Responsible Economic Development Incentives, LLC

Helping communities and businesses find mutually beneficial solutions for the greater good.

Examining the efficacy of the "but for"

This is the third in a series of articles where we will study why discretionary economic development incentives are not functioning as intended, reforms that need to be implemented, and tactics that can be used to build consensus for changes to the systemic issues.

Background

Discretionary economic development incentives are supposed to be subject to the "but for" provision, that is, "but for the availability of the incentive, the project (e.g., capital investment, job creation, etc.), will not proceed." This requirement is in place to prevent waste, or incentivizing projects that will occur regardless of the incentive award. Yet research indicates, for incentivized projects, the same decision would have been made 75% to 98% of the time without the incentive.[1] But why is this so?

We will dive into this answer, cover policy and process improvements that will put an end to this madness, and discuss strategies to help us move beyond the prisoner's dilemma by covering a variety of topics. In our first two articles, we highlighted the importance of "leverage" with respect to maximizing incentives, and how project and/or location "uncertainty" and/or "competition" are used to gain leverage. We now move on to "transparency," a solution that could drastically change the incentive "game."

Transparency: It's time to level the playing field

As discussed in our first two articles, incentive granting bodies are currently at a severe disadvantage when it comes to site selection and economic development incentive negotiation projects. It is very easy to create the appearance of uncertainty and/or competition for a project, gain leverage, and use that leverage to secure and maximize incentives, often when there was no true uncertainty or competition for the project. The location decision had been made long ago, the project was going to happen in the targeted community, and securing incentives just became a "game" to extract as much as possible while still keeping the other side sufficiently happy.

The result is wasted taxpayer dollars, less money for education, infrastructure, essential services, workforce development, and investments in our communities that would make them more attractive from a quality of life perspective. So what can we do to put an end to this? It is actually fairly simple, incentive granting bodies need to take back control of the incentive "game," start making the rules, and stop letting others dictate how the "game" is played; really, to eliminate the "game" aspect entirely.

Incentives are funded by taxpayer dollars. Thus, a strict, fiscally responsible approach must be followed in order to ensure that no funds are given away unnecessarily, that is, above the minimum required to win the project. So how does one determine what is necessary? Is it even possible? Absolutely, and the answer is merely a new requirement for "transparency" in the incentive negotiation process.

In our prior articles, we discussed how certain information is frequently not shared with incentive granting bodies, things like the location of competing site(s) and the financial gap for the project or location. This is done to maintain leverage and keep incentive granting bodies in the dark, with the goal to obviously maximize incentives. After all, one would not want to indicate that the financial gap is $1,000,000 when there is a possibility to secure a $5,000,000 grant.

Additional information and documentation that incentive granting bodies should require include:

- Exact status of the project from an internal funding approval standpoint
- Actions taken with respect to the project (e.g., contracts signed, assets purchased, job openings advertised, etc.)
- Description and amount of incentives offered in connection with competing/alternative site(s)
- Copies of incentive offer letters for the competing/alternative site(s)
- Locations for the project's primary suppliers and customers, and service area for the project
- Rationale for the locations being considered from an operational perspective, and the advantages and disadvantages associated with each
- Copy of the financial gap calculations
- Whether a third party is providing incentive services in connection with the project and, if so, the exact nature and amount of the fee arrangement
- If a third party is providing incentive services, whether applicable lobbying registration and disclosure requirements have been met (or will be met in terms of periodic reporting)
- If a third party is providing incentive services on a contingent fee basis, whether the legality of such arrangement has been confirmed (e.g., lobbying, Circular 230, etc.)

While instituting policies to require this information and documentation would be a giant step forward, alone it is still not sufficient. Incentive policies also need to be updated to require validation of the necessity of the award. Thus, in addition to incentive granting bodies reviewing all of the information and documentation provided to verify the uncertain and/or competitive nature of the project and confirm the financial gap, incentive recipients should be required to publicly certify that "but for" the incentive, the project *will* not move forward in the specific community.

Please pay close attention to the definitiveness of this language. There is no more *could* or *may*, no more gray areas or room for gamesmanship. It also goes beyond the undefined "material factor" certification and finding required by one to a few current incentive programs across the country. Indicating that the incentives are a material factor in the project or location decision is not conclusive evidence that the same decision would not have been made without the incentives.

Either the incentives are necessary or they are not. If they are necessary and desired, then sign on the dotted line. With this more stringent certification, all parties -- the business, incentive granting bodies, community, taxpayers, citizens, children, and even future generations -- can be fully confident in the vetting process and celebrate the mutually beneficial nature of the deal.

Both sides win, better yet, all sides win. The community wins a project that otherwise would not have located there, the business is able to implement a project at its preferred location that it otherwise would have been unable to do, capital will be invested, jobs created, workforce skills enhanced, vendors engaged, wages paid, small businesses patronized, tax revenue generated, etc.

There is no waste, and money that would have historically been squandered due to unwarranted or excessive "incentivization" can now be invested in all of the things that will improve the community and make it more desirable, as well as used to support small businesses, many of which are currently struggling just to survive due to the pandemic. Multiply this across 75% to 98% of the thousands of incentive deals per year and ~$50 billion[2] in incentives handed out each year in the U.S., and this represents powerful reform and significant impact to say the least.

In our next article, the fourth and final in this series, we will touch on a variety of topics in the site selection and economic development incentive industry, including the current culture, changing landscape, ethical considerations, and additional appeals that can be made to help drive positive transformation.

By C.J. Girod | February 16, 2021

[1]Bartik, Timothy J. 2018. "'But For' Percentages for Economic Development Incentives: What percentage estimates are plausible based on the research literature?" Upjohn Institute Working Paper 18-289. Kalamazoo, MI: W.E. Upjohn Institute for Employment Research.

[2]Florida, Richard (2019, November 12). How Cities and States Can Stop the Incentive Madness. *Bloomberg*. https://www.bloomberg.com