



Business Incentives and Economic Development Expenditures: An Overview of Tennessee's Program Investments and Outcomes

Summary

Across the country, state economic development incentives have evolved into a complex mixture of programs with diverse structures and goals. The Council for Community and Economic Research (C2ER) and the Center for Regional Economic Competitiveness (CREC) have been working to catalog and document the range of available state programs through the [C2ER State Business Incentives Database](#), which features detailed information about nearly 2,000 state-administered incentive programs; and the [C2ER State Economic Development Expenditures Database](#), a compilation of economic development expenditure data from every state. This report adds to that body of work by exploring Tennessee's complete catalog of incentive programs, including an analysis of the available outcome data used by state policymakers and program administrators to evaluate program effectiveness.

The [Center for Regional Economic Competitiveness \(CREC\)](#) is working with The Pew Charitable Trusts (Pew) on the Business Incentive Initiative. This initiative engages forward-thinking teams of economic development policymakers and practitioners from six states, including Tennessee. These leaders are working together to identify effective ways to manage and assess economic development incentive policies and practices, improve data collection and reporting on incentive investments, and develop national standards. The initiative is supported by a grant from the Laura and John Arnold Foundation.

To form a better understanding of the economic development landscape in Tennessee, we examined data from a range of state statutes, reports, and websites, including annual tax reports and annual state budgets. The numbers cited in this report are CREC and C2ER's best estimate of the dollars spent on economic development incentives at the state level in Tennessee.

In FY 2015, the most recent year for which spending data are available, Tennessee has proposed to spend \$173 million on economic development program expenditures, and spend an estimated \$608 million on economic development tax expenditures.¹

Overview of Business Incentives

Tennessee administers a moderate number of incentive programs, with a total of 25 active programs in 2014.² The C2ER State Business Incentives Database defines state business incentives as state-administered programs designed to influence business investment behaviors. States design their programs to influence these behaviors through tax incentives as well as through non-tax programs such as grants, loans, business assistance, and other investment vehicles. These incentives help businesses

¹ See Appendices for detailed lists of all items included in this report as incentives, economic development program expenditures, and economic development tax expenditures.

² Please note that data regarding state spending on economic development was gathered through reviewing state budget publications. This data is not linked to the individual business incentives described in this section.



address one or more needs, such as capital access, workforce preparation, technology transfer, site facility improvements, and so forth.

Figure 1: Tennessee State Business Incentives by Agency, 2014

Agency	Number of Programs
Tennessee Department of Economic and Community Development	10
Tennessee Department of Revenue	10
Tennessee Department of Transportation	2
Film, Entertainment & Music Commission	1
Launch Tennessee	1
Tennessee Department of Labor and Workforce Development	1

