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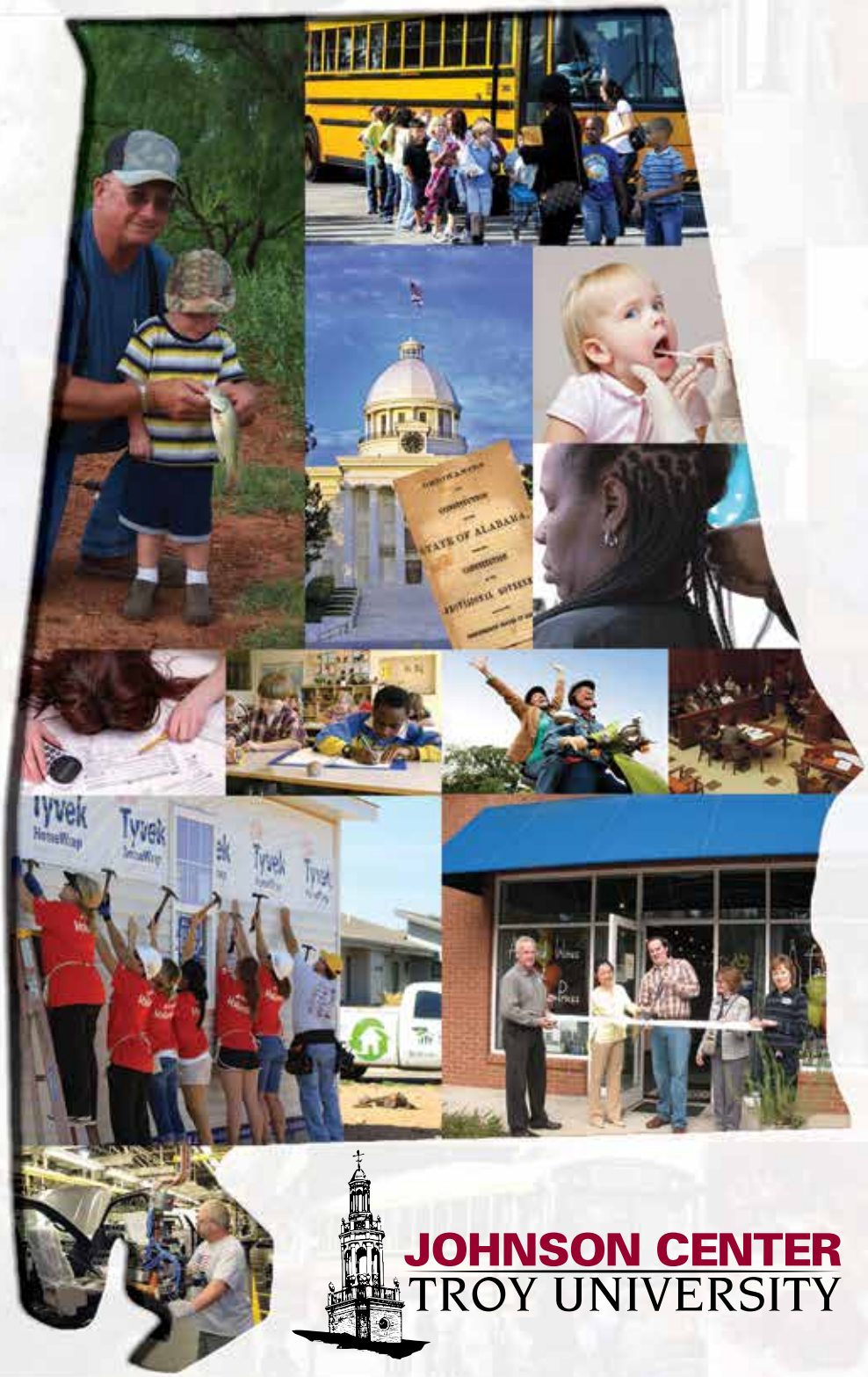

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Tax Incentives Job Creation and the Unseen: Is Alabama Giving Away the Store to Attract New Industry

George R. Crowley, Ph.D.

