Commonwealth of Virginia
Economic Development Incentives

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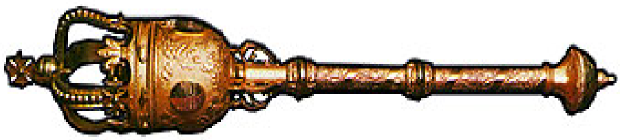
House Appropriations Committee

November 19, 2019



Virginia Scored 1,610 points out of a possible 2,500 with the highest marks coming in workforce & education

- Workforce (1)
- Economy (16)
- Infrastructure (13)
- Cost of Doing Business (35)
- Quality of Life (17)
- Education (1)
- Technology & Innovation (17)
- Business Friendly (3)
- Access to Capital (15)
- Cost of Living (32)

Commonwealth of Virginia is Competitive

- In July 2019 Virginia regained its status as the best state in the country to do business in the annual CNBC rankings that placed the state No. 1 for the first time in eight years
- The financial news cable network extolled **Virginia's "world-class workforce, high-performing education system and business-friendly regulations"**
- Others: TX (2nd), NC (3rd), UT (4th), WA(5th), GA(6th), OH (10th), IN (11th), TN (13th), NY (27th), PA (28th), MD (31st), SC (34th), AL (37th), KY (39th)

Various Forms of Incentives are Used to Spur Economic Development

- Economic development incentives make up for potential shortcomings in a State's portfolio and give state and local governments an extra edge when under consideration for a project
  - Incentive programs may reduce the potential costs incurred by companies to open or expand business facilities by providing needed infrastructure, workforce training, and site preparation
- When effectively designed and structured, incentive programs stimulate economic development through enhancing a State's attractiveness by complementing its strong economic fundamentals, such as workforce, education and regulatory environment
- Tax preferences and grant programs are the most commonly-used forms of economic development incentives
  - Loans and gap financing programs complement tax and grant incentive programs by helping companies secure additional debt and equity financing

Types of Tax Preferences & Features Offered to Companies

Type of tax preference	How incentive works	Possible features
▪ Income tax credits	▪ Reduce company’s state income tax liability	▪ To be usable by companies with low or no tax liability, may be: ▪ Carried forward/back against tax liability in other periods ▪ Refundable and reimbursable ▪ Transferable to other companies
▪ Income tax structure	▪ Offers preferential state income tax treatment relative to other industries (e.g. data centers single sales factor apportionment), other states (e.g. market-based sourcing), etc.	
▪ Income tax exemptions	▪ Exempt company’s income from state taxation	▪ Can be partial (e.g. temporary, above income threshold) or complete (e.g. not-for-profits)
▪ Income tax subtractions and deductions	▪ Reduce company’s state taxable income	
▪ Sales and use tax exemptions	▪ Exempt company’s purchases from state and local sales and use taxes	▪ Can be limited to specific taxable items (e.g. manufacturing equipment) and/or partial (e.g. reduced rate, above threshold)
▪ Tax abatement	▪ Lowers or eliminates local taxes on company’s tangible property	▪ Can be achieved by lowering tax rates or property’s assessed value

Grant Programs Are Widely Available to Attract Companies

Type of grant program	How incentive works	Possible features
▪ Discretionary	▪ Administered by agencies that have some discretion over grant recipients and amounts awarded ▪ Projects and/or companies must meet certain eligibility criteria ▪ Payment generally subject to agreed-upon performance	▪ May target specific industries (e.g. manufacturing), geographies (e.g. distressed localities), or projects (e.g. major employers) based on eligibility requirements
▪ Custom	▪ Awarded on a case-by-case basis ▪ Generally no discretion over recipient(s) of grant ▪ Typically larger amount ▪ Payment generally subject to agreed-upon performance	
▪ By right	▪ Awarded automatically to all companies or projects that meet eligibility criteria (no discretion)	
▪ Capacity building	▪ Generally not tied to specific projects or companies, and awarded to communities (e.g. industrial park, broadband access)	

Virginia and Other State Competitors

- There are 2,080 total state business incentives in the United States*
  - Top 5 Program Types: Tax Credit (539); Grant (484); Loan/Loan Participation (423); Tax Exemption (278); and Other (181)
- Many programs exist, and Virginia's number of incentives is well within the range of its competitor states
- Number of programs is not a measure of how effective a state is when utilizing incentives
- Other measures must be looked at to determine effectiveness

State	# Programs	State	# Programs
Maryland	70	Florida	43
Ohio	51	Georgia	42
South Carolina	51	North Carolina	31
West Virginia	47	Alabama	31
Virginia	**46**	Louisiana	26
Kentucky	44	Tennessee	22

*Council for Community & Economic Research; includes all 50 states & 5 territories

