Tools in the Toolbox: How Incentive Grant Programs Work

With the advent of the William S. Lee Quality Jobs and Business Expansion Act, the N.C. Department of Commerce has attempted to arrange its financial programs and incentives in a sort of one-stop toolbox called the Commerce Finance Center.[1] Here are the major compartments in the Commerce toolbox and the tools within each compartment:

Tax Credit Programs: These include job creation tax credits, machinery and equipment investment tax credits, research and development tax credits, and worker training tax credits. The most publicized of these is the *job creation credit*, which ranges from $12,500 per job created in the state's most distressed counties to $500 in its most affluent. Firms must certify that they have met the job creation requirements before they can claim the credit, which can amount to no more than 50 percent of a firm's franchise or income tax liability. Like the job creation tax credit, the *machinery and equipment investment tax credit* is most generous in the state's poorest counties. Eligible firms may claim a credit of 7 percent of their investment above a certain threshold. The amount of the threshold rises with the affluence of the county. The state's most prosperous counties—the so-called Tier 5 counties—have a threshold of $1 million, while the poorest (or Tier 1) counties have a threshold of $0. The *research and development tax credit* piggybacks on the federal research and development tax credit program, giving firms that qualify for the federal program a 5 percent credit for the state's apportioned share of the investment. Finally, the *worker training tax credit* gives firms a credit for up to 50 percent of eligible training expenses, with credits of as much as $1,000 per worker trained in the state's poorest counties and a $500 per worker cap in the remaining counties. A common characteristic of all of the tax credit programs is that the state does not write a check to the firm. Instead, the credit reduces the tax liability of the firm, and the firm must document that it has met the requirements of a particular program to claim the credit.

Loan and Grant Programs: These include community development block grants, an industrial development fund, and business energy loans. *Community development* funds may be awarded only to local governments for proposed projects that involve specific businesses that create new jobs or retain existing jobs. Most of the jobs must benefit low- or moderate-income citizens. The community development program also contains a microenterprise loan component to assist small business, but again, there must be a local government applicant willing to administer the program. *The industrial development fund* aims to assist the state's most distressed counties (53 of 100 counties are currently eligible) by providing loans to local government. These can be used to rehabilitate existing manufacturing facilities or provide infrastructure such as water and sewer to a new site. Projects are undertaken by local government on behalf of an industrial prospect. The amount available is determined by multiplying $4,000 times the number of jobs to be created, with a ceiling of $400,000 on the cost of the project. In most cases, a 25 percent local match is required, although this can be waived in cases of extreme distress. For the most severely distressed counties, there is a special *utility account* program for construction of or improvements to existing water, sewer, gas, or electrical lines. Finally, there is the *business energy improvement program,* which provides low-interest loans of up to $500,000 for energy conservation-related improvements at new and existing businesses.

Industrial Revenue Bonds: These include tax exempt, taxable, and pollution control/solid waste disposal bonds.[2] Tax exempt bonds are limited to no more than $10 million in any local jurisdiction but carry the lowest interest rates because payments to bond holders are free of state and federal taxes. Taxable bonds carry a slightly higher cost to the borrower because they do not exempt the bondholder from federal taxes, but they can be issued for amounts in excess of $10 million. Pollution control/solid waste disposal bonds are tax exempt and there is no restriction on amount. All three bond programs work in similar fashion. The state supervises, approves, and guides bond applications, but the bonds are issued by the county bond authority where the facility will be located. Three principal rules governing these programs are: (1) firms must be engaged in manufacturing; (2) bond proceeds can be used only for land, building, equipment, and issue costs; and (3) the company must agree to pay its employees at least the average weekly manufacturing wage of the county or the state average weekly manufacturing wage plus 10 percent.

The Governor's Industrial Recruitment Competitive Fund: With the expansion of the state's tax credit program, the Governor's Industrial Recruitment Competitive Fund has shrunk. Established at $5 million in the 1993–94 fiscal year, the fund has contracted to $1 million for 1997–98. As a result, winning a grant from the fund is now a competitive process. Grants are available for up to $1,000 per job created but may not exceed $100,000. The payment goes not to the industry itself but to a local government entity, which must match the grant on a dollar-for-dollar basis. Firms must prove they have created the jobs before they receive any payment. Clawback provisions protect the state's investment in case a firm fails to live up to the terms of its agreement.

Other Local Programs: Also of increasing importance in North Carolina are local programs aimed at wooing industrial prospects. One of the more aggressive programs is the Cabarrus County incentives grant program under which firms meeting investment thresholds can receive a grant equal to a portion of their tax payment. Other counties and municipalities have emulated this program, which, if challenged, may or may not pass constitutional muster. Tax abatement programs are unconstitutional in North Carolina,[3] but grant payments to companies for industrial projects apparently are not.[4] The gray area in the Cabarrus case is use of the property tax payment to determine the amount of the grant, according to David Lawrence, a faculty member at the University of North Carolina at Chapel Hill's Institute of Government. Other local incentives have included payments for everything from parking decks and spousal relocation expenses to land, buildings, and water and sewer line extension.

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FOOTNOTES

[1] Further information on the Commerce Finance Center may be obtained from the N.C. Department of Commerce website at http://www.commerce.state.nc.us.

[2] For more on industrial revenue bonds, see Bill Finger and Donald E. Horton Jr., "Tax-Exempt Bonds for Manufacturers: How Effective in North Carolina?" *North Carolina Insight*, Vol. 9, No. 2 (September 1986), pp. 2–17.

[3] Article V, Sec. 2 (1) of the North Carolina Constitution.

[4] See *Maready v. City of Winston-Salem*, 342 N.C. 708, 467 S.E.2d 615 (1996), in which the state Supreme Court ruled that local governments have broad latitude to grant incentives for economic development.