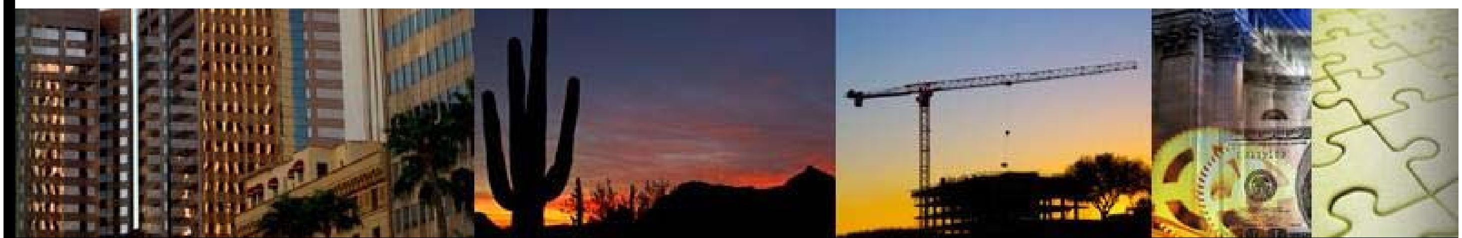
The Job Recovery Package for the State of Arizona - Executive Summary



Prepared for:

The Speaker of the House of Representatives, State of Arizona

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Executive Summary

Purpose of the Job Recovery Package

The State of Arizona should strive to not just grow, but to *grow well*. Unfortunately, the State's economic performance could be lackluster for some time to come. The current downturn has exposed the weaknesses in the State's economic composition including an overreliance on growth, a relatively uncompetitive tax structure, and a lack of targeted economic development programs. Forecasts identify 2014 as the year that the State returns to the employment levels of late 2007. Population growth is currently anemic and per capita personal income (a measure of standard of living) remains on a general downward trend compared to the rest of the country. Without some policy action the State risks the further decay of its standard of living compared to the U.S. as a whole.

During previous decades the State benefited from specific opportunities that changed the momentum of the economy for the better. One primary example includes the movement of military operations away from the coasts both during and following WWII (which facilitated the development of the local aerospace and semiconductor industries). Strong political leadership also facilitated economic expansion in earlier decades. Unfortunately, there have been few successful attempts at the local level to further diversify the State's economic base during the last couple of decades.

The purpose of this report is to provide a list of recommendations that could assist in this effort and also result in the creation of high quality jobs for Arizona residents. The State's tax code was reviewed for select areas that could be improved upon. The report does not recommend a complete overhaul of statute though. Scores of economic development programs from all parts of the country were also reviewed in order to identify a list of best practices for diversifying the State's economic base. A review of both tax policy AND economic development programs is key to improving the State's economy.

Since many of the recommendations contained in this report have already gone through the "experimental" phase in other states, the level of risk associated with implementation is reduced. However, no recommendations will result in the creation of jobs and the betterment of the State's economic base without the political will to become more competitive. *The goal is not to reinvent the wheel; the goal is simply to bring the wheel to Arizona.*

What Makes an Economy Tick?

One needs to first understand how different types of businesses impact the economy before recommendations can be made. Not all companies are alike. "Base" (a.k.a. export) industries are those that export their products out of a region, and result in the importation of money into that region. The issue of importing dollars into the State is a crucial economic development concept. Once a dollar makes its way into the State, it flows from person to person as demanded products and services are supplied. These local goods and services are provided by "domestic" sector companies. Eventually some money leaves the local economy when products (and some services) are provided by companies outside of the State.

Base industry operations can be considered the engine that drives an economy. The ghost towns of the Old West further illustrate their importance. Once the local mine ran out, the railhead moved, or a drought caused agriculture to no longer be viable, many communities ceased to exist because monies were no longer flowing into the community.

Examples of base industries include the manufacturing sector, export-related business services, tourism, retirement, and federal government employment. Some base industries are high paying while others are relatively low paying. Also, some base industries such as tourism and retirement require marketing but do not require incentives for operations (i.e. they are more captive to the State). The key is to encourage higher value added/higher paying base industry development. Base industry companies also tend to be more capital intensive, and/or utilize skilled labor (not in every case though, i.e. tourism, federal government). As local capital investment improves and as more high skill workers are employed, productivity increases. This also leads to higher incomes and a higher standard of living for employees in these industries.