Virginia's Incentive Portfolio

	Admin. Entity	Purpose & Benefit	Eligibility	Avg. Volume*
Commonwealth's Opportunity Fund (COF)	VEDP	▪ Deal closing fund ▪ Designed to secure a company location or expansion ▪ Cash grant (structured up-front or when milestones achieved)	▪ Min. threshold: $5M cap. invest. & 50 jobs; lower for distressed regions ▪ Local match required ▪ Out-of-state competition ▪ Traded sector only	▪ $21.5 million/yr. ($18.3 million in FY19)
Virginia Investment Partnership (VIP)	VEDP	▪ Designed to encourage continued investment by Virginia manufacturers or R&D firms supporting manufacturers ▪ Cash grant (post-performance)	▪ Min. threshold: $25M capital invest. ▪ No net reduction in employment ▪ Local match required ▪ Out-of-state competition ▪ Traded sector only ▪ At least 3 years operating in Virginia	▪ $5.2 million/yr. ($2.9 million in FY19)
VA Econ. Devel. Incentive Grant (VEDIG)	VEDP	▪ Designed to encourage firms to create high-paying jobs by locating HQs or service-sector operations in VA ▪ Cash grant (post-performance)	▪ Min. threshold: 400 jobs @ 150% PAW; or 300 jobs @ 200% PAW and $5M in capital investment ▪ Lower thresholds for smaller MSAs ▪ Traded sector only	▪ $4.2 million/yr. ($1.5 million in FY19)
Major Eligible Employers Grant (MEE)	VEDP	▪ Designed to encourage investment and job creation by major employers/corp. HQs ▪ Cash grant (post-performance)	▪ Min. threshold: $100M cap. invest. and 1,000 jobs ▪ Min. of 400 jobs if avg. wage is at least 2x locality's PAW ▪ Traded sector only	▪ $6.8 million/yr. ($0 million in FY19)
Virginia Jobs Investment Program (VJIP)	VEDP	▪ Reduces training costs of new and expanding firms ▪ Cash grant (post-performance) ▪ Consulting services and funding offered	▪ Min. threshold: $1M cap. invest. and 25 jobs (lower for small business) ▪ Wages 1.35x federal minimum wage ▪ Traded sector only	▪ $9.3 million/yr. ($6.9 million in FY19)

* Volumes based on HB 1191 report; figures are generally for the period of FY 2015-2019 with some programs having different start dates

Virginia's Incentive Portfolio

	Admin. Entity	Purpose & Benefit	Eligibility	Avg. Volume*
Brownfields Restoration Fund	VEDP	▪ Promotes restoration and redevelopment of brownfield sites ▪ Cash grant to locality	▪ Only localities may apply ▪ Property publicly or privately owned	▪ $1.4 million/yr. ($2.1 million in FY19)
Business Ready Sites Program	VEDP	▪ Supports site assessment and site remediation ▪ Addresses need for more project-ready sites ▪ Cash grant to locality)	▪ Consideration based on viability, alignment, economic impact, commitment, and resources leveraged	▪ $460,000/yr. ($1.0 million in FY19)
Performance-based Custom Grants	VEDP	▪ Focus on major projects with transformational impact ▪ Cash grant (structured up-front or when milestones achieved)	▪ Requires special legislation (MEI Commission) ▪ Traded sector only	▪ $870.5 million awarded in FY19 (Amazon HQ2, Micron, Huntington Ingalls, and AWS)

Note: Virginia has other incentives that complement those listed above and on previous slide and are managed by other state agencies, including, but not limited to, the following: Department of Agriculture, VDOT, VRPT, SBSD, DHCD, VTC, CIT, VPA and Tobacco Commission. Many of these are specific to an industry, region or assist with a component part of a larger economic development incentive package.

* Volumes based on HB 1191 report; figures are generally for the period of FY 2015-2019 with some programs having different start dates

How Has the General Assembly Increased its Oversight of Incentive Programs?

- In FY 2010, the General Assembly re-organized funding of incentive programs in the budget to make it easier to know how much was dedicated to economic development incentives
  - Established a new "agency" the Virginia Economic Development Incentive Payments, or VEDIP, to increase transparency and cluster more of the funding in one place in the budget
- That same year the General Assembly passed House Bill 2550 (Cox), which established the MEI Project Approval Commission to review financing for individual incentive packages
  - This effort stemmed from concern by the General Assembly that by the time they had the option to approve incentive packages requiring new legislation, the deals had often already been signed, sealed and delivered
  - Membership includes 5 House members, appointed by Chairman of Appropriations, 3 Senate members appointed by Chair of Senate Finance, and two ex-officio members, the Secretaries of Finance and Commerce and Trade

Proliferation of Incentives and Lack of Accountability Led to Increased Legislative Oversight

- Originally Commission reviewed only projects which required new incentives or amendments to existing incentive packages
  - Many large incentives remained outside the purview of legislation if, as is often the case, the package combined grants from multiple sources like COF, VJIP, tax credits and exemptions, etc.
  - Subsequent changes in 2015 amended the scope of the process
  - Added a requirement for 48 hour advance provision of relevant materials to Members
  - Expanded scope to include any incentive package where total value of all incentives – including tax incentives – exceeds $10.0 million
    - Previously had instances where high value packages were offered but only a small portion was from “new” incentives thus the project was outside scope of Commission
    - Because tax credits and exemptions were added, also changed the composition of the Commission to also include House Finance members
  - Subsequently added all discretionary incentive package that would entail an in-state relocation of an existing Virginia employer
  - All second extensions of performance agreements forwarded by the VEDP Board also require MEI review and approval