Source: C2ER State Business Incentives Database

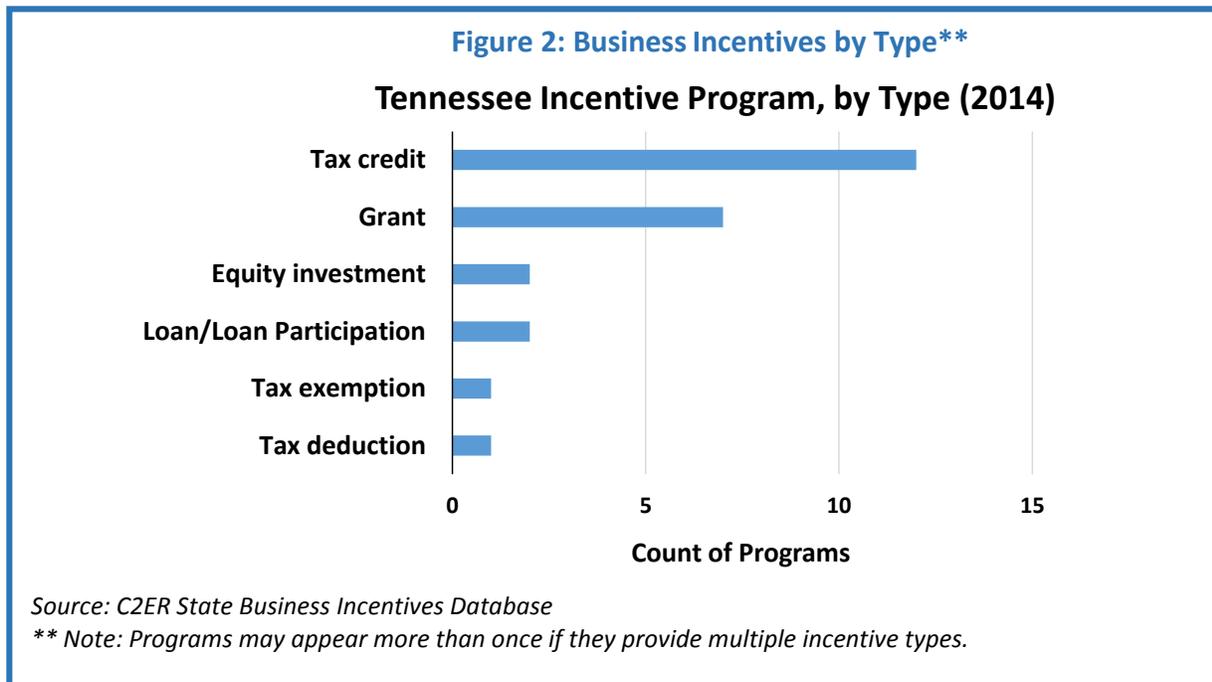
Tennessee incentive programs are currently administered by six different state agencies. The Tennessee Department of Economic and Community Development (ECD) and the Tennessee Department of Revenue (DOR) administer the majority of the state's business incentives. (See Figure 1.) Other state agencies and public-private partnerships, such as Launch Tennessee, are responsible for managing a small number of incentive programs. (See Figure 1.)

Soon after Governor Haslam took office in 2011, ECD conducted an internal review to evaluate its incentive programs against best practices in economic development. This review found that the state's suite of incentives lacked coherence, in part because of an accumulation of incentives that had been enacted over the years to serve short-term purposes. Since the review, ECD has made a conscious effort to improve transparency and efficiency in administering its business incentives.

