Ohio Basic Economic Development Course:

Finance and Incentives

Mark Barbash
John Glenn College, The Ohio State University
Mark.Barbash@gmail.com
Quinten Harris, JD MPA
Deputy Director, City of Columbus Department of Development
QLHarris@Columbus.gov

Overview of Session

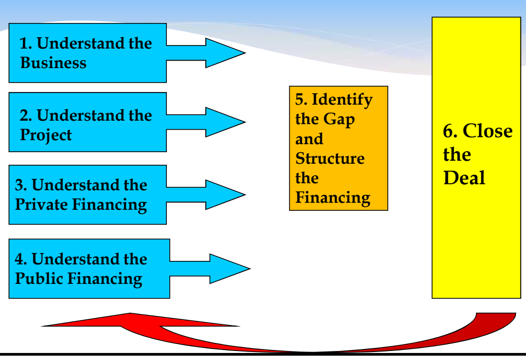
- Finance
  - Basics of Financing
  - Financing Continuum
  - Ohio Financing Programs
  - Current Issues
- Incentives
  - Principles of Incentives
  - Types of Local and Ohio Incentives
  - Current Issues in Incentives

Part One: Financing

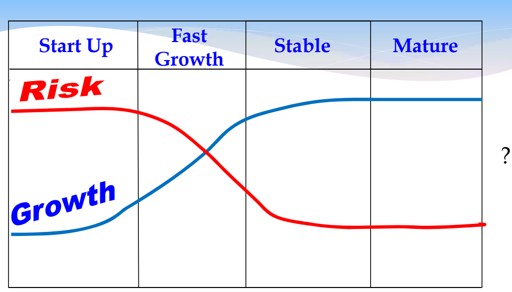
Economic Development Financing

- Financing as a step in the Development Process
- Private Financing
- Working with Bankers
- Public Sector & Non profit Financing
- Types of Public Sector Programs
- Tax Incentives

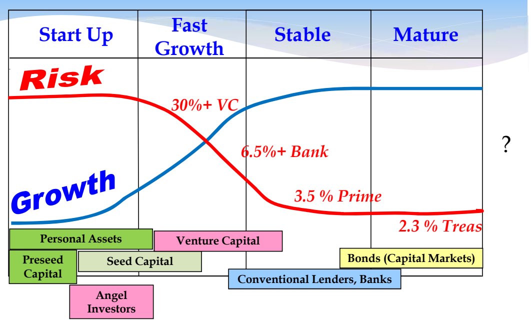
Steps in the Development Financing Process



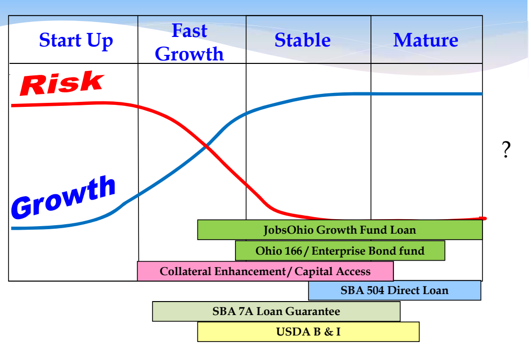
Business Lifeline



Private Sector Financing



Public Sector Financing



Profile of Private Investors

- Types of Investors:
  - Who provides funds for investment
- Risk Level:
  - How much risk will be taken
- Control of Business:
  - How much control of business desired
- Type of Investment:
  - What is the format of the investment

Private Investor Profiles

	Investors	Risk	Control	Investment
Seed Capital	Individuals, Local funds, Foundation	Extremely high (20 – 30%), most lose money	Informal process, Very high control	Ownership, Out quickly to VC
Venture Capital	Managed VC funds & SBICs	Very high (15 – 30%), 90% lose money	Formal process, high control	Ownership, Out 5–7 years through IPO
Banks +	Commercial banks and leasing cos.	Medium to low or 0 risk; Prime +	Very formal process, low control	Loans, leases per asset life, 3–20 yrs.
Capital Markets	Corporate/ Investment banks, insurance, REIT	No risk, Treasury rate return	Highly structured process, no control	Loans, leases based on asset life, 7 – 30 yrs.

REMEMBER…

All lenders and investors are money managers – nothing more and nothing less -- with different goals for return on investment based upon their source of funding.