MEI Commission Process and Procedures

VEDP's VP of External Affairs and/or AVP of Business Investment (VEDP staff) meet regularly to provide updates to the Legislative Fiscal Analysts (HAC/SFC staff) on the project pipeline

↓

Secretary of Commerce and Trade calls MEI meetings when VA has been shortlisted for a project

MEI meetings are scheduled around JLARC, when possible

↓

Prior to a MEI meeting, VEDP staff meets with HAC/SFC staff to review the draft proposal

VEDP finalizes presentation based on feedback and submits to HAC/SFC staff for distribution to MEI members at least seven days prior to the meeting

↓

VEDP CEO, or his designee, presents projects for consideration and a vote to MEI

↓

Upon approval, MEI members alerted by Secretary of Commerce & Trade that package was accepted and announcement is expected

VEDP staff drafts legislation/budget requests for MEI-approved projects and special appropriations

Other Changes to Increase Legislative Oversight

- 2014 General Assembly passed HB 1991 (Massie) which set out a process to review all incentives issued in the prior 3 years, as well look-back at relative success of projects 5 years after completion
- Emanated from a recommendation in the JLARC study on economic development incentives released November 2012
- Concern was that although metrics were in place to gauge whether an incentive seemed like a good investment prior to the offer being made, no examination was being made on the back-end of the project
  - VEDP has robust ROI estimating model of what could happen, but did not look at what actually occurred after a project was completed
  - Dispersion of incentives was also a concern, with many other entities – including groups like the Tobacco Commission – offering incentives that were never evaluated post-facto

Changes Made to Improve Evaluation Process

- To address the belief that an outside-entity would be able to examine the economic development incentive process holistically, the General Assembly established a unit in JLARC to undertake on-going oversight
- In addition to the annual process of reviewing the success or failure of individual projects offered the 3 prior years, this unit looks at individual tax and grant incentives on a periodic basis, with in-depth reports made annually on specific incentives
- JLARC could also assist in evaluating proposals to change apportionment methods for different types of corporations, including current consideration of market-based sourcing of intangible property as well as review of tax exemption usage

JLARC's Most Recent Findings
(December 2018)

- Virginia spent $1.8 billion on 78 economic development incentives from FY10 to FY17, about 1.3% of total GF spending
- Total spending on incentives in FY17 ($248 million) was slightly less than spending in the previous two fiscal years
- Completed projects receiving grant funds created about 59,000 jobs and $12.2 billion in capital investment or other spending
- The majority of completed projects receiving grant funds met their capital investment goals, and only one-quarter met their job creation goals
- Nearly 60 percent of the spending on incentives was for tax incentives such as sales and use tax exemptions ($835 million) and tax credits ($180 million) even though studies have indicated grant programs have substantially larger economic benefits
- The remaining 42 percent was spent on grants ($715 million) and other incentives such as loans and gap financing programs ($25 million)
  - Grant programs have a higher economic benefit because they tend to target projects by sector or region that are expected to have higher economic benefits.

Further Incentives Reform Adopted By VEDP

Based on the 2016 JLARC recommendations VEDP created the Project Review & Credit Committee (PRACC) to evaluate all projects

- *All projects* receiving discretionary incentives from VEDP are reviewed by PRACC regardless of size, name recognition, or locality.
  - CEO/COO, VPs, AVP, General Counsel, Project Research Manager, and Senior Economist
  - Review all elements of the project
  - Consider strategic, competitive, and financial implications
  - Evaluate Risk Assessment and ROI analysis
  - Approve any proposed conditions for release of incentive funds
  - Determine whether to proceed with SCT preapproval

Further Incentives Reform – Adopted by General Assembly & VEDP

General Assembly Session 2017 – VEDP Reform legislation passed included a number of significant changes to the Authority & incentives management processes, including but not limited to the following:

- Creation of an Incentives Division that is *"responsible for reviewing, vetting, tracking, and coordinating economic development incentives administered by or through the Authority or economic development incentives offered by the Commonwealth or a locality in conjunction with Authority-administered incentives…"*
- New Board was assigned more responsibility regarding reporting & oversight of incentives management
- Board granted authority to authorize first-time extensions, clawbacks and referrals of clawbacks to the OAG for collection
- Any second time extensions require both Board and MEI approval

Following JLARC Report: Sample Incentives Management Challenges & Lessons Learned

- Having an open-ended performance agreement with no defined termination for the agreement should metrics not be achieved
- Basing decisions and offers on future supply chain development without contractually requiring the additional investment and jobs
- Addressing situations where a company has submitted falsified documentation (i.e. presenting another company's website as their own/fake letters of credit)
- Fully researching a company, going so far as to visit their existing facility
- Tying release of funds to milestones achieved, keeping revenues ahead of incentive payments