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Summary Points

- Alabama has a long history of aggressive use of tax incentive packages for industrial recruitment. The state's various tax incentive deals with manufacturing firms have likely reached into the billions of taxpayer dollars.
- Alabama is not alone in this campaign, as many states are similarly aggressive in offering tax deals to large, high-profile corporations. Despite the popularity of using tax incentives for industrial recruitment, there is little scholarly evidence of their effectiveness, and the potential exists for the incentives to crowd out investment by firms lacking the political clout to receive a deal.
- This chapter analyzes five recent, high-profile tax deals between the state of Alabama and Mercedes-Benz, Honda, Hyundai, National Alabama Corporation, and ThyssenKrupp. Evidence suggests most of these deals have a strong impact on the manufacturing sector where they are located, but surrounding areas do not appear to benefit. Tax revenue data show a modest increase in the growth rate of property tax revenues in these counties relative to the state as a whole.
- Although the majority of manufacturing plants created through tax incentives have created thousands of jobs for Alabamians, the jobs have come at a significant cost, both in taxpayer dollars and potentially lost opportunities.
- Alabama should establish itself as competitive without the use of selective incentives by maintaining its low tax rates and simplifying its tax code, and get policymakers out of the business of picking winners to receive tax benefits. At a minimum, the development process should be revamped to improve oversight, transparency, and accountability.

1. Introduction

The past several decades have seen an explosion of competition between state governments for large-scale investment projects by high-profile companies. A recent report by the New York Times estimates that state and local governments spend (or give up in terms of abated taxes) roughly $80 billion per year on incentive packages for companies.[1] Alabama has been particularly aggressive in recruitment of business. The state already boasts some of the lowest tax rates in the country, and has over the last several years offered a series of massive tax incentive packages to encourage businesses to invest in the state. Alabama's dedication to industrial recruitment has directly led to investment by a number of multinational manufacturing businesses, with each hiring thousands of Alabamians.

The variety of tax incentives available in Alabama is extensive, and any attempt to simply list all of them quickly becomes unwieldy. The Alabama Department of Revenue "Summary of Alabama Taxes and Tax Incentives" report from June 2009 lists incentives to which businesses may be entitled by meeting certain qualifications including abatements and exemptions to the business privilege tax, sales and use tax, property tax, and corporate income tax.[2] The Economic Development Partnership of Alabama adds the capital investment tax credit and industrial grant program to the list of major incentives in Alabama.[3] *Business Facilities* lists several additional incentives available in the state, including possible abatement of local taxes (in addition to state taxes), programs designed to provide infrastructure, training programs, and special loans designed to attract business (2012)[4]. Alabama has also designated 28 so-called depressed economies Enterprise Zones (25 counties and three cities); businesses choosing to locate or expand in these areas may qualify for additional tax and non-tax incentive packages (Economic Development Partnership of Alabama 2012b)[5]. In addition to all of these programs, the Alabama Department of Commerce offers "to develop an incentives package uniquely designed" for specific businesses. [6]

Examples of successful industrial recruitment in Alabama date back to the state's 1993 agreement with Mercedes-Benz. The state offered a lucrative $253 million incentive package to win the company's first American manufacturing plant. [7] This deal, which was controversial at the time because of its size, has since been viewed as an important step towards establishing Alabama as a state where industry was welcomed.[8] Since then, Alabama has struck similar incentive deals for large-scale investments by Honda, Hyundai, and Boeing. The practice

shows no signs of stopping, with announcement in July 2012 of a $158 million package for Airbus's first American manufacturing plant.[9] In November 2012 Alabamians voted to further expand the use of economic incentives. [10] In addition, two bills passed by the State Legislature in 2012 (HB 160 and HB 159) expanded the Governor's discretionary power to create tax incentive packages.[11]

Alabama's use of tax breaks to attract high-profile business to the state, while successful, has also generated controversy. In 2012, the Alabama Education Association (AEA) filed a lawsuit against Governor Bentley attempting to block a number of tax incentives over concerns the adverse effects on revenue sources could potentially harm funding for education.[12] The suit was eventually dismissed, but the AEA's concerns merit serious consideration for a state faced with significant budget issues. Further criticisms center on the lack of transparency in the process of issuing the incentive packages.[13]