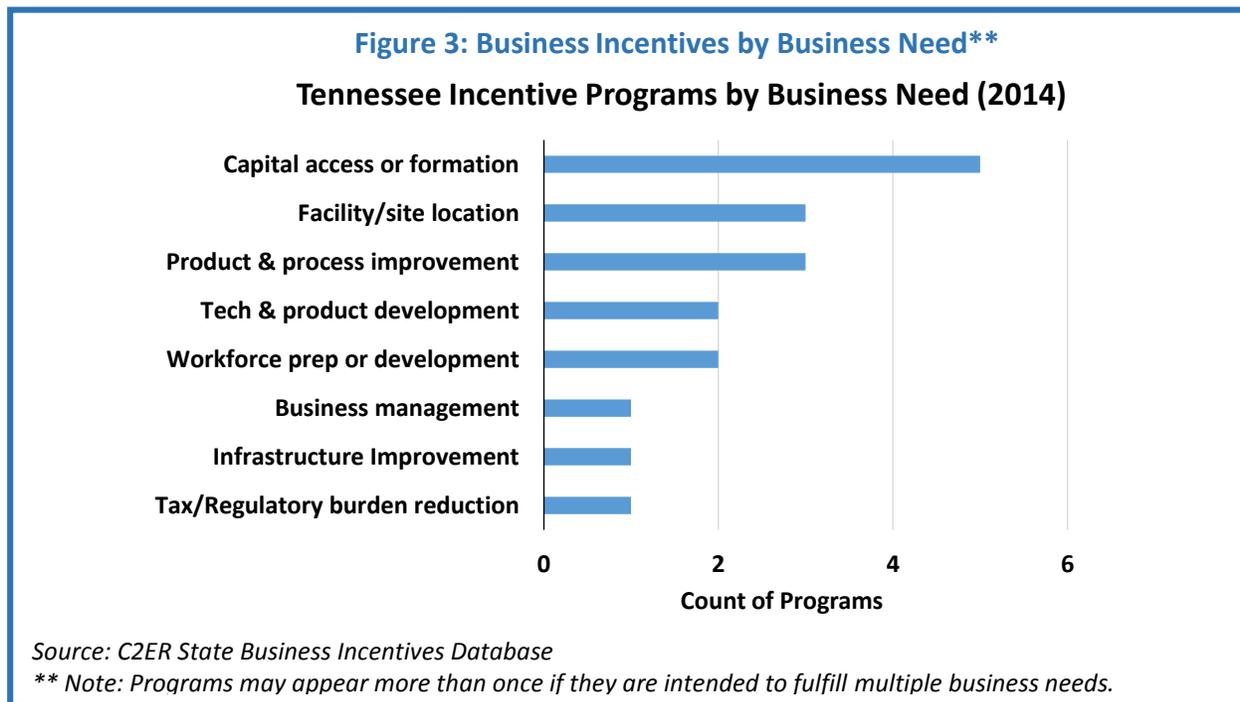
For example, in 2012, Tennessee enacted a law to replace business development grants, informal awards subject to little oversight by state officials and the public, with the FastTrack Economic Development Grant Program. FastTrack, a pay-for-performance grant program, requires companies that apply for funding to provide detailed information to assist ECD in making informed decisions about how to most effectively pursue the state's economic development goals. The program offers selected companies training, job-creation, and infrastructure assistance.

ECD's review also found that Tennessee was lagging many other states in its efforts to share information about economic development incentives with the public. Because transparency and reporting on incentive awards are central to public trust, ECD created a new website, [OpenECD](#), which includes a brief description and award amount offered for each state incentive and grant.

As part of the FastTrack program, Tennessee now performs rigorous due diligence as part of the application process for companies requesting funding. As a result, there has been more emphasis on assessing applicants' financial capacity and investigating the incentives a company has claimed in other states and localities. This additional data enables ECD to make more informed decisions about the types of grants that will help achieve the state's economic development goals and ensure that standard contractual deliverables can be met.



Currently, 76 percent of Tennessee’s active incentive programs offer direct business financing benefits. About half of the programs provide tax benefits and 23 percent offer indirect financing. (See Figure 2.) The most common business needs addressed by these programs are access to capital, facility location, product and process improvement, technology and product development, and workforce development. (See Figure 3.)