The aforementioned local serving industries provide goods and services to the local population. Activities include most retail operations, construction, and local service banks, to name a few. The existence of base industries creates demand for these local serving industries. *Without base industries, there is no means of supporting local serving businesses.*

Local serving employment created as a result of export activity is often referred to as "indirect and induced" employment. These are also called multiplier effects. "Indirect" jobs are those created by businesses that provide goods and services to the export-oriented business/industry. "Induced" jobs are created as a result of the spending by direct and indirect employees in the local economy on such things as food, housing, transportation, etc. Many forget that when the higher paying base industries are pursued, new job opportunities arise for all levels of employment from the highly skilled to those with basic skills. Therefore, base industry promotion actually serves all Arizonans. Higher wages in base industry operations directly enhances the multiplier effects in terms of job creation and salaries.

No public policy measure, no matter how well crafted, can result in an immediate and significant change in a large community's economic composition. However, if the proper tools are made available, public policy can indeed begin to attract individual base industry companies to a region rather quickly. Policymakers will not only need to provide these tools but will need to continue to be aggressive about economic development for many more years. This will allow for a gradual improvement in per capita personal income among Arizona residents.

How does Arizona Recover?

The State's economy will recover in time. Even with no new public policy measures, job growth and population growth may again be among the top five in the nation. Those sectors that grew rapidly during the last decade (i.e. construction and other industries related to growth) will generate many jobs. However, the goal of policymakers should be to direct attention to the higher value added industries that tend to pay higher wages, export their product, and generate new economic activity within the State. We can no longer rely on untargeted growth as the State's primary economic driver.

The attraction, retention, and internal growth of these base industries will not only result in higher income levels, but will also result in *__more government tax revenue__* *and will improve upon the standard of living.* Diversifying the State's economic base will also mitigate the ill effects of future downturns. Therefore, in order to recover from the current economic downturn the State must become more focused and competitive in terms of its economic development policies.

Arizona's Competitiveness Today

For decades, Arizona's economic development strategy loosely consisted of its quality of life, sunshine, good transportation system, affordable workforce, and pro-business governments, just to name a few. These factors primarily facilitate the expansion of lower value added industries such as tourism, retirement, and labor intensive operations such as customer service and call centers.

Times have changed and Arizona finds itself several years behind the curve when it comes to strategic economic development across the State. Today, more is needed to lure higher value added industries to the State. Other states (mostly east of the Mississippi River) are providing *limited and* *__very__* *targeted* economic development tools designed to have an immediate influence on business decisions. In combination with aggressive and strategically targeted business development efforts, these incentive tools have been implemented to respond to a company's primary concern of finding the best overall net economic opportunity. Arizona is considered by many as being uncompetitive in this regard. This view can change though as modifications in public policy and how elected officials view economic development practices improves.

Specific Policy Recommendations for the Recovery

As previously noted, there are two components to economic growth that are addressed in this report: 1) the provision of a competitive tax structure, and 2) the provision of competitive economic development programs. Many studies have been written on how tax policy impacts an economy. However, most exclude the necessary economic development component. Competitive tax policy that targets base industry operations gets you "in the game", but competitive economic development policy "closes the deal." This entire report can be reduced down to a singular question: How can policymakers best facilitate the closing of such deals and create higher paying base industry jobs while diversifying the economic base and stabilizing the revenue base?

Job growth and retention is achieved through the attraction and retention of base industry companies and through the internal growth of companies from within the State. There are multiple options for identifying these base industries in statute. States across the country have utilized a combination of industry classification, wage level, percentage of sales outside of the state, and economic & fiscal impact. Specific examples, by program, are provided in the body of the report.

The following recommendations were derived in consideration of this point and place additional weight on the attraction of base industry operations. The recommendations are separated into various types. Some items will have an immediate impact on the State and also do not require a monetary appropriation to implement. Other items could require a legislative appropriation for enactment, at least in the initial stages of the program. In these cases, it is recommended that policymakers first use any remaining federal stimulus monies.

A more complicated problem arises related to focused business retention. The Arizona aerospace industry is of particular importance in this example. A "saved" job is just as valuable as a "created" job. In fact, the level of incentive needed to retain a current job is often less than the level of incentive needed to create a new job. However, current jobs are already contributing monies to the State General Fund. If an industry such as aerospace expands, and the expansion otherwise would not have occurred absent some economic development or tax law policy change, then *redirecting a portion of the related new tax revenues for use on economic development will come at "no-opportunity-cost". This means the State will not lose any tax revenue that otherwise would be here.*

If a program instead focuses on retaining jobs that are already here, then redirecting a portion of the related tax revenues could cost the State when compared to current collections. In these cases, some tough decisions must be made related to the appropriate use of current funds. On the other hand, *if a business is confirmed to be leaving the State absent some incentive program, the incentive can also be considered a no-opportunity-cost provision.* Job retention should be considered, along with both benefits and costs, when adopting the recommendations contained in the following sections. Unfortunately, it is very difficult to identify those companies that are truly considering leaving versus those that are making threats for financial gain.