Evolution of Incentives Administration at VEDP

	Pre-2016	2016	Late-2017	Future (tentative)
Staffing	▪ No full-time staff for incentives admin.	▪ One full-time staff member dedicated to incentives monitoring	▪ Four full-time staff members dedicated to incentives admin., including commercial credit experience	▪ Potential for staffing growth as program activity increases
Due Diligence	▪ Due diligence on firms performed by individual project managers, with no systemic review, creating potential for major errors (e.g., Lindenburg)	▪ Established vetting process, incl. financial condition, risk level of firm, project financing ▪ Project Review and Credit Committee (PRACC) created to review, discuss, and approve due diligence	▪ PRACC assigns a risk rating for firm and incentive for every project ▪ Vetting process refined	▪ Further refinements will be made from time to time based on experience and benchmarking
Incentives Structuring	▪ COF grants typically provided up front	▪ COF grants typically provided up front	▪ Typically low-risk incentives paid in first year; others after tax milestones (to avoid financial risk)	▪ No change anticipated
Monitoring and Reporting	▪ No comprehensive incentive reporting, except post-performance report required by HB1191	▪ No comprehensive incentive reporting, except post-perf. report required by HB1191	▪ Comprehensive public reporting for all active projects ▪ Extensions require Board/MEI approval	▪ Executive-level dashboard reports created to enable board to effectively monitor portfolio
Clawbacks	▪ Firms sometimes allowed to meet obligations outside strict contract terms	▪ Management policy for clawbacks in transition	▪ Strict adherence to Code and contract terms	▪ Strict adherence to Code and contract terms

Have these Changes Improved Virginia's Oversight of Its Economic Development Incentives?

- In 2017, PEW Research has conducted an assessment of state evaluation processes of the effectiveness of their incentives and divided states into 3 categories:
  - **Leading** states have well-designed plans to regularly evaluate tax incentives, experience producing quality evaluations that rigorously measure economic impact, and a process for informing policy choices
  - States that are **Making Progress** have made a plan by enacting a policy that requires regular evaluation of major tax incentives
  - **Trailing** states lack a well-designed plan to regularly evaluate major tax incentives

Leading	Making Progress	Trailing
Virginia	Ohio	North Carolina
Maryland	Tennessee	South Carolina
Florida	Louisiana	Kentucky
Ohio	Alabama	West Virginia
		Georgia
		Florida

Lessons Learned: Guiding Principles for Use of Incentives

- Incentives should not be paid-out until after hires and capital expenditures have been made
- Finite term agreements
- More transparency in project financials and ability to execute the project – incentives unit works with grantees to ensure benchmarks known and agreed to by all
- Locality should contribute to incentive packages
- Increased oversight, experience and flexibility via MEI Commission review of major projects
  - Amazon HQ2 proposal took over 1 year to develop and review
  - Staff and Commission members met several times with VEDP staff, local government representatives and private sector to evaluate and critique state & local package as it evolved
- New model has been accepted by most – if not all – of those, including industry partners, that participate in the process of project proposal, evaluation and offer

In Offering Incentives, VEDP is Guided by the Following

- Align with strategic sectors
- Impactful
- Maximize community wealth
- Align with local/state strategy
- Diversify the job base in regards to skill sets
- Solve a specific need (versus a by-right expectation)
- Use as real competitive advantage
- Leverage other state resources
- Advance quality of life

Reformed & New Incentives Programs With Budgetary Impact That Require General Assembly Approval