Economic Development Program Expenditures

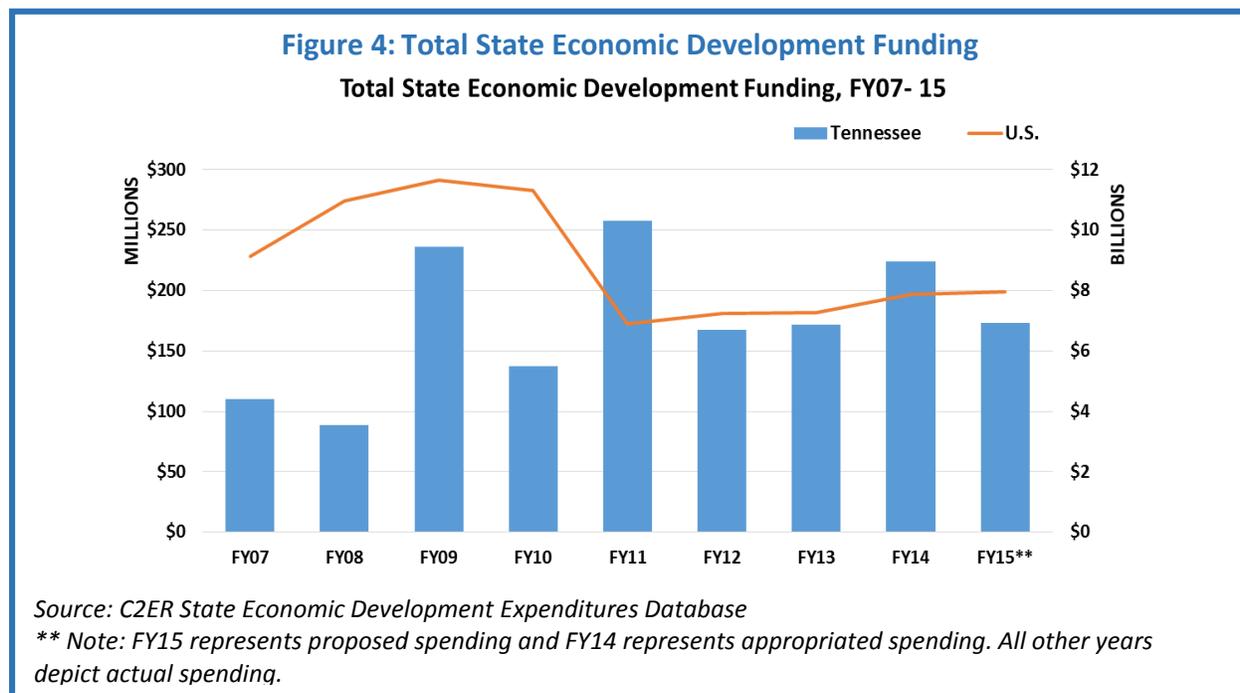
Examining Tennessee’s state budget reveals how various state agencies outlay money for economic development programs. Expenditures fall into 15 functional areas for economic development, defined by the C2ER State Economic Development Program Expenditures Database.³

According to the [FY 2015 Tennessee Proposed State Budget](#), the state is projected to spend \$173 million on economic development in FY 2015. (See Figure 4.) This means the state is projected to spend approximately \$1,194 per business establishment, which is above the national average investment of \$972 per business for that fiscal year.

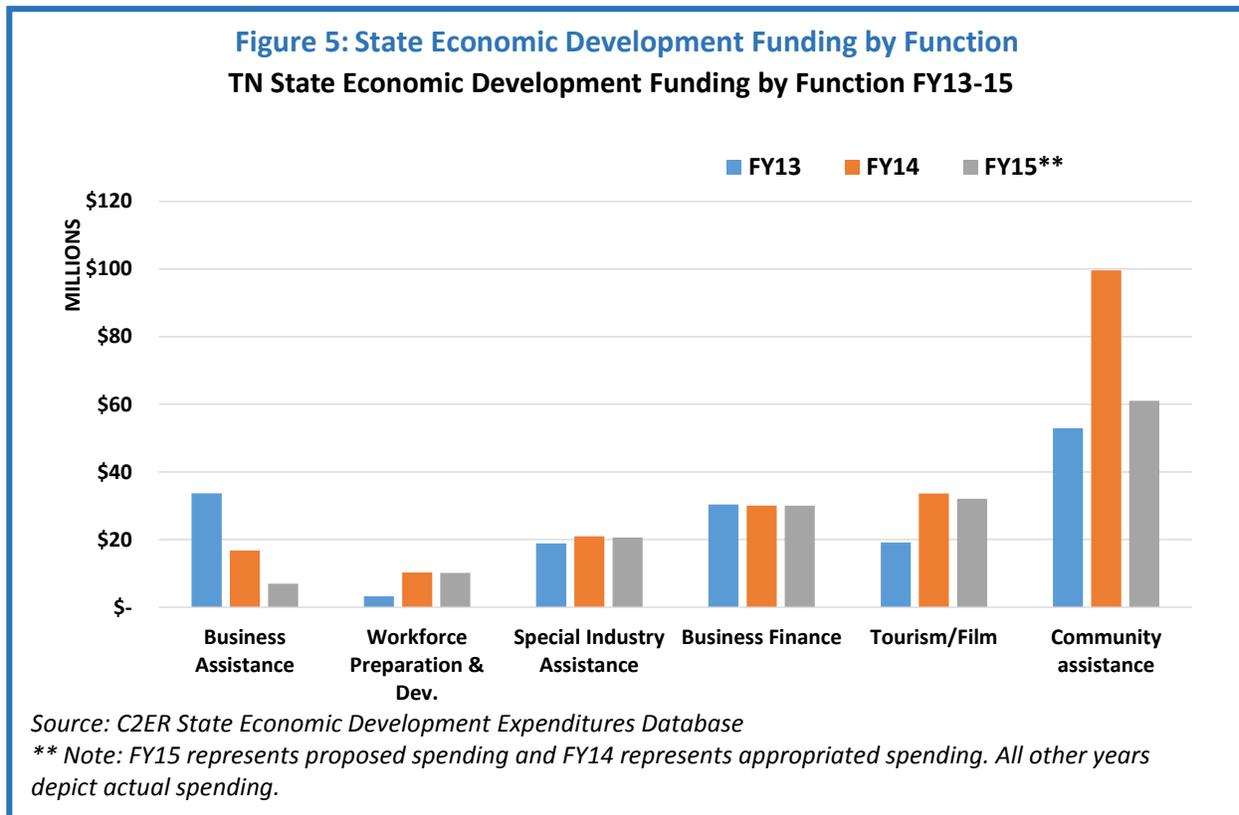
State Economic Development Expenditures Function Areas