The numerous deals for industrial recruitment have rarely been subject to retrospective review to evaluate if promised benefits have materialized. Alabama does not provide any official report of the cost of business tax incentives.[14] A 2012 study by the PEW Center on the States reported Alabama (along with 25 other states) had no formal criteria for evaluating the effectiveness of tax incentives.[15] The creation of thousands of jobs through the location of large-scale manufacturing facilities in the state is undisputed but it is far less clear that the incentive packages in terms of costs and benefits to taxpayers. While the benefits of a deal—the employees hired, the capital invested—are visible, the costs—the outcomes absent government intervention—are often "unseen" and consequently easily overlooked. Are these firms simply drawing workers from other businesses? Further, is it possible that these high-profile investments have crowded out other entrepreneurs who lack the clout to receive a large tax deal? This chapter seeks to answer these questions through a comprehensive analysis of several high-profile deals between Alabama and private companies.

The following section summarizes some of the key findings of the academic literature on tax incentives and industrial recruitment. Section 3 provides background on manufacturing in Alabama, while Section 4 provides comprehensive case studies of six recent high-profile tax deals made by Alabama. The policy implications of this report are discussed in Section 4, while the final section offers concluding remarks.

2. Tax Incentives and Job Creation: Theory and Evidence

A motivation for tax incentives exists in what is known as economic base theory. While the simple economic base model has been repeatedly modified in attempts to make it more realistic since its inception, its general themes remain a crucial component of regional impact analysis. [16] According to this model, certain industries such as manufacturing are "basic" and depend on factors external to the local economy. In other words, these basic industries export most, if not all, of their products to other states, regions, or countries. For example, the Airbus plant will sell the aircraft produced there exclusively to companies located outside of Mobile County and Alabama. According to base theory, these industries are important because by exporting their products, they import money and capital which then support the non-basic industries in the area that depend on the local economy, such as restaurants, convenience stores, and suppliers. In fact, according the model, basic employment has a "multiplier effect" in that each basic job supports multiple non-basic jobs. Thus, basic industries drive growth in the economic base model and its more complicated variants.

The implications of base theory as a model for economic development are straightforward. In theory, states or regions should seek to strengthen their basic industries to drive growth of the economy as a whole. It is unsurprising, then, that states engage in contentious bidding wars with one another through the use of tax incentives whenever a high-profile company announces plans to build a new manufacturing facility. After all, if the economic base model is accurate, each of those manufacturing jobs will lead to several additional jobs in local businesses, hence the claims of indirect jobs due to the plants. Alabama's major tax deals accord well with the guidance of base theory, as all have been for large-scale manufacturing facilities.

Despite the intuitive nature and widespread acceptance among policymakers for the use of tax incentives in industrial recruitment, this sort of governmental intervention is not without criticism. By definition, the process is unfair because certain firms are given advantages not available to other firms. In a survey of the literature aimed at informing policy in developing countries, Zee, Stotsky, and Ley questioned the usefulness of tax incentives for businesses. Specifically, they pointed to the various costs associated with a regime of tax incentives: distortionary effects caused by giving incentives to one firm and not another, forgone revenue (by design), administrative costs, and costs associated with rent-seeking as firms attempt to secure favorable tax deals.

Further, previously-invested firms may be unable to compete with newly subsidized ones, leading to no improvement in employment rates as old firms are merely replaced by new ones.[17] Alabama's own history provides insight into this phenomenon of competing firms threatened by selective incentives. Following the Mercedes-Benz deal, steel firm Trico secured its own incentive package under an expanded version of the incentive law. Rival incumbent firm Gulf States Steel, finding itself at a competitive disadvantage, attempted to block the incentive package through a lawsuit, which was ultimately withdrawn.[18]

In these kinds of interventions, the visible effects (capital investment, jobs created, etc.) are often trumpeted while the potential alternative uses for taxpayer money and other resources devoted to creating the incentive are overlooked.[19] Nineteenth century French theorist and political economist Frédéric Bastiat referred to this as the "unseen," and offered his now-famous parable of the broken window to illustrates the point: if a shopkeeper's window is broken by a child and must be replaced, this creates work for the glazier, and may at first be seen as having a positive impact on the local economy. This line of thinking overlooks that the shopkeeper has fewer resources to spend on some completely different activity. The broken window does not create any economic activity, but simply redirected the shopkeeper's purchases.

