

Economic Development Q&A with Andy Shapiro

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1. Are tax incentives often the determining factor in a company's location decision?

When I first started managing location engagements twenty years ago incentives typically received a lower weight during the initial location decision-making process, and became a more key determinant only as the project neared its final stages. Now, as projects become more footloose and cost control more critical, the search for effective incentives plays a more pronounced role in earlier project stages. All other factors considered (e.g., labor, costs, access, etc.) incentives can swing an investment toward an otherwise comparable jurisdiction; or they can make the difference between a decision to move forward and one not to invest at all.

2. Are tax incentives a cost effective tool for job creation?

While there has been little research into how effective state job creation tax credits are in promoting job creation, according to the Federal Reserve, researchers have investigated the effectiveness of other state business tax credits, and have found that these programs appear to be quite effective at increasing overall business activity within a state. Also, remember that in a growing number of states the tax credit per new job is a percentage of the state income tax withholdings associated with that job. So what you really have is a form of revenue sharing whereby very little public monies are spent on actual job creation. Finally, any calculus of job creation benefits should be sure to take into account the indirect and induced (or "downstream") jobs created as a result of the multiplier effect from each "direct" new job. Often each new job will cause the creation of as many as two additional jobs elsewhere in the economy. We conducted a recent survey that revealed as many as two-thirds of all US jurisdictions used some sort of economic impact model to help understand the direct and indirect job creation benefits associated with prospective projects.

3. Do you think states will begin to reduce their reliance on tax incentives or will they view them as essential to avoiding "unilateral disarmament" in the ongoing site selection competition between locations?

We have certainly witnessed budgetary pressures in many states that have threatened existing incentive programs. Incentives targeting emerging industries, including investment tax credits and venture capital funds, appear to have taken the brunt of this impact. However, so-called "pay as you go" incentives such as job creation tax credits will likely endure as they are considered to be revenue neutral. Also, some states have chosen to double-down during the current recession and to increase incentives for new jobs and investment. In just the past year or so, my home state, New Jersey, has enacted a new tax increment financing program and an "Urban Transit Hub" tax credit that provides potential tax credits in the amount of up to 100% of a qualifying commercial project's capital costs.



4. Do you think tax incentives generally are applied too broadly?

Incentives are pricing tools, in other words, their impact goes right to a project's bottom line. In the U.S. the practice is for state agencies and local jurisdictions to use incentives to intervene in the market where a marginal, additional public investment is capable of leveraging significant additional direct investment. These jurisdictions have learned how to invest incentives in transactions where they would have made a difference, including having the ability to reverse an analysis where a competing locale was more cost effective. So, while there may be examples of the indiscriminate use of incentives, they are most effective when employed in a targeted fashion.

5. What are the most effective types of tax incentives?

The most effective incentives are those that apply to our client's needs and particular circumstances. For example, commercial organizations tend to be more job intensive while industrial projects may feature higher levels of investment. The former may derive more benefit from job creation grants the latter from investment tax credits. In every instance we ask the question, "Can the client utilize the benefits being offered?" Usability is paramount. If the client has insufficient corporate tax liability will the tax credits be refundable, or assignable? And, the incentives should be effective for public agencies as well. Do they respond to the changing economic environment? Is job retention treated as if it was equal in value to job generation?

Note: there are many incentive programs that are not tax-based. To be accurate and more comprehensive I would just refer to all of these as just "incentives"

ABOUT BIGGINS LACY SHAPIRO & COMPANY

For more than 25 years, Biggins Lacy Shapiro & Company has provided professional expertise and creativity in the field of Location Economics: the mix of specialized disciplines that enables companies and communities to plan and execute successful location strategies. We create value on both the demand and supply side of the market for corporate location decisions.

ABOUT ANDY SHAPIRO | MANAGING DIRECTOR, BIGGINS LACY SHAPIRO

Andy heads the firm's location advisory practice, helping clients translate their business objectives and strategic vision into rational, balanced location decisions. His primary responsibilities include site selection (in partnership with Wadley Donovan Gutshaw Consulting), feasibility analysis and labor market analysis.

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