It's Critical to Understand the Private Financing First

- **Use of Funds:** Real Estate, Equipment, Working Capital
- **Risk:** Higher the risk, the higher the rate
- **Interest Rate:** Fixed, Variable
- **Term of Loan:** Term of Loan = Live of Asset
- **How much equity required:**
- **Collateral Required:** Mortgages, Liens, Guarantees

Financing Gaps

- **Cash Flow Gap:** Insufficient cash generated to pay debt service on financing
- **Collateral Gap:** Cash flow is sufficient to make payments, but the collateral doesn't support the amount of the private sector financing
- **Credit Gap:** Start up business with insufficient history to support private financing
- **Character Gap**

How public sector programs help fill the financing gap

- Guarantee risky credits or lower value collateral
- Long Term Financing
- Fixed Rate Financing
- Lower down payment financing to preserve cash for working capital
- Lower rate financing
- Reduced Debt Service Needs
- Increased Borrowing Capacity
- Bring lower rate and long term financing through capital market bond financing (*tax exempt or taxable*)

The Nine Rules for Working with Private Lenders

1. **The Donald Trump Rule**
2. **The Al Capone's Safe Rule**
3. **The Henry F. Potter Rule**
4. **The George Steinbrenner Rule**
5. **The Herb Cohen Rule**
6. **The Berlitz Rule**
7. **The Scouts Rule**
8. **The Elephant Rule**
9. **The Don Quixote Rule**

Purpose of Public Sector Programs

- Achieve social or economic goals
  - Create or retain jobs
  - Assist specific groups of citizens or neighborhoods
- Leverage bank financing
- Fill a financing gap
- Reduce bank risk
- Finance non-bankable businesses
- Provide incentives for targeted investments

Understand Public Sector Financing

- Purpose of Public Sector Programs
- Types of Public Sector Programs
- Tax Incentives and TIFs
- Taxable and Tax Exempt Bonds
- Joint Economic Development Districts +
- Selecting the Public Sector Program
- Rules for Working with Public Sector Programs

Types of Public Sector Financing Programs

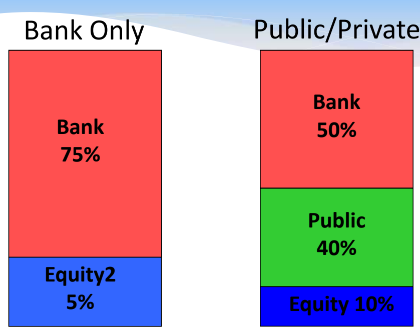
- Direct Loans
- Loan Guarantees
- Bonds: Taxable and Tax-Exempt
- Tax Incentives (Property Tax, Income Tax)
- Tax Increment Financing (TIF)
- Intermediary Programs: New Markets Tax Credits, CDBG, CDFI
- Hybrid Programs

Direct Loans

- Finance 30-50% of a Project Cost
- Fixed Interest Rates
- Terms Equal to or Longer than the Bank
- Loan is Subordinated to the Bank
- Reduced Business Equity Requirement (10%)
- Generally for Fixed Assets Only

- JobsOhio
- Ohio 166
- SBA 504
- Community Development Block Grants
- Intermediary Programs depending on local structure

How a Direct Loan Makes the Deal Better…



Loan Guarantees

- Guaranty of Bank's Loan
- Bank's Rate and Term
- Guaranty up to 85% of Bank Loan
- Can Finance Working Capital
- Alternative: Provide secured deposit

- SBA 7(a)
- SBA Community Advantage
- Collateral Enhancement Program
- Capital Access
- USDA Business and Industry Loan Program

Bonds

- Debt issued by local authorities
- Underwritten by investment banking firms
- Purchased by national capital market investors
- Better credit companies or
- Companies backed by bank Letter of Credit or other security
- Larger projects

Bond Programs

- Stand alone Industrial Revenue Bonds (Private Activity Bonds)
- Ohio Enterprise Bond Fund
- Port Authority Bonds
- Ohio Air Quality Development Authority
- Ohio Water Quality Bonds

Taxable and Tax-Exempt Bonds

Tax Exempt Bonds
- Finance public-benefit projects
- Job creation, housing, education, government, student loans
- Lenders of tax exempt bonds pay no income tax on interest earned
- Savings passed on to the borrower in the form of lower interest rates
- Typically very high "cost of issuance"

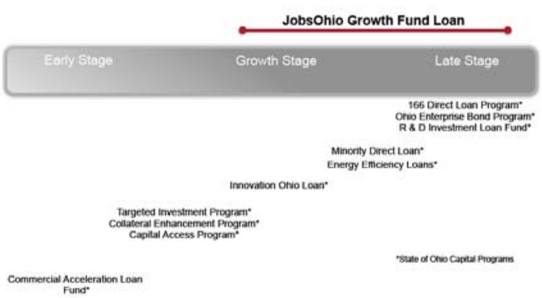
Taxable Bonds
- Can be used for almost any purpose
- Lenders pay tax on interest income
- No interest savings to the borrower other than the lower national market rates
- Better credits, larger issuances