Following Bastiat's logic, Alabama's incentive deals beg the question of whether the workers would have been employed in other jobs without these incentives. The evidence suggests in at least some cases, yes. A 2002 study by Faulk on Georgia's use of employment tax credits indicates 72.4 to 76.5 percent of the jobs created by firms participating in the program would have been created in the absence of the program, meaning taxpayers paid over $3 million for jobs that would have been created without the state's intervention.[20] Of course it is also possible that the taxpayer money spent to lure industry could have been used instead for an even more inefficient project, or simply to grow the size of government. While economists differentiate themselves from practitioners in other disciplines in part due to their understanding of these opportunity costs, "the unseen" is by definition impossible to measure and thus left out of the impact analysis used to justify intervention.

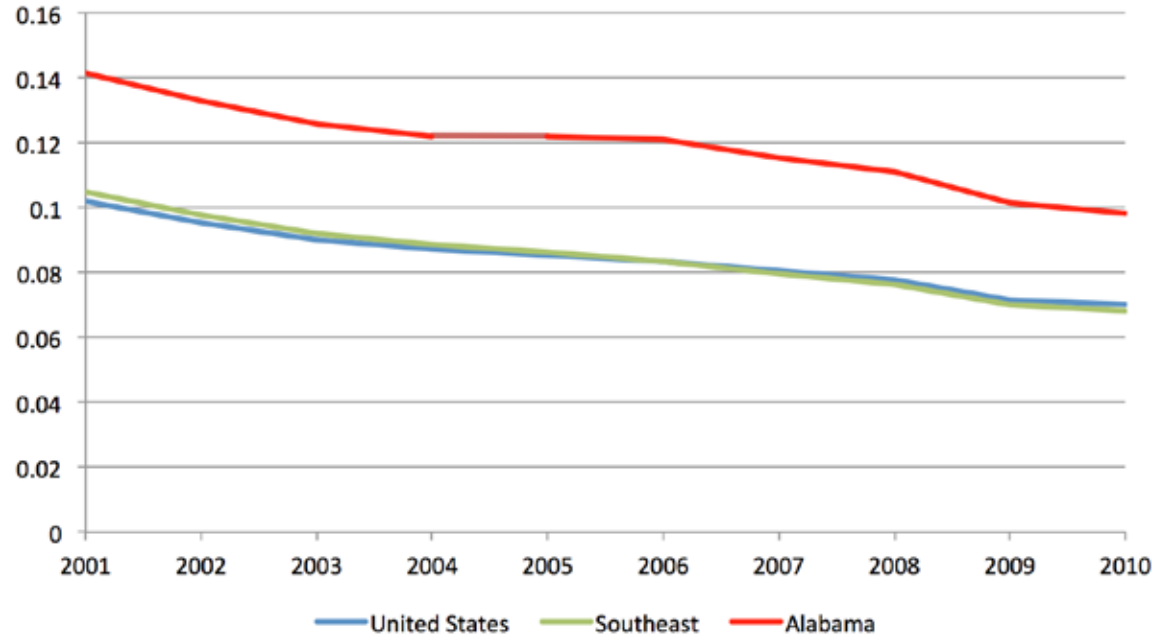
In fact, it may be the case that if those resources are employed only because of government intervention in the form of incentives, then their use is not economically efficient. In other words, if a firm can only locate a new manufacturing plant in the state with massive subsidization, it is likely the case that the project is not an efficient use of resources. Had the location been viable, the firm would have located there on its own. Thus, for truly efficient projects, tax incentives are likely subsiding activities that would have occurred anyway. In these cases, tax abatements represent a pure cost to the state in the form of lost revenue. Tennessee's former governor has indicated that his state's multi-million dollar incentive packages used to secure Nissan and GM-Saturn plants were probably too large since the firms were likely to locate in the state anyway, and South Carolina used incentives to secure a BMW facility already attracted to the state's skilled labor.[21]

A common response to this line of thinking is the claim that states must engage in industrial recruitment in order to stay competitive. In other words, even if Alabama were to represent an efficient and profitable opportunity for a firm absent any incentive deal, the firm may choose to locate in another state which was willing to offer a lucrative tax package. This would seem to be the case prior to Alabama's adoption of tax incentives as a tool for industrial recruitment, with firms locating in neighboring states despite Alabama's low tax rates. For example, one of the reasons Tennessee landed the Saturn automotive plant in Spring Hill in 1985 was because the state agreed to provide $20 to $30 million in training for workers, plus another $50 million for the Saturn Parkway and other roads.[22]