The following tax policy modifications and economic development programs should be considered during the 2010 Regular Legislative Session and would not require an immediate appropriation except for possible program management or, in select cases, targeted job retention.

- Create a new business real and personal property classification with an assessment ratio equal to the residential ratio of 10%. This class will be available on a discretionary basis to base industry operations only. "Base industries" will be difficult to identify in statute and careful wording must be incorporated into any proposed legislation. Property tax sub-classes that distinguish between a building's precise operational use may be a good starting point. Absent political support for a new property tax class, it is recommended that the legislature continue to lower the assessment ratio on commercial property.

- Create a "Quality Jobs" program that provides incentives for the creation and retention of high paying jobs at base industry companies. This type of a program is typically funded through withholding taxes that otherwise would not be collected absent the new business location and new job creation. Job *retention* could have a cost unless the "retained" job would have left the State absent the incentive provision. This is not always easy to verify. In this specific case, the retained job can be treated as new for analysis purposes.

- Create a new Job Training program to replace the one that was recently suspended. This program would also be funded through net new withholding taxes instead of the previous legislative appropriation and separate business tax. The same issues related to job retention also apply here.

Incentives for the Quality Jobs and Job Training programs are designed to be primarily revenue neutral or positive in relation to new business development. Any incentive benefits paid to a qualifying company are directly funded from a percentage of employee personal income tax revenue (i.e. withholding taxes) that the new target company contributes. For one example, if incentive benefits are equal to 50% of employee personal income tax revenue, the State collects 50 cents and the Company collects 50 cents for every $1 of net new tax collections. These percentages can vary from program to program. In addition, the State's net benefit can be increasingly positive with the potential generation of net new State sales taxes, unemployment taxes, and corporate income taxes. This would be enhanced further as “spin-off” multiplier jobs are created and the State collects the associated revenues. This basic design effectively requires no cost to the State (except for program management; see recommendations below) and, under the right program details, could produce excess revenues that could seed or fund other economic development programs *such as job retention.*

The next set of policy recommendations are of similar importance as those above and may require an appropriation for enactment. Again, discretionary federal stimulus monies would be of proper use or any net new revenues to the State from the implementation of other economic development programs. The second option will require accurate economic modeling prior to funding.

- Create a “deal closing” fund to provide financing/grants for individualized investment that may be required to attract a particular base industry company. The fund may require an initial endowment of discretionary stimulus dollars or an initial appropriation but could be designed to be self sustaining in the longer term as a result of new businesses locating in Arizona along with their associated tax liability. Too long of a delay in providing seed money for the fund could dampen economic development prospects and high-quality job creation in the State.

- Reduce the corporate income tax rate from 6.968% to 5.0%. This will make the State more competitive in terms of the visible, up front tax rate. This will allow for better marketing of the area and will be in closer alignment with the State’s top individual income tax rate. It should be noted the State’s effective corporate income tax rate is not overly oppressive on those businesses that fuel the economy, but it is high enough to make the State appear less competitive in terms of business relocation or expansion decisions. Only a moderate rate reduction is recommended and must be combined with enhanced marketing of the State.

The final set of policy recommendations require additional study to strategically implement for purposes of achieving the State’s economic development goals and still may be considered in 2010. Appropriations may also be necessary in certain cases.

- Modify the State’s Enterprise Zone Program to be base industry oriented and to better target new growth. Currently, to receive the designed property tax assessment ratio of 5%, a company must first meet certain criteria that typically do not apply to export industry businesses. The businesses are already eligible for corporate income tax relief though. The current program design is of limited economic development value and needs to be enhanced. The appropriate vehicle for this modification could be through a broader review of state economic development programs and tax credits by legislators and economic development professionals to ascertain what programs/credits work and which programs/credits need to be modified or eliminated altogether.

- Adequately fund a State entity that promotes economic development along with improvements in branding. All successful business recruitment states rely on an adequately funded *state* entity to serve as the primary point of contact to coordinate with the State's economic development entities. One recommendation is that any new or modified State entity must utilize a seasoned economic development director that is appointed by individuals from the private sector for a limited term. The main point is to limit political influence when it comes to economic development. Other public/private partnering options may also be viable.

- Commission a State economic development strategy that *focuses on coordinated marketing and branding.* The successful business recruitment states also have a specific focus when implementing economic development policy. These documents also outline how the economic development entities utilize each other's services. To date, the documents produced by the State on economic development have been relatively weak in terms of this kind of proactive effort and not in full consideration of site selection and economic facts. Overall, the State currently does not tell its economic story very well.

