



Incentives Maneuver May Prove to be Savvy By Andrew Brod *Greensboro News & Record*, October 1, 2006

The Guilford County commissioners get a lot of ribbing, for hyper-partisan politics and occasionally for odd behavior. But on the issue of economic-development incentives (the targeted grants and tax breaks given to individual companies to locate and expand in a particular area), the commissioners did the right thing this year. In fact, they did it *twice*. First, they declared a 90-day moratorium on EDIs back in June. Then they removed the moratorium and put the county back in the business of granting them.

How can it be commendable to do something and then reverse yourself so quickly? It's because of the strategic nature of the incentives game. As I've noted in a number of columns in the *News & Record*, states and counties are mired in a pernicious strategic environment that economists call the Prisoner's Dilemma, in which individually rational decisions end up generating the worst collective outcome.

The "invisible hand" that makes competition a good thing in most markets is absent in the incentives game. Society is worse off when everyone competes in the incentives game, but few states and counties feel they can choose not to play.

It's easy to see why the moratorium was declared. EDIs present local governments with an array of challenges. How much should be offered? Will the incentives work? Rarely do local governments go back and assess the incentives they've granted in the past, to confirm that job creation, wages, and capital investment really were as advertised. Fortunately, some incentives are contingent on taxes paid or jobs created, and hence they come with a built-in assessment scheme. But other EDIs are up-front grants.

And of course there's the nagging feeling that companies don't really make decisions based on EDIs. Would the company have located here anyway if not for the incentives? Surveys of executives generally place EDIs fairly far down the list of regional attributes that matter to location and expansion decisions. For example, a 2000 survey ranked them as the 15th-most important factor to executives, out of a total of 34 factors. But those surveys fail to address the potential significance of incentives once the short list of sites is chosen. At the margin, perhaps EDIs matter. No one really knows.

Moreover, local governments are up against companies and consultants who really know how to play the game. In a 1999 article in *Expansion Management*, one site-selection consultant advised his corporate clients to:

- Negotiate incentives for the new project in two or three finalist locations, preferably in different states.
- Spend the most time negotiating in the preferred location and use offers from the alternate areas for leverage.

- Tie incentive negotiations in the preferred area to a couple of sites, ideally in separate communities.

Sounds familiar, doesn't it? We've seen this drama played out again and again. Maybe local governments need to try to play hardball too.

Ultimately, of course the county commissioners had to end the moratorium. One consultant told them that it had "created the beginnings of a little yellow flag about Greensboro" that sent the signal that "maybe this community is not so friendly to business anymore." The commissioners heard about tough competition for site selection and some of the basics of the Prisoner's Dilemma (though I doubt anyone used that name). By ending the moratorium, the commissioners showed that they understand that as problematic as the incentives game is, we can't simply refuse to play.

But declaring the moratorium in the first place may also have sent a signal. It says that even though Guilford County is back in the incentives game, it will play with a sharp eye directed at performance and with a healthy dose of skepticism. Fortunately, the commissioners' final decision on EDIs prior to the moratorium lends some credibility to this stance. They denied \$50,000 in incentives to TriQuint Semiconductor, a company looking to locate a research-and-development facility in High Point. Armed with incentives from the city of High Point, TriQuint located the facility there anyway.

Since the moratorium ended, some commissioners have talked about developing a hard-nosed performance-based EDI policy. This is a good idea, because the incentives game has just started up again. On Thursday, the commissioners will hear from three companies asking for a total of \$444,000 in incentives from the county. The commissioners should keep the following in mind:

- Incentives should be structured as much as possible on a contingent basis; try to minimize the proportion of up-front grants.
- Don't just count the number of jobs; pay attention to the type of jobs, the wages paid, and the potential economic impact.
- Never grant incentives to retail establishments, except to help address separate goals such as improving an economically blighted area.
- Be willing to lose a company from time to time.

Local governments may always be at a disadvantage in the incentives game, but perhaps by declaring and then ending its incentives moratorium this year, Guilford County can make the odds a little less uneven next year.

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