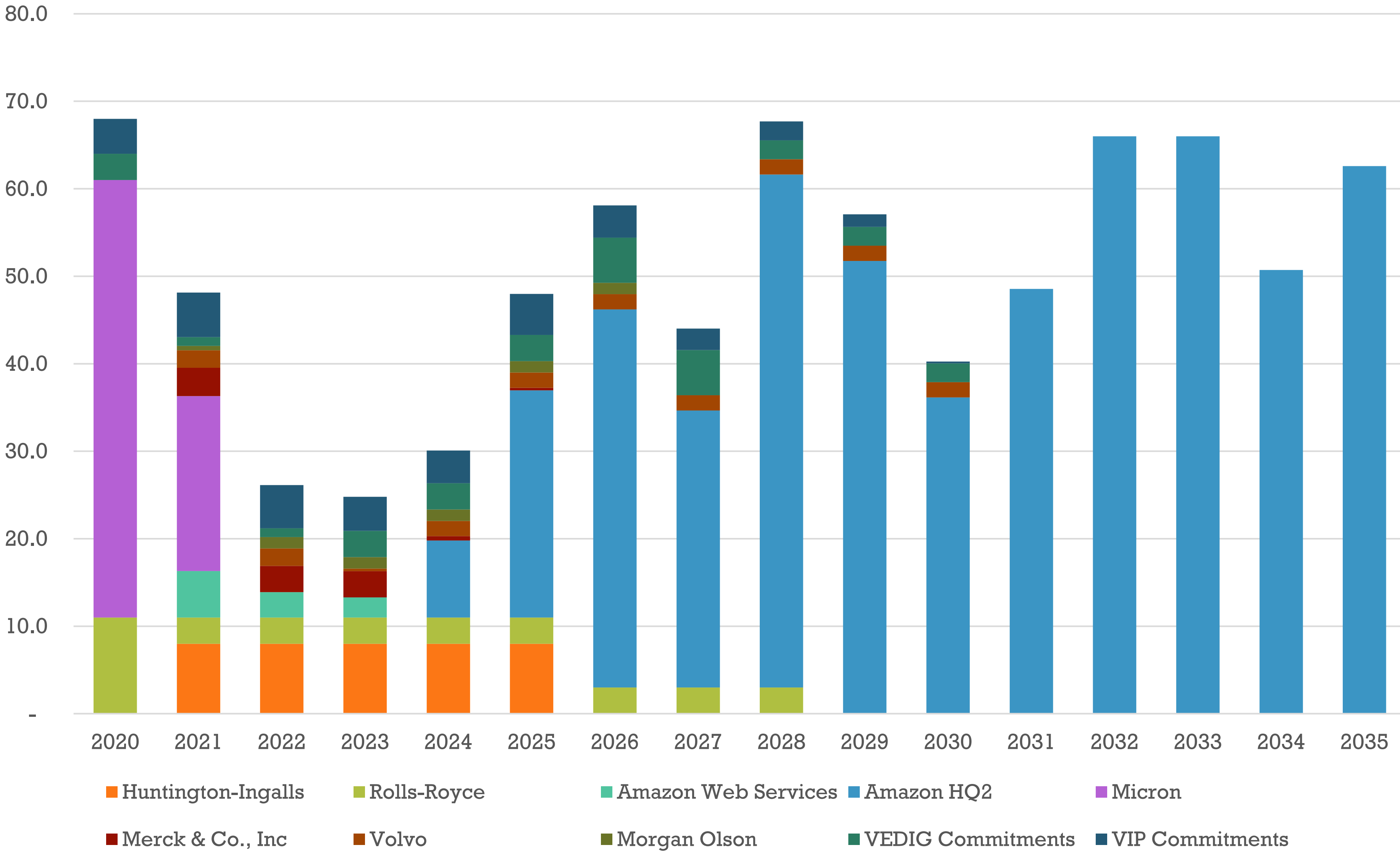
- **Business-Ready Sites Program** – Increasing Virginia's site readiness portfolio with improved sites of various sizes and locations, as well as marketing these through VEDP's partners, will incentivize companies to look deeper into what Virginia has to offer
  - Business-Ready Sites program has been re-energized with a recent investment that funded a site characterization plan (get numbers from VEDP Board Mtg) which is now complete
- **Custom Workforce Development (VTAP)** – This is a new and developing program that has proved effective in Virginia's competitor states (e.g. GA, LA, etc)
  - It is the development & delivery of a customized, comprehensive workforce recruitment & training solution for a project
  - A discretionary incentive offered through VEDP that attracts companies looking to locate in Virginia or serve those current resident-companies seeking to expand
- **Tech Talent Pipeline** – Component of the Amazon HQ2 project; a stand-alone workforce development plan to serve the entire Commonwealth's increasing needs for IT workers in select fields to support future growth by ensuring a steady flow of qualified workers
  - Increase by FY2039 the number of new eligible degrees by at least 25,000 more degrees than the current number awarded in 2018 and to improve the readiness of graduates to be employed in technology-related fields and fields that align with traded-sector growth opportunities identified by the Virginia Economic Development Partnership
- **GO Virginia** – The State GO Virginia Board recently approved guidelines for regions seeking funds to build out broadband infrastructure for economic development purposes