Intermediary Programs

- Government provides funds or allocates tax credits to local economic development for relending
- Local group takes responsibility for policy, underwriting, marketing, processing and management of funds
- Local group assumes responsibility for funds management and repayment of funds to the government, if a loan

- EB 5 Financing
- SBA Microloan
- Regional 166
- CDBG
- New Markets Tax Credits
- Community Development Financial Institutions
- USDA Intermediary Relending
- SBA Intermediary Program

JobsOhio — Financing Continuum



JobsOhio — JobsOhio Growth Fund Loan

- Fixed Assets: Land, Building & Equipment
- $500,000 to $5,000,000
- Generally up to 50% of Total Project Cost
- Generally 10% Equity from Borrower
- Term: Real Estate – 15 years; Equipment – 10 Years
- Interest rate based upon investment risk

JobsOhio Growth Fund Grant

- Fixed Assets: Land, Building & Equipment
- Moving Costs
- Demolition
- Infrastructure / Rail access / Roadways
- Utilities
- Generally $100,000 to $500,000

Key Factors to Consider

- Emphasis on creation of new jobs, increase in payroll
- Return on Investment generally by year 3
- Targeted Industries
- Financial Strength of Company
- Average Wage at least 150% of federal minimum wage
- Utilities
- Generally $100,000 to $500,000

Part Two: Incentives

Purpose of Incentives

- Goal: Reduce operating costs or compensate for perceived market or locational disadvantages
- Tax Abatements:
  - Reduce the amount of property taxes owed
- Tax Credits:
  - Reduce taxes owned on income tax statements
- Tax Increment Financing
  - Redirecting property tax revenue to project costs
- Closing Funds
  - Grants for infrastructure, moving, investment

Overcome Locational Disadvantages

- Need for additional investment
- Higher costs vs. the market or vs. the business project specifications
- Costs for remediation of environmental contamination

Negotiating Incentives

- What do the rules say?
- What does your policy say?
- What precedents have been set with prior incentives to similar businesses?
- One voice for your community
- Research your customer
- Know your threshold of pain and be willing to walk away

How much is enough?

- "But for"
- Return on Investment
- Identified economic development priorities
- How much subsidy is too much subsidy?
- "Developer's Windfall"

Calculating the Value of…

- Income Tax Credit
- Property Tax Abatement
- New Markets Tax Credit

Calculating the …. ROI

- Return on Investment
  - How much are you spending
  - How much are you gaining from the project
    - Property Tax
    - Income Tax
    - Sales Tax
  - How much are you spending:
    - Value of incentives offered
    - Infrastructure Investment
- Return on Investment
  - Gaining – Spending = Net Growth
  - Gain / Spend = Return on Investment

Incentive Controversies

- Corporate subsidy
- Lack of transparency
- Lack of accountability
- Impact on "other" taxing jurisdictions
- Lack of cost/benefit analysis
- GASB 77
- www.smartincentives.com
- www.goodjobsfirst.org

Tax Credits

- If business spends funds for a specific purpose…
- … or creates new jobs
- Reduces taxes owed by a predetermined about
- Typically based:
  - % of investment or
  - % of tax liability
- Depends on tax liability of business

- Job Creation Tax Credit
- Job Retention Tax Credit
- Film Tax Credit
- New Markets Tax Credits
- Historic Preservation Tax Credits

Ohio Job Creation Tax Credit

- Ohio Tax Credit Authority
- Primary measures: Jobs and Payroll
- Refundable tax credit
- Minimum Payroll: $660,000
- Max: 75% for up to 15 years
- Must pay 150% of federal minimum wage
- Percentage of state income tax withholdings
- Applied to Commercial Activities Tax (CAT)

Motion Picture Tax Credit

- Payroll and productions costs for a motion picture, TV or digital production in Ohio
- Refundable, Transferable
- Maximum: 30% of production costs and crew wages
- Minimum $300,000 investment
- Ohio Development Services Agency

Job Retention Tax Credit

- Tax credit for existing company job retention
- Must retain at least 500 jobs
- Must maintain operations in Ohio
- Payroll of at least $35 million
- Minimum Investment:
  - $50 million for manufacturing
  - $20 million for corporate / professional services
- Non refundable, against CAT or person Income taxes

