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Typical business incentive policies need reforms to rein in costs and maximize benefits

Careful funding and targeting of tax incentives helps, report finds, and other business services provide even greater local returns

KALAMAZOO, Mich.— As state and local governments have assembled lavish incentive packages to lure business such as Foxconn and Amazon, many have questioned whether these incentives are a good deal. In a new report from the Upjohn Institute, Senior Economist Timothy Bartik shows that the typical incentive package has only modest benefits for local jobs and incomes. Carefully targeted incentives can provide much larger local benefits, but those that draw money from public services such as education can significantly harm local economies.

While tax breaks make up over 90 percent of incentives, Bartik finds that other forms of incentives, such as customized business services, create 10 times the number of jobs. These include job training tailored to the business' needs; manufacturing extension services that offer advice on improving technology, productivity and sales; and small business development centers. Although large corporations tend to receive the biggest incentive packages, it's small-to-medium-sized firms that get the most benefit from business services and create the most jobs. Smaller businesses also spend their money closer to home, which creates even more local jobs.

Bartik built a simulation model that describes how incentives' benefits and costs are divided among residents at different income levels. The model shows how those benefits and costs change if incentives are structured or funded differently or targeted at different types of firms.

Incentives can have large benefits if they're targeted at industries with a high "job multiplier"—that is, those that create multiple indirect jobs for each job created by incentives. New jobs in high-tech manufacturing, for example, may each spur five additional jobs in the community. Targeting the new jobs at the local unemployed population also increases the benefits.

The incentives' funding also matters. Paying for incentives by shifting money from public schools, for example, can create jobs. However, the long-term loss in wages from cuts to education far outweighs this benefit. Incentives paid for by increasing taxes on out-of-state businesses fare better.

A policy brief distilled from the report offers recommendations for incentive reforms, including capping incentive budgets to preserve education and other public services and only offering tax incentives to high-multiplier industries. It also recommends a greater focus on the customized business services that produce more local benefits.

The report is "Who Benefits From Economic Development Incentives? How Incentive Effects on Local Incomes and the Income Distribution Vary With Different Assumptions About Incentive Policy and the

Local Economy," by Timothy J. Bartik. More information, including the full report, executive summary and policy brief, is at http://bit.ly/IncentivePolicies.

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