Custom Projects Requiring General Assembly Approval

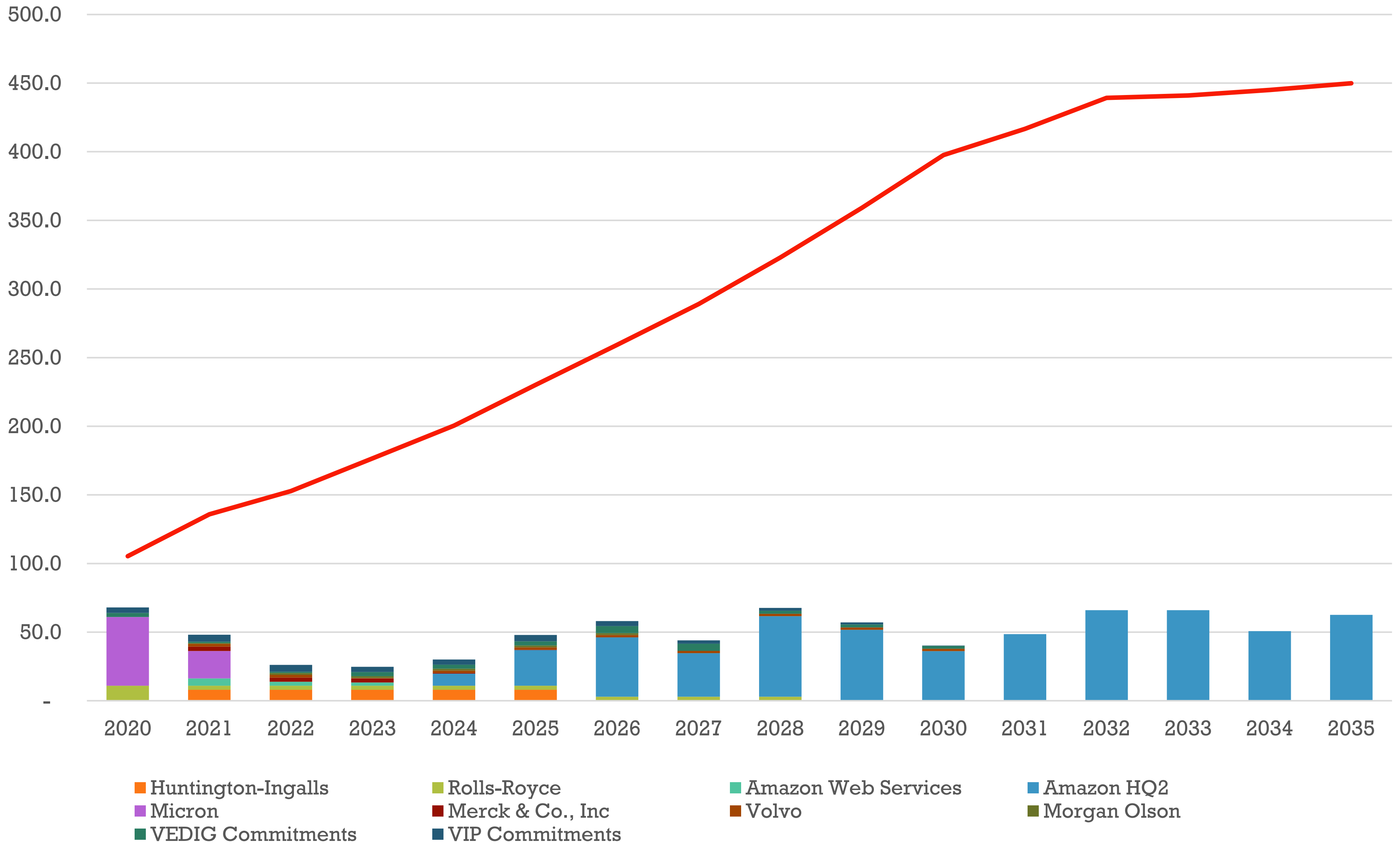
Project/Company	FY 2021 (millions)	FY 2022 (millions)	Biennium (millions)
Newport News Ship	$8.0	$8.0	$16.0
Rolls Royce	$3.6	$3.3	$6.9
Merck *	$3.2	$3.0	$6.2
Micron	$20.0	$0.0	$20.0
Volvo*	$2.0	$2.0	$4.0
AWS	$5.3	$2.9	$8.2
Tech Talent Pipeline (1)	$13.6	$8.5	$22.1
Tech Talent Pipeline (2)	$15.2	$15.2	$30.4
Morgan Olson*	$0.0	$.50	$.50
Total	$70.9	$43.4	$114.3

* Projects require separate legislative approval in addition to funding in budget.

Incentive Commitments & Their Budget Impact Through FY 2035 ($ millions)



Incentive Commitments to Companies Compared to Estimated Tax Revenues Generated Through FY 2035 (millions)



Nearly 47,000 Virginia Jobs Expected From VEDP-Assisted Projects Announced Over the Past Two Years