While Alabama today is certainly aggressive in its use of tax incentives for industrial recruitment, it is hardly alone amongst the states; Alabama was amongst multiple suitors for each of the major recruitments discussed in the following section. In public finance literature, commentators describe this competition as a "race to the bottom" with all states attempting to offer increasingly attractive deals to attract investment, theoretically resulting in a shortage of tax revenue needed to fund other government services. For example, according to The New York Times, Kansas cut its education budget by $104 million after offering a $36 million incentive package to recruit AMC Entertainment, a company which had been located in neighboring Missouri. Not to be outdone, Missouri used an incentive package to recruit Applebee's headquarters from Kansas.[23] Concerns about tax incentives' potential to reduce funds available for other government services have been voiced in Alabama as well, as the aforementioned Alabama Education Association (AEA) lawsuit against Governor Bentley illustrates.[24]

In *The Wealth of Nations*, Adam Smith listed four principles for judging any tax system: the system must raise appropriate revenues, be equitable, be easily administered at low cost, and ensure accountability. [25] George Washington University public policy professor David Brunori argues that company-specific tax

Figure 8.1: Ratio of Manufacturing Employment to Total Employment, 2001-2010



Source: Bureau of Economic Analysis

deals violate all of these criteria since they fail to collect enough revenue (since the taxes are abated, at least in the short run), are by definition not equitable, add to an already complicated tax code, and are notoriously difficult to monitor. Citing Alabama's deal with Mercedes-Benz specifically, he claims that it is difficult to see how the company will ever generate enough activity to allow the state to recoup the $253 million in incentives.[26]

Empirical studies of the effectiveness of tax incentives show incentives policymakers overestimate the role incentives play in attracting new firms. In a survey of the literature, Wasylenko concludes state tax incentives have little effect on firm location decisions and that, "States appear to overestimate the degree to which taxes affect economic outcomes," suggesting that while a state's business tax climate is clearly important, policymakers may have less power to encourage investment than they might think.[27] In another survey of the literature, Peters and Fisher echo this sentiment noting that despite their popularity, the majority of the scholarly evidence shows minor at best benefits of tax incentives targeted towards specific firms. The authors warn of policymakers who "believe that they can influence the course of their state or local economies through incentives and subsidies to a degree far beyond anything supported by even the most optimistic evidence" and call for alternative methods of economic development including infrastructure improvements and worker education.[28] This argument of the policymaker's lack of knowledge necessary to improve upon market outcomes dates back to Hayek.[29] To its credit along these lines, Alabama has made substantial investments in workforce development programs in recent years. According to the Governor's Office for Workforce Development, more than $8.3 million was approved in FY 2011 and another $9.6 million in FY 2012 for community colleges to offer dual enrollment in career technical programs, career coaching, equipment purchases, parolee transition programs, and training systems for robotics, welding, injection molding, and other careers.[30]

Wasylenko summarizes several studies of the effects of taxation on economic development. He advocates against the use of any "Band-Aid approach," stating that if tax laws need to be frequently changed to attract business to a state, it is likely indicative of some fundamental problem with the tax system as a whole. Broader tax reform is preferred, as it does not attempt to pick winners and losers.[31]

Evidence of the effects of broader tax policy (such as overall tax rates or credits available to all businesses rather than specific firms) on employment is more positive. In a study of Georgia's Jobs Tax Credit, Faulk finds evidence that this broader type of tax incentive leads to modest increases in employment. The Georgia program differs from the types of deals discussed in this report in that it is a broad policy which all firms meeting certain qualifications may benefit from, and not a set of special tax breaks given to any one specific firm.[32] In a study of the Washington D.C. metro area, Mark, McGuire, and Papke show that higher sales and personal property tax rates are linked to