- Business Finance
- Strategic Business Attraction Fund
- Business Assistance
- International Trade and Investment
- Domestic Recruitment/Out-of-State
- Workforce Preparation & Development
- Technology Transfer
- Entrepreneurial Development
- Minority business development
- Community Assistance
- Tourism/Film
- Special Industry Assistance
- Program Support
- Administration
- Other Program Areas

Tennessee has not always followed national trends in economic development spending. From FY 2008 through FY 2010, economic development spending rose in many states, before falling sharply in FY 2011.



³ See Glossary definitions here - http://www.stateexpenditures.org/about/Definition_of_ED_Functions.pdf



By contrast, Tennessee’s economic development funding reached its lowest point in FY 2008 – prior to the onset of the Great Recession. In FY 2011, as the majority of states reduced their spending on economic development, Tennessee increased its funding by \$120 million, an 87 percent jump from the previous year. Since FY 2012, economic development funding has more closely followed national trends. For FY 2015, the state has proposed (referred to in the budget document as “recommended”) to decrease funding from FY 2014 levels of appropriated spending (referred to in the budget document as “estimated”).

Compared to other states in FY 2015, the state is proposing to spend a higher proportion of its economic development budget than the average for other states in the functional areas of business finance, community assistance, and tourism and film. Tennessee is proposing to spend a lower proportion of its economic development budget than the average for other states on workforce preparation and development, technology transfer, program support, and business assistance.



Economic Development Tax Expenditures

Tax expenditures can be defined as “revenue losses attributable to tax provisions that often result from the use of the tax system to promote social goals without incurring direct expenditures.”⁴ *Economic development tax expenditures* in this context represent those tax provisions that use the state tax system to promote business investments that promote state economic priorities.

Each year, the Tennessee Department of Finance and Administration (DOFA) reports to the Tennessee House and Senate Finance and Ways and Means Committees on two areas of finance: 1) tax exemptions and 2) vendor compensation for the collection of the sales tax. DOFA, with the assistance of DOR, publishes the estimated revenue losses from tax expenditures within the state’s annual budget proposal. The report outlines the fiscal impact of Tennessee’s major tax exemptions and revenue foregone on services not currently taxed. These services represent activities that were not included in the original tax base. Each exemption is considered separately without regard to how it overlaps with other provisions of the tax code and the estimates of revenue provided do not reflect secondary or feedback effects.