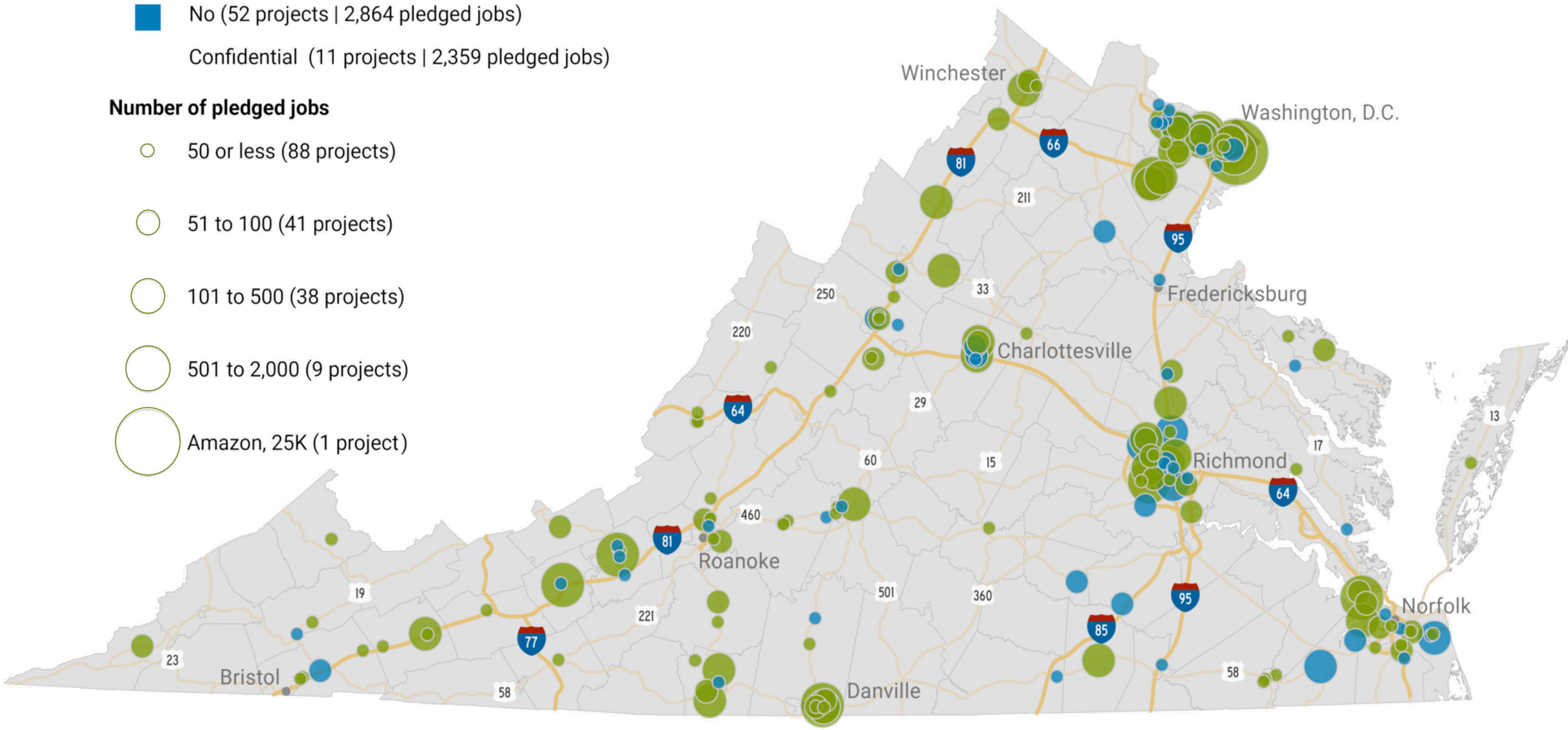
Location of VEDP-assisted announcements and expected jobs[1]
Projects announced between 1/13/18 and 11/13/19

Received VEDP-administered incentive

- Yes (125 projects | 41,655 pledged jobs)
- No (52 projects | 2,864 pledged jobs)
- Confidential (11 projects | 2,359 pledged jobs)

Number of pledged jobs

- 50 or less (88 projects)
- 51 to 100 (41 projects)
- 101 to 500 (38 projects)
- 501 to 2,000 (9 projects)
- Amazon, 25K (1 project)



[1]Includes 14 projects that pledged zero jobs
Source: VEDP's announcements database

amazon

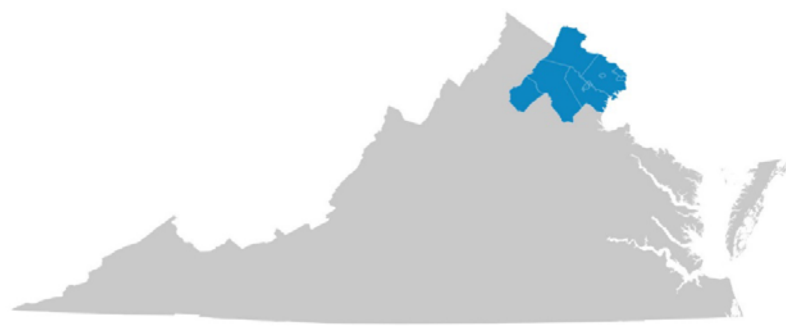
Amazon, Inc. will establish a major new headquarters in Northern Virginia that will create more than 25,000 high-paying jobs over 12 years. The economic benefits of the Amazon project will be shared throughout the Commonwealth and are expected to result in more than $3.2 billion in new state general fund revenues over the 20-year incentive term with Amazon, after accounting for direct company incentives. In addition to the 25,000 direct jobs Amazon will create, the Commonwealth estimates the creation of more than 22,000 permanent, direct, and indirect jobs in Virginia.

New Jobs | 25,000

Capital Investment | $2.5B

> "We're no stranger to Virginia. We have over 10,000 Amazonians already in the state of Virginia. And we look forward to bringing more jobs to the state."

Holly Sullivan
Amazon
November 13, 2018



** State incentives total $550m over 20 years

Micron

Micron Technology, Inc. will increase memory production at its operation in the City of Manassas. The expansion will position the Manassas site as Micron's Center of Excellence for long-lifecycle memory and will cement the company's position as one of Virginia's largest exporters, as it is expected to increase exports from the Commonwealth by more than $1 billion annually after completion.