Table 8.1: Ranking the Size of State Manufacturing Sectors (By Employment), 2013

Top Ten States					Bottom Ten States				
Rank	State	Total Employment	Manufacturing Employment	Percentage Manufacturing	Rank	State	Total Employment	Manufacturing Employment	Percentage Manufacturing
1	Indiana	3,682,999	506,683	13.76	41	Colorado	3,351,702	148,904	4.44
2	Wisconsin	3,530,389	474,374	13.44	42	New York	11,555,389	490,939	4.25
3	Iowa	2,018,830	221,508	10.97	43	Alaska	461,935	16,783	3.63
4	Michigan	5,309,084	581,113	10.95	44	Montana	638,747	22,619	3.54
5	Ohio	6,663,005	691,317	10.38	45	Florida	10,556,082	358,105	3.39
6	Alabama	2,542,368	258,953	10.19	46	Maryland	3,474,596	116,000	3.34
7	Arkansas	1,577,678	157,444	9.98	47	New Mexico	1,079,067	35,431	3.28
8	Kentucky	2,413,942	236,098	9.78	48	Wyoming	395,312	11,512	2.91
9	South Carolina	2,498,641	233,565	9.35	49	Nevada	1,559,621	45,331	2.91
10	Mississippi	1,535,589	141,999	9.25	50	Hawaii	875,837	18,012	2.06

Source: Bureau of Economic Analysis

lower employment growth.[33] As noted above, Alabama has made strides in this area and already boasts some of the lowest income and sales taxes in the country.

Terry Buss notes that tax incentives are typically politically popular, largely because they are typically implemented outside of the budget process, unbeknownst to voters. Indeed, in Alabama the projects are secret before they are officially unveiled, and even carry code names such as "Project Rosewood" and "Project Bingo," which were used for the Mercedes-Benz and Honda deals respectively. Further, states rarely evaluate tax incentive programs once they have been implemented, so even bad policy is left unnoticed. Buss advocates a number of policy prescriptions including requiring formal cost-benefit before and periodic evaluations after a tax incentive has been granted, including sunset provisions which terminate incentive deals without reauthorization, requiring legally binding performance contracts, concentrating incentives on other industries and not just manufacturing, and ensuring that incentive deals do not harm competitors or neighboring economies.[34] However, as states find themselves attempting to remain competitive with one another, these reforms become problematic if implemented by one state alone. To some extent, Alabama has required specific firm performance in the form of tying incentives to quotas on job creation, as evidenced by a number of the agreements described below.

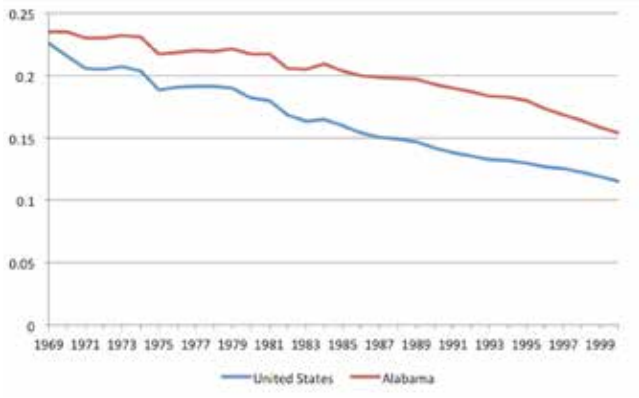
3. Manufacturing in Alabama

Before delving into the specific details of some of Alabama's most prominent tax incentive deals, it is useful to discuss overall trends in the manufacturing sector both within the state and the country as a whole. This overview will shed light on the overall strength of manufacturing in the state (relative to the country as a whole) and will also provide at least suggestive evidence of effectiveness of Alabama's industrial recruitment efforts. Chart 1 shows the ratio of manufacturing employment to total employment over the past decade for Alabama, the Southeast, and the United States as a whole. While the ratio is declining for each area, Alabama has maintained a noticeably higher ratio of its employment in manufacturing.

Table 8.1 provides more recent data (2013) on the ratio of manufacturing employment to total state employment. Alabama remains home to a relatively strong manufacturing sector (in terms of employment), ranking 6th amongst the states with just over 10% of all state employment in manufacturing. This exceeds both the national average of roughly 7%, as well as the ratios in nearby states such as Mississippi and South Carolina. Alabama's dependence on manufacturing is also nearly 5 times that of the states with the smallest manufacturing sectors.