According to the FY 2015 Tennessee Proposed State Budget, Tennessee is projected to forego \$608 million in economic development tax expenditures in FY 2015. Sales and use tax exemptions for economic development (\$487 million) account for 80 percent of the state’s total projected loss of revenue, while corporate franchise and excise tax credits and exemptions for economic development account for the remaining 20 percent (\$122 million). Around 90 percent of tax expenditures were directed toward businesses in the manufacturing and agricultural industries.

Analysis of Available Outcome Data

The Tennessee legislature currently does not regularly evaluate its business development tools. According to the [State Economic Development Incentives Survey](#) conducted by C2ER, which covered all fifty states, approximately 70 percent of state program respondents collected data on program impact or performance data for reporting purposes on either a regular basis or occasionally.

However, ECD and DOR have committed to improving administrative practices to ensure the state secures its return on investment while remaining business-friendly. ECD and DOR staff collaborate to make decisions on incentive applications and review program results. Through this arrangement, ECD and DOR staff are able to share data that aggregate the amount of tax credits claimed in a fiscal year by industry. This cooperation aids in comprehensively managing in the state’s entire portfolio of incentives and planning for future awards.

Taking a data-driven, evaluative approach to understanding what works best for the state’s economy controls for unintended consequences that often stem from outdated programs and an evolving economy. To address these issues, in February 2015 Governor Haslam introduced legislation to repeal several little used tax credits. Moreover, he also introduced another piece of legislation requiring a review of the state’s economic development tax credits. Gathering pertinent data and asking the right

⁴ *Tax Expenditures: What are they and how are they structured?* Tax Policy Center. Accessed November 25, 2014 at: www.taxpolicycenter.org/briefing-book/background/shelters/expenditures.cfm



questions about the value of incentive programs provides evidence for improving the mechanisms the state has at its disposal.

Conclusion

Tennessee's economic development structure is evolving. The state has undergone internal reviews of its policies in hopes of developing a cohesive long-term economic development strategy that objectively evaluates the effectiveness of each state incentive program. In addition, two new pieces of legislation have been introduced to make the state's portfolio of economic development tax credits more coherent and to ensure that they are achieving their intended outcomes. The state is moving toward making data more accessible to stakeholders involved in the policy-making process. The state's incentive portfolio favors grants and tax credits for improving infrastructure and increasing business' access to capital. Consistent with Governor Haslam's priorities, Tennessee continues to develop more fiscally responsible methods to grow its economy and provide both executive and legislative officials with the information needed to make sound policy decisions.



Appendix A: Full List of TN State Business Incentives (2014)

Program Name	Program Provider	Business need	Type
Tennessee Film/TV Incentive	Film, Entertainment & Music Commission	Business management	Grant
The INCITE Co-Investment Fund	Launch Tennessee	Capital access or formation; Tech & product development	Equity investment
FastTrack Economic Development Fund	Tennessee Department of Economic and Community Development	Facility/site location	Grant
FastTrack Infrastructure Development Program (FIDP)	Tennessee Department of Economic and Community Development	Facility/site location; Infrastructure Improvement	Grant
FastTrack Job Training Assistance Program (FJTAP)	Tennessee Department of Economic and Community Development	Workforce prep or development	Grant
Integrated Supplier and Integrated Customer Tax Credit	Tennessee Department of Economic and Community Development	Capital access or formation; Workforce prep or development	Tax credit
Jobs Tax Credit	Tennessee Department of Economic and Community Development	Capital access or formation; Workforce prep or development	Tax credit
Jobs Tax Super Credit	Tennessee Department of Economic and Community Development	Capital access or formation; Workforce prep or development	Tax credit
Rural Small Business and Entrepreneurship Loan Fund	Tennessee Department of Economic and Community Development	Capital access or formation; Product & process improvement	Loan/Loan Participation



