corporation	2012	275	Illinois	Retention
Prudential Insurance	2011	250	New Jersey	Retention
Nissan	2005	244	California	Tennessee
Sears Roebuck	1989	168	Illinois	Retention
NCR	2009	109	Ohio	Georgia
Panasonic North America	2011	102	New Jersey	Retention
Motorola Mobility (Google)	2012	100	Illinois	Retention
American Greetings	2011	93	Ohio	Retention
Depository Trust & Clearing Group	2009	90	New York	New Jersey
Goya Foods	2012	82	New Jersey	Retention
38 Studios	2009	75	Mass.	Rhode Island
Marathon Petroleum	2011	72	Ohio	Retention

Source: Good Jobs First

Others, such as the relatively small $275,000 that went toward voestalpine's site development, are discretionary, meaning they go to specific companies for specific purposes—most often to large companies relocating or expanding in a state. The largest source of discretionary funds is probably the Texas Enterprise Fund (TEF), which Rick Perry, the governor, created in 2003. Texas calls this a "deal-closing" fund, critics a slush fund for the well-connected; either way, it provides grants that have ranged between $194,000 and $50m to companies choosing between a site in Texas and one in another state. Companies must promise to hire a lot of people (at least 75 in cities and 25 in rural areas) at wages above the county average. Since 2004 the TEF has dispersed $487.4m. Texas also offers grants to technology companies through its Texas Emerging Technology Fund, which has given nearly $195m to 137 businesses since 2005.

Texas's free hand has inspired copycats: all its neighbours now have discretionary deal-closing funds, as do several other states. They have come into vogue even as cash grants have generally grown scarcer. Companies may prefer cash grants to help them hedge risks and defray costs during a major expansion or those tenuous first few years, but in recent times states have tended to prefer credits and abatements, which have little or no upfront cost and have impacts that can be spread over several years.

The downturn has also led to demands for greater accountability for recipients of incentives and greater scrutiny from state legislatures. Many states now have clawback provisions written into their incentives. A 2012 study by the Pew Centre on the States found that (only) four states rigorously assessed their economic-development incentives, and used the results of those assessments to inform policy decisions. Without such measures costs can balloon. Louisiana, for instance, brought in an extraction-tax exemption for horizontal drilling in 1994, when that was a newish technology. In 2007 it cost the state $285,000. By

2010 horizontal drilling had become a common method of getting natural-gas deposits from the Haynesville Shale in northern Louisiana, and the exemption cost the state $239m. Such scrutiny may have helped inspire the welcome trend away from film-tax credits, which have limited lasting effect; the number of states offering them fell from 40 in 2010 to 34 in 2012, though that is still a lot more than four in 2001.

Even supporters admit that there is no simple way to determine how effective incentives are. Take Texas. According to the Federal Reserve Bank of Dallas, between June 2009 and June 2011 the state was responsible for nearly half of all jobs created in America. How much of that is due to the generous incentives it offers, and how much to other factors? Texas, after all, is a state where union closed-shops are banned, and with a lot of cheap land; a company could relocate there from Chicago, Boston or New York and come out ahead on land and labour costs alone.

A study by Angelou Economics, a consultancy headed by Angelos Angelou, a former vice-president of economic development for the Greater Austin Chamber of Commerce, in April 2012 found job growth correlated less with the amount of incentives states offer than with rates of entrepreneurship, retention of young professionals and overall business climate. States with an ageing population and high corporate taxes, such as Maine, may need to be more generous with incentives than young, low-tax states such as Georgia or Texas. Some may not like it, but brisk interstate competition is far better than none.

Correction: According to the original version of this story a study by the Pew Centre on the States found that 13 states assessed all of their economic-development incentives and used the results to inform their policy choices. In fact, only four do. This was corrected on April 30th 2013.

Fonte: The Economist, London, v. 407, n. 8833, p. 27-28, Apr. 27th – 3rd May 2013.