The decline in manufacturing in both Alabama and the nation depicted in **Figure 8.1** above is not a new phenomenon, nor is the relatively large size of Alabama's manufacturing sector. **Figure 8.2** shows the same ratio of manufacturing employment to total employment for Alabama and the United States from 1969-2000. These historical data also point to Alabama's continued dedication to manufacturing. While roughly 23% of workers in both the United States and Alabama were employed in manufacturing sectors at the beginning of the sample in 1969, manufacturing's share of total employment in the U.S. fell to just over 11% by 2000, the ratio in Alabama remained at roughly 15%. In sum, while employment in the manufacturing sector has been on the decline across the nation, Alabama has retained a relatively large share of its employment in manufacturing, even predating the use of industrial recruitment incentives.

Figure 8.2: Ratio of Manufacturing Employment to Total Employment, 1969-2000



Source: Bureau of Economic Analysis

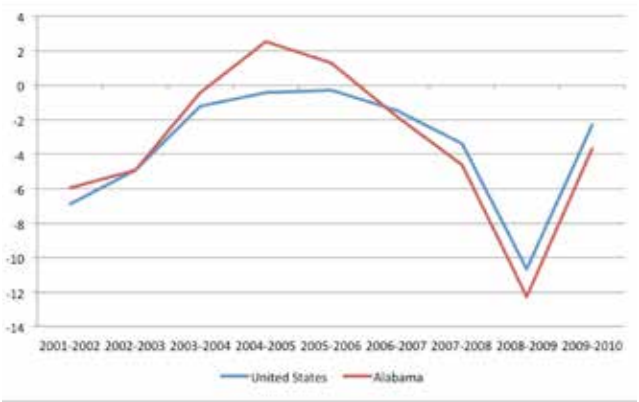
While declines in manufacturing for both Alabama and the country as a whole are apparent, the rate at which the sectors are shrinking is important. **Figure 8.3** shows the annual growth rates for manufacturing employment in the United States and Alabama from 1969-2000. Early in the sample, Alabama experienced less severe declines in the manufacturing sector than the United States as a whole, but from roughly 1972-1984 the rate of growth in the sector mirrored the national growth rate almost exactly. From the mid-eighties through the early nineties, however, Alabama experienced growth in the sector in spite of national declines. This trend was reversed in the late-nineties, with United States growth outpacing state growth.

Figure 8.3: Annual Percentage Growth Rate in Total Manufacturing Employment, 1969-2000

Source: Bureau of Economic Analysis

More recently, Alabama's manufacturing sector growth has outpaced the national rate. **Chart 8.4** presents annual growth rates for 2001-2010. From 2003-2006, Alabama experienced modest positive growth in manufacturing employment, while the US as a whole continued to experience declines. High profile agreements with Hyundai and Honda were reached in the years preceding this above-national-average growth. From 2006-2010, however, changes in manufacturing in Alabama again mirrored the national average.

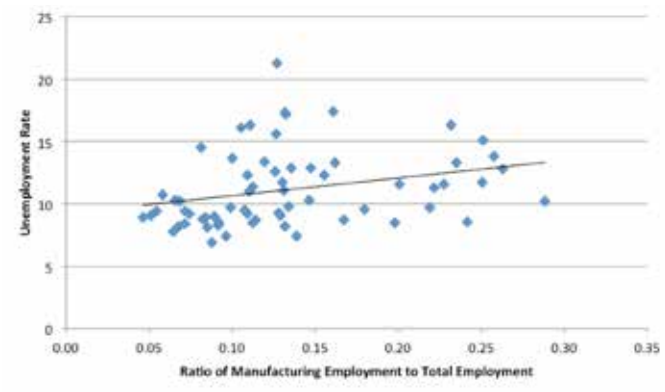
Figure 8.4: Annual Percentage Growth Rate in Total Manufacturing Employment, 2001-2010



Source: Bureau of Economic Analysis

For Alabama, the claim that focusing on manufacturing is essential to prosperity appears dubious. **Figure 8.5** plots the 2010 unemployment rate against the ratio of manufacturing to total employment for each county in the state. Only a slight positive correlation is observed, suggesting that a higher dependence on manufacturing is associated with a higher unemployment rate.