Many of the above items have not been considered in recent years by State policymakers so additional education is in order. Very detailed justification for these items is included in the body of this report. Ideally, the above eight recommendations should serve as the starting point in the development of an *economic package* that focuses on job creation via base industry growth. However, politics is not always ideal. Given the current economic environment, there is a concern among policymakers about the need to provide broad-based business relief to Arizona employers.

There have also been tax policy and economic development program changes that have indeed been considered recently and appear to have political support. These items are likely to be more familiar to the legislature and legislative analysts. It is well known by now that Arizona has historically been kind to households but tough on businesses regarding tax policy, as noted throughout this report. While the following items are not part of this report's formal recommendations specifically related to base industry development, they have addressed issues related to excessive business taxation and the desire to assist in internal economic growth. These items are listed for reference purposes only but are likely to be considered by policymakers again in 2010.

- Eliminate the State Equalization Tax. While not a targeted approach, such a business tax reduction would address the issue of Arizona being kind to households but overly tough on businesses. Both base industries as well as local market industries would receive this reduction in tax burden.

- Flatten or enact a truly "flat" individual income tax. Arguments have been made that a reduction in the higher income tax brackets may result in enhanced, long term small business development. This relates to the issue of improving the State's ability to grow from within. It is possible to do this with no net cost to the State General Fund. This policy issue would have less of an impact on out-of-state business relocations though.

Longer Term Issues:

- Establish tax increment financing (TIF) legislation. There are issues related to whether or not this would be constitutional based on previous legal interpretations and would likely require the expenditure of some political capital to implement. However, Arizona is the *only* state that does not utilize this tool and policymakers should be open to at least considering such a program with adequate public debate. Properly designed TIF programs can be revenue positive.

- Track immigration reform. It is not appropriate to ignore current laws regarding immigration policies as many politicians suggest. However, agricultural communities have already realized problems related to worker supply and have realized reductions in production and a shifting of food processing out of their areas. The next worker shortages will be realized within the tourism and construction industries after the economic recovery is in full force. This could result in wage inflation and may have negative economic consequences. This issue is beyond the scope of this report but policymakers will need to pay attention to any related Federal reform on this topic.

Current State Tax Structure

Many have recently argued that the current State tax code is outdated and, as a result, has produced record budget deficits. Unfortunately, this may be an oversimplification of the facts. The recent deficits are the direct result of a very harsh economic downturn, the State's dependence on growth, and poor decisions that were made by policymakers. These are deficiencies that can change over time.

One well publicized point that may not be accurate is the State is overly reliant on the sales tax. Basic economic theory finds that a tax on consumption (i.e. a sales tax) is far less disruptive than a tax on production (i.e. an income tax). Furthermore, a simple review of historical tax collections data identifies that the sales tax is actually far less cyclical than the income tax and is also easier to predict based on economic variables. Finally, the current deficits could have been more manageable with proper fiscal policy through recent years including the maintenance of an adequately funded Budget Stabilization Fund and spending constraints. However, a review of additional tax law changes as it relates to fiscal stability would still be a worthy endeavor. This is beyond the scope of this particular report.

As previously noted, one point that is indeed accurate is that Arizona has historically been kind to households but tough on businesses. The State appears to be non-competitive in its corporate income tax rate and also in its business property taxes. The property tax issue is the foremost economic development concern. Business property is assessed at twice the rate of residential property. The aforementioned modifications to the business real and personal property taxes, as they relate to base industry development, are a critical component of any State economic recovery package. This modification could serve as a business expansion/relocation/retention "deal closer." The corporate income tax modification is the type that would get us "in the game" more often but would need to be paired with aggressive marketing of the State and the enactment of other economic development tools. This tax cut would benefit both base and local market industries but the negative consequences in this particular case are likely to be offset by the positive effects of being more competitive in terms of overall tax rates.

Keep in mind that Arizona cannot be "number one" in every economic development category. A State cannot be first in low tax rates and also be first in education and infrastructure spending. Having a competitive tax structure, adequate spending in those areas that impact economic development, along with very focused and efficient economic development programs, will have a far greater impact on the State's economic health than leading the nation in any one area.

State Business Climate Rankings

There are both positive and negative points that can be made of state ranking articles. Some articles are written by individuals that are doing nothing more than pushing a personal agenda. For this reason it is important to be selective in what documents are used. For some perspective, a set of very select ranking articles were reviewed to identify any consistent facts. Unfortunately, the findings indicate that Arizona is far from competitive.