New Jobs | 1,100 **Capital Investment | $3B**

"Micron's Manassas site manufactures our long-lifecycle products that are built using our mature process technologies, and primarily sold into the automotive, networking and industrial markets. Micron is grateful for the extensive engagement of state and local officials since early this year to help bring our Manassas expansion to fruition. We are excited to increase our commitment to the community through the creation of new highly skilled jobs, expanded facilities and education initiatives."

Sanjay Mehrotra
Micron Technology
August 29, 2018

** State incentives total $70m over two years

MORGAN OLSON®

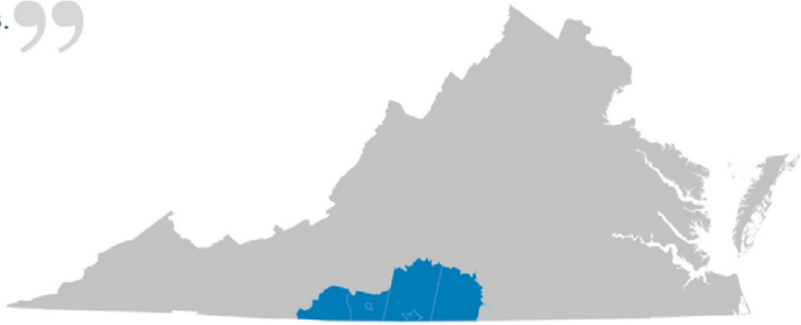
Morgan Olson, LLC, North America's leading manufacturer of all-aluminum walk-in step vans, will establish a new walk-in step van assembly operation in a 925,000-square-foot plant in Danville-Pittsylvania County currently owned by IKEA. The company is the first to receive support from the new Virginia Talent Accelerator Program.

New Jobs | 703

Capital Investment | $57.8M

> "One of the most attractive aspects of locating in Danville-Pittsylvania County is that we will be able to take advantage of the new Virginia Talent Accelerator Program, which will help us quickly attract and train the high-quality workforce we need to deliver for our customers."

Mike Ownbey
Morgan Olson
October 25, 2019



** State incentives total $7m over six years

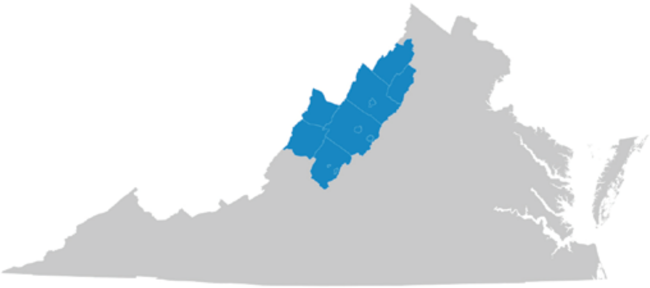
MERCK
INVENTING FOR LIFE

Merck & Co., Inc., a publicly held global healthcare company known as MSD outside the United States and Canada, plans to expand its manufacturing operation in Rockingham County. The company will add 120,000 square feet to its existing 1.1 million-square-foot operation in Elkton, Virginia to increase production of its Human Papillomavirus (HPV) vaccines.

New Jobs | 100 **Capital Investment | $1B**

"Our strong partnerships with local and state elected officials, educational institutions, and organizations throughout the Elkton community help us sustain our commitment to the area's economic growth."

Sanat Chattopadhyay
Merck & Co., Inc
May 6, 2019



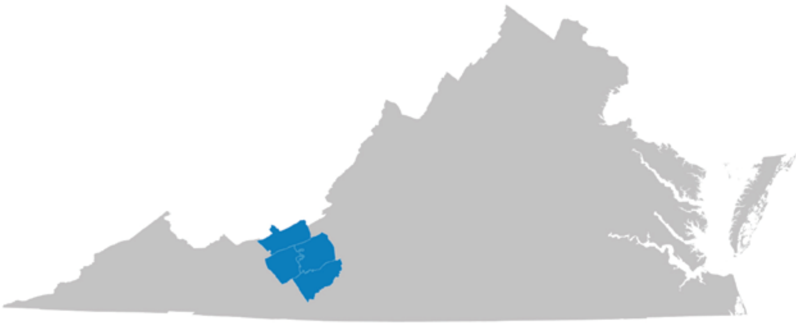
** Total state incentives $10m over five years

The Volvo Group will expand its Volvo Trucks North America New River Valley (NRV) assembly operation in Pulaski County. Major components of the investment include a new 350,000-square-foot building that will house truck cab welding operations; an expansion of the existing plant to allow for further improvements to the facility's paint operations and overall material/production flow; and a variety of equipment upgrades.

New Jobs | 777

Capital Investment | $400MM

"This investment will give our employees the tools they need to continue providing our customers the highest quality products. Creating more value-added processes through these investments is good for our employees, our plant, and our region."



Franky Marchand
Volvo Trucks North America
June 28, 2019

** Total state incentives $16.5m over three years