Small Business Energy Loan Program	Tennessee Department of Economic and Community Development	Product & process improvement	Loan/Loan Participation
TNInvestco Program	Tennessee Department of Economic and Community Development	Capital access or formation	Equity investment
Wind Energy Systems Exemption	Tennessee Department of Economic and Community Development	Product & process improvement; Tax/Regulatory burden reduction	Tax exemption
Tennessee Job Service	Tennessee Department of Labor and Workforce Development	Workforce prep or development	Grant
Carbon Charge Tax Credit	Tennessee Department of Revenue	Tech & product development	Tax credit
Data Center Tax Credit	Tennessee Department of Revenue	Capital access or formation; Facility/site location	Tax credit
Emerging Industry Tax Credit	Tennessee Department of Revenue	Capital access or formation; Product & process improvement	Tax credit
Green Energy Tax Credit	Tennessee Department of Revenue	Capital access or formation; Tech & product development	Tax credit
Headquarters Tax Credit	Tennessee Department of Revenue	Capital access or formation; Facility/site location	Tax credit
Industrial Machinery Tax Credit	Tennessee Department of Revenue	Capital access or formation; Product & process improvement	Tax credit
Pollution Control Equipment Tax Credit	Tennessee Department of Revenue	Capital access or formation; Product & process improvement	Tax credit
Reduced Tax on Electricity	Tennessee Department of Revenue	Capital access or formation; Product & process improvement	Tax deduction
Rural Opportunity Initiative Enhanced Job Tax Credit	Tennessee Department of Revenue	Capital access or formation; Workforce prep or development	Tax credit



Sales and Use Tax Credit for Qualified Facility to Support an Emerging Industry	Tennessee Department of Revenue	Capital access or formation; Facility/site location	Tax credit
Green Island Corridor Grant Program	Tennessee Department of Transportation	Capital access or formation; Product & process improvement	Grant
State Industrial Access Program	Tennessee Department of Transportation	Facility/site location; Infrastructure Improvement	Grant



Appendix B: TN Economic Development Program Expenditures (2015)

Function	Activity	Total State Funding
Administration	Info systems, accounting, human resources, etc.	\$6,049,300
Business Assistance	Business retention/expansion	\$6,906,200
Business Finance	Other Business Finance	\$30,000,000
Community assistance	Community development	\$1,933,900
Community assistance	Funding for targeted geographic zones	\$1,530,100
Community assistance	Grants to local/regional dev. orgs.	\$546,000
Community assistance	Infrastructure (e.g., road/sewer)	\$56,985,400
Domestic Recruitment/Out-of-State	Other Domestic Recruitment/Out-of-State	\$6,000,000
Special Industry Assistance	Agriculture/agribusiness	\$20,612,900
Technology Transfer	Other Technology Transfer	\$237,700
Tourism/Film	Film Promotion	\$6,048,600
Tourism/Film	Other Tourism/Film	\$9,484,600
Tourism/Film	Tourism promotion (exc. Advertising)	\$16,529,400
Workforce Preparation & Dev.	Customized training	\$78,000
Workforce Preparation & Dev.	Incumbent worker training	\$5,285,200
Workforce Preparation & Dev.	Other Workforce Preparation & Dev.	\$4,766,500



Appendix C: TN Economic Development Tax Expenditures (2015)

Description	Total Funds
Cap on value of inventories (Franchise)	\$23,600,000
Certain warehouse equipment	\$4,800,000
Energy and water sales to manufacturers. for direct processing (exempt)	\$51,400,000
Energy and water sales to manufacturers (reduced rate)	\$178,400,000
Fertilizers, pesticides, seeds, and related items to nurseries	\$8,200,000
Gasoline/diesel fuel for agriculture	\$17,400,000
Industrial and farm machinery and equipment	\$225,600,000
Industrial machinery credit (Franchise and Excise)	\$55,700,000
Jobs credit (Franchise and Excise)	\$42,500,000
Used factory-manufactured structures	\$ 800,000