Company executives, economic development agencies, and site selection consultants actually keep a close eye on a state's business climate ranking. Whether to confirm a perception or satisfy curiosity, business climate rankings tend to be one of the first items of business when considering new locations for operations. A number of business climate rankings are periodically published by Site Selection Magazine, Business Facilities, CNBC, Forbes, Chief Executive Magazine, and IBM Global Business Services, just to name a few. The validity of the methodologies used in each business climate ranking survey can certainly be argued. However, right or wrong, the typical CEO tends to rely on these rankings at face value. Arizona's ranking in these surveys should not be the primary focus of a state's economic development policy, but it is important to recognize the perceptions among the general business community. A top 10 ranking in the major categories should certainly be attainable for Arizona.

State Business Climate Rankings

	2009 Business Climate Rankings	2009 Top Ten Competitive States	2009 Top States & Provinces in North America	2009 Best & Worst States for Business	2009 America's Top States for Business	2009 The Best States for Business	2009 Top 10 States for Business Climate
	Site Selection Magazine	*Site Selection Magazine*	*IBM Global Business Services*	*Chief Executive Magazine*	*CNBC*	*Forbes*	*Business Facilities*
1	North Carolina	Ohio	Ontario	Texas	Virginia	Virginia	Texas
2	Texas	North Carolina	Virginia	North Carolina	Texas	Washington	South Dakota
3	Virginia	Michigan	Ohio	Florida	Colorado	Utah	Wyoming
4	Ohio	Pennsylvania	South Carolina	Georgia	Iowa	Colorado	Utah
5	Tennessee	Kentucky	Pennsylvania	Tennessee	Utah	North Carolina	Florida
6	South Carolina	Texas	Quebec	Nevada	Minnesota	Georgia	Delaware
7	Alabama	Tennessee	North Carolina	Virginia	Kansas	North Dakota	Washington
8	Georgia	Alabama	California	Arizona	Massachusetts	Texas	Montana
9	Indiana	Indiana	Illinois	South Carolina	North Carolina	Nebraska	Oregon
10	Kentucky	South Carolina	Indiana	Colorado	Georgia	Oregon	New Hampshire
Arizona	**24**	**--**	**--**	**8**	**18**	**36**	**--**

Source: Elliott D. Pollack & Company; Site Selection Magazine; IBM Global Business Services; Chief Executive Magazine; CNBC; Forbes; Business Facilities.

What Drives Business Locations?

Site Selection Magazine conducts an annual survey of corporate real estate executives from a broad array of industries. This survey asks each executive to list the main site selection factors they consider when evaluating a location decision. Infrastructure, workforce, and tax climate are on the top of the list. Following these items are availability and cost of real estate, and regulatory concerns. Economic incentives tend to be one of the final factors in a location decision. Again, a competitive tax structure (and an adequate supply of affordable or skilled labor, etc.) may get us on the list of considered sites, but the incentive programs tend to separate the winners from the losers. In some cases, such as in the recommendations included in this report, improving workforce skills can be part of the incentive package (Quality Jobs Program) as can infrastructure improvement or the offsetting of start-up costs (Deal Closing Fund, etc.).

Top Site Selection Factors
2009 Corporate Real Estate Executive Survey

1	Transportation infrastructure
2	Existing workforce skills
3	State and local tax scheme
4	Utility infrastructure
5	Land/building prices & supply
6	Ease of permitting & regulatory procedures
7	Flexibility of incentives programs
8	Access to higher education resources
9	Availability of incentives
10	State economic development strategy