Property Tax Abatements

- Reduction in taxes owed based upon eligible investment, job creation
- Based on:
  - Eligible investment
  - Property tax value increase

- Community Reinvestment Area
- Enterprise Zone
- Federal HUB Zones

Enterprise Zone (EZ)

- Property tax abatement for real estate and building investment.
- Designation of geographic area where EZ incentives will be available.
- Maximum: 75%/10 Years in Cities, 60%/10 years in unincorporated areas
- If School District approves, can go up to 100% / 15 years
- Generally project by project

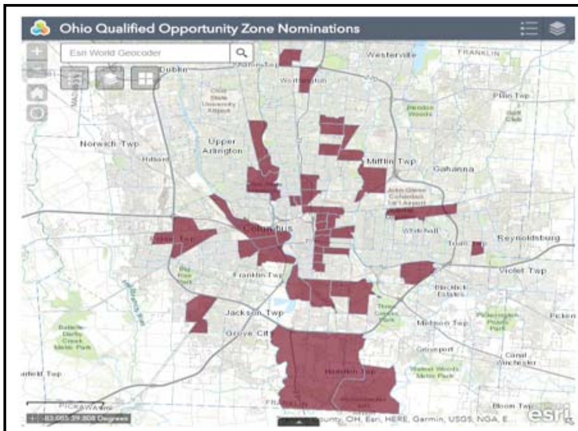
- Enterprise Zone agreement with business specifies required commitments to investment, jobs, project details and level of incentives

Community Reinvestment Area (CRA)

- Property Tax Abatement
- Designation of CRA area where abatements apply to all investments.
- Used **primarily** for residential incentives but used for commercial projects as well...
- Typical rate and term is 50%/15 Years
- School district OK required for abatement over 50%

Opportunity Zone (New)

- Provides for Capital Gains Exemptions
  - Deferral of Gain by 2026
  - Step Up in Basis by 10% if held for 5 years
  - Exclusion of Gains if held for 10 years
- Investment in Designated Opportunity Zones
- Apply for OZ Status through State; Deadline was 03/31/2018

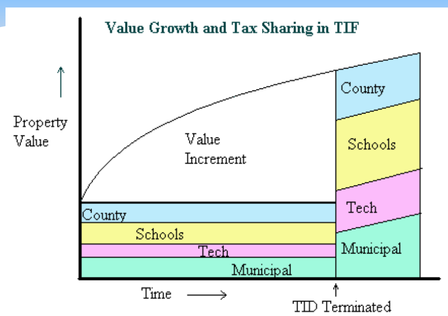


Tax Increment Financing

- Purpose is to generally finance infrastructure
- Source of Funds: Tax revenue redirected to eligible costs
- Based on a district or a specific project
- Funded through “pay as you go” or by issuing bonds

- Key Challenges:
  - Assumes increase in value as a result of new investment
  - Controversial because of impact on other taxing jurisdictions (Schools, Library, etc.)
  - Developer still pays; funds go to the project

How does TIF work?



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Collaboration for Economic Development

- Intended as a way for two or more jurisdictions collaborate to support an economic development project
- Municipalities & one or more townships
- Agreement to share revenue and expenses
- Ability to levy an income tax in a township, if partnering with a city that currently has an income tax
- If unanimous trustee vote, no referendum

- Joint Economic Development Districts (JEDDs)
- Joint Economic Development Zones (JEDZs)
- Cooperative Economic Development Agreements (CEDA)
- Annexation Agreements
- Community Improvement Corporation
- Other Agreements

Conclusion

How to Determine If Its A Real Deal on the First Visit

1. Are they willing to provide business and personal financial statements?
2. Are they willing to provide references?
3. How do they respond to challenging "devil's advocate" questions?
4. Is their answer always "Someone Else is in Charge?" and do they blame everyone else for their problems?
5. Do they expect "free money?"
6. Do they have a realistic assessment of the market, competition and job creation potential?
7. Are they willing to spend money up front?

Rules for Economic Development Professionals

1. Allow the business to tell their story…once;
2. Don't waste time with a dog;
3. Not all projects can fit with public sector programs;
4. Let the program people represent their program;
5. Don't overpromise what the program can deliver;
6. Don't pile on government programs;
7. Explain the strings up front;
8. Find a cooperative lender;
9. Keep written records of your activities;
10. Be prepared to do the paperwork;
11. If it sounds too good to be true, it probably is;
12. Take informed risk!

Contact information

Mark Barbash
Mark.barbash@gmail.com
(614) 774-7599

Quinten Harris, JD/MPA
QLHarris@Columbus.gov
(614) 645-0772