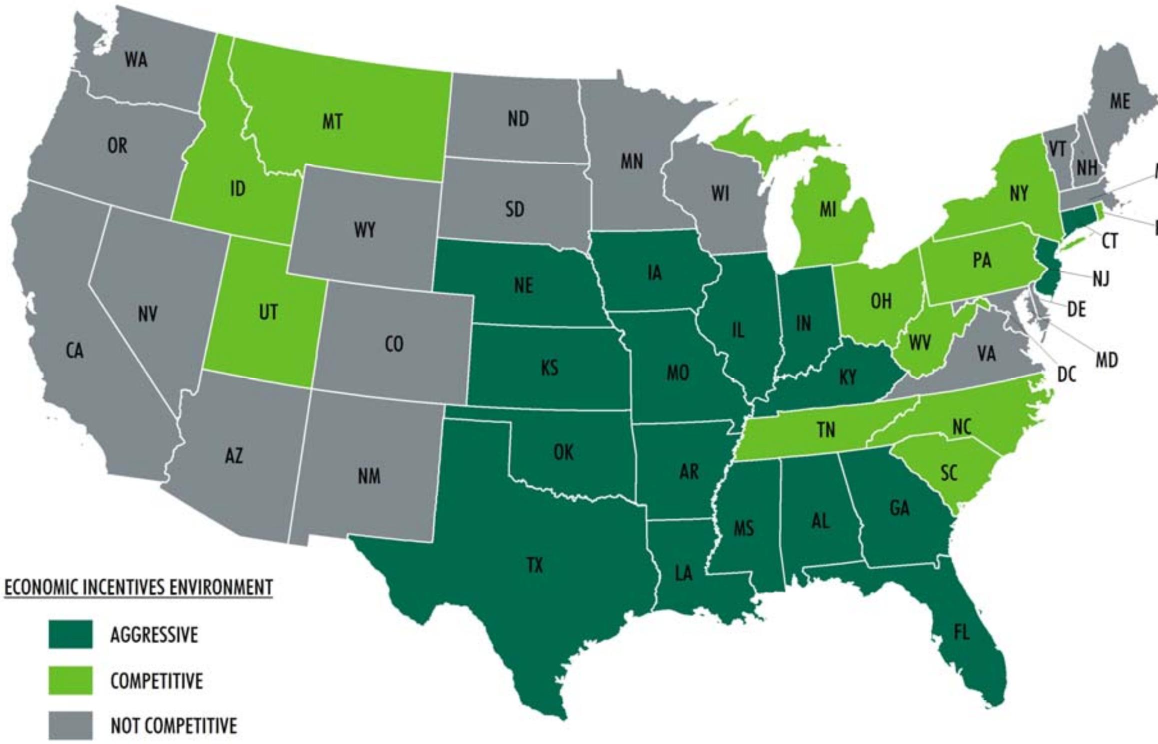
Source: Site Selection Magazine

The results of the Corporate Executive Survey provide a practical and realistic picture of site selection today. Based on a fifteen year history of site selection engagements conducted by the CBRE Labor Analytics Group and Economic Incentives Group, the availability and cost of adequate labor, land, and facilities are usually the most important initial site selection factors. *Incentives become more decisive when competing markets have relatively similar labor costs, tax structures, employee skill levels, etc. Again, being broadly competitive in terms of tax rates gets us in the game, but the economic development packages close the deal.*

How Competitive is Arizona with Economic Incentives?

All things considered (including geography, transportation infrastructure, supply chain, labor cost and availability, and other factors), economic incentives play a critical role in recruiting and retaining strong economic development prospects across the U.S. The following map illustrates each state's relative competitiveness with economic incentives. This map is produced by CBRE's Economic Incentives Group and is based on the Group's extensive experience with economic incentive negotiations across the U.S. during the past five years, each state's main economic incentive programs, and recent precedence for offering discretionary incentives. Arizona is currently considered "Not Competitive" in this particular assessment. *Keep in mind that the map does not highlight a state's economic health or ability to grow. It highlights those states that have implemented economic development programs that are likely to have a significant impact on their ability to create new, higher wage jobs over time.*

Economic Incentives Environment in 2009



Source: CBRE Economic Incentives Group

Case Study: A General Comparison of Incentives by State

All 50 states have a number of economic incentive programs. These programs vary by type, availability, target industries, performance metrics, and methods of payment. For purposes of comparing Arizona to each state and for simplicity, the following example is limited to six incentive programs available for general commercial and industrial businesses. Exclusions to this analysis are direct business financing, municipal grants & loans, local incentive programs, and other state programs not directly available to economic development prospects.

***Job Tax Credit**:*

- 38 of 50 states offer job tax credits;
- *Arizona – Limited: Enterprise Zone Program*
- These programs provide corporate income tax credits based on job creation and/or retention. Tax credits are issued upon employment verification on an annual basis, allowed to cover between 50% and 100% of tax liability in any given year, and permitted to be carried over to future tax years should tax liability not be sufficient to cover the earned tax credits. Some states allow tax credits to be transferred/sold to third parties. A few states allow these tax credits to be refunded.

Investment Tax Credit:
- 32 of 50 states offer investment tax credits;
- *Arizona – Limited: Renewable Industries ("Solar" legislation)*
- These programs provide corporate income tax credits based on capital investment in real and/or personal property. Tax credits are issued upon investment verification, allowed to cover between 50% and 100% of tax liability in any given year, and permitted to be carried over to future tax years should tax liability not be sufficient to cover the earned tax credits. Some states allow tax credits to be transferred/sold to third parties. A few allow tax credits to be refunded.

Job Training Grant:
- 49 of 50 states offer job training grants;
- *Arizona - Inactive*
- These programs provide grants to offset a portion of a company's training costs. Grants typically cover a defined list of eligible training costs and are typically paid out on a reimbursement basis. These costs include trainer salaries, travel costs, books, materials, training facility rent, and other items. Few states allow reimbursement of trainee wages.

Payroll Rebate:
- 9 of 50 states offer payroll rebates;
- *Arizona - None*
- Payroll rebates involve annual or quarterly cash refunds of a proportion of new annual payroll generated by an approved business. Payroll rebate benefits are expressed as either a percent of gross taxable wages or a percent of withholding taxes. Refunds are typically approved for 3 to 10 years.

Cash Grant / Closing Fund:
- 19 of 50 states offer cash grants or closing funds;
- *Arizona – Inactive/Previously limited (CEDC Fund)*
- Cash grant funds are discretionary incentive programs that provide upfront cash to qualified businesses whose operations have a significant economic and fiscal impact on a State. These cash grants are typically paid upon receipt of full government approvals of an economic development agreement, prior to certificate of occupancy, or within two years. State deal closing funds are part of this category.

Sales/Use Tax Exemption or Rebate:
- 19 of 50 states offer sales/use tax exemptions or rebates;
- *Arizona – Limited (i.e. Film Tax Credit)*
- Sales/use tax exemptions allow for full or partial abatements of sales or use taxes due on purchases of construction materials, equipment, and/or utility usage. Most sales/use tax exemption programs are limited to certain industries, types of operations, or performance metrics (i.e. job creation or capital investment).

Other Tax Exemptions:
- 19 of 50 states offer sales/use tax exemptions or rebates;
- *Arizona – Limited: Government Property Lease Excise Tax*
- Miscellaneous tax exemptions are offered by states to offset burdens of sales taxes, income taxes, use taxes, local property taxes, and fuel taxes just to name a few. These programs

generally are not applicable to the typical economic development prospect. Most other tax exemption programs are limited to certain industries, types of operations, or performance metrics (i.e. job creation or capital investment).

Inventory of State Economic Incentive Programs

(Most widely used economic development programs)

State	Job Tax Credit	Investment Tax Credit	Job Training Grant	Payroll Rebate	Cash Grant / Closing Fund	Sales/use tax exemption or rebate	Other Tax Exemptions
Alabama	X	X	X			X	X
Alaska			X				
Arizona	**X**	**Renewable**	**Suspended**				**X**
Arkansas	X	X	X	X	X	X	
California	X		X				X
Colorado	X	X	X			X	
Connecticut	X	X	X		X		X
Delaware	X		X	X			
Florida	X	X	X		X	X	
Georgia	X	X	X		X		X
Hawaii	X	X	X				X
Idaho	X	X	X			X	
Illinois	X	X	X		X	X	
Indiana	X	X	X				X
Iowa	X	X	X		X	X	
Kansas	X	X	X	X	X	X	X
Kentucky	X	X	X				
Louisiana	X	X	X	X	X	X	
Maine		X	X			X	
Maryland	X	X	X		X		
Massachusetts		X	X				
Michigan	X	X	X				
Minnesota	X		X			X	X
Mississippi	X		X	X			
Missouri	X	X	X	X		X	X
Montana	X	X	X		X		
Nebraska	X	X	X			X	
Nevada			X			X	
New Hampshire			X				
New Jersey	X	X	X	X		X	
New Mexico	X	X	X		X		
New York	X	X	X			X	X
North Carolina	X	X	X	X	X		
North Dakota	X		X				X
Ohio	X	X	X				X
Oklahoma		X	X	X			
Oregon			X		X		X
Pennsylvania	X		X		X	X	X
Rhode Island	X	X	X				X
South Carolina	X	X	X		X		X
South Dakota			X				
Tennessee	X		X				X
Texas			X		X	X	
Utah	X	X	X		X		
Vermont	X	X	X			X	
Virginia	X		X		X		
Washington			X				X
West Virginia		X	X		X		X
Wisconsin	X		X				
Wyoming			X				

Source: CBRE Economic Incentives Group.

Best Practices of Economic Incentive Programs

In consultation with the CBRE Economic Incentives Group, a review was conducted on all 1,300+ economic incentives programs in their database to find the most effective, flexible, targeted, and financially significant state programs across the U.S. These best practices are considered the most effective at recruiting and retaining businesses. The benefits, eligibility thresholds, and funding mechanisms should serve as the basis for any new economic incentive program in Arizona.

Job Training Grant Programs

Forty-nine out of 50 states (Arizona being the exception) currently have an active State job training grant program. Most job training grant programs across the U.S. are funded by general appropriations and reimburse a limited proportion of actual training costs incurred by businesses. Eligible training costs tend to include trainer salaries, books, materials & supplies, travel costs, curriculum & development, and some portion of rent for a training facility.

Iowa, Kansas, and New Mexico have the most effective State job training grant programs in the U.S. according to CBRE. These job training grant programs have unique funding mechanisms and have evolved beyond the standard program to include reimbursement of trainee wages.

Payroll Rebate Programs

Nine out of 50 states offer some type of payroll rebate incentive program. A payroll rebate mostly involves annual or quarterly cash refunds from a state based on a percentage of either new gross wages or new withholding taxes. This type of incentive is designed to be pay-for-performance. Incentives are directly tied to new payroll generation and job creation. Upon payroll generation and remitting withholding taxes to a state, the company is eligible for a cash refund. A state's motivation for offering a payroll rebate incentive is two-fold. First, the periodic refunds directly motivate an eligible company to create new jobs and generate new payroll. Second, the refund is delivered in the form of cash rather than tax credits or tax exemptions.

Beyond the marketing benefits, a well-designed payroll rebate program can be inherently revenue neutral or positive. Cash refunds are only paid out when payroll and withholding taxes are received. Cash refunds will not exceed incoming tax revenue. Arkansas, Kansas, Louisiana, Missouri, and Oklahoma have the most effective payroll rebate programs in the U.S.

Deal Closing Funds

Nineteen out of 50 states offer some type of deal closing fund or cash grant program. A deal closing fund involves upfront cash grants and/or forgivable loans only in highly competitive situations and only for projects with a substantial economic and fiscal impact to a state and community. Deal closing funds are mostly financed through periodic general fund appropriations.

The Texas Enterprise Fund is the most plentiful, active, and highly marketed deal closing fund among the states. Arkansas, Florida, Louisiana, North Carolina, and Virginia have established deal closing funds and have been actively funding projects during 2009, according to the CBRE Economic Incentives Group.

Retention Incentive Programs

Nearly all statutory and discretionary state incentive programs are designed to subsidize the creation of new jobs, new payroll, and new capital investment. These programs inherently cannot support the retention of major employers and their corresponding on-going generation of tax revenues in a state. Even the payroll rebate and deal closing fund programs previously discussed focus on net new business recruitment.

According to the CBRE Economic Incentives Group, there are only six state incentive programs specifically designed to target business retention. These best practices are found in Illinois, Indiana, Kentucky, Michigan, New Jersey, and Ohio.

Business Personal Property Tax Exemption

Recognizing the need to help reduce a company's total cost of doing business, about 10 states have statutorily eliminated ad valorem taxes on business personal property for commercial and industrial uses. This means that neither a municipality, county, or school district accrue property tax revenue from business personal property. The statutorily exempt states include Delaware, Illinois, Iowa, Kansas, Minnesota, New York, New Jersey, Ohio, North Dakota, and South Dakota.

Tax Increment Financing

Forty-nine states and the District of Columbia have enabled the use of Tax Increment Financing (TIF) for qualified economic development opportunities. Arizona is the only state without a tax increment financing law.

Tax Increment Financing allows cities to help offset a company's start-up investment by capturing increased property tax revenues generated by economic development projects. These tax revenues are used to pay back city funds (with interest) injected at the front end of the development of new industrial or commercial facilities. TIF may be used to offset the cost of public improvements and utilities that will serve the new private development, to finance direct grants or loans to a company, or to provide the local match for federal or state economic development assistance programs. TIF has been an effective economic development tool because infrastructure improvements do not leave if a company chooses to leave. Infrastructure improvements funded by TIF are a perpetual benefit.

Final Points

Arizona's competitive disadvantage regarding its economic development programs lies in three primary areas: 1) the lack of strategic focus within its economic incentive programs; 2) the marketing of those programs and location successes; and 3) the perceived lack of leadership and overall economic governing strategies.

Policymakers must propose the creation of new, self supportive economic development programs *along with* accompanying tax law modifications and then provide support with a long term commitment to quality growth in the State. Any new incentive program that is dependent on business investment and job creation needs to be closely monitored.

Monitoring programs is critical. If a business does not perform as expected, "clawback" provisions should be used to recoup a portion of State incentive expenditures. The new programs should also be reviewed on a regular basis to ensure that they are working as intended and providing a benefit to Arizona. Therefore, sunset review provisions are also recommended. Since multiple programs are being recommended, it is also critical to assure that no "double dipping" of incentives occurs. In other words, in some cases, the relocating or expanding company may need to select only one program to utilize. It may also be worth while to design some form of a cap on select programs until they are later evaluated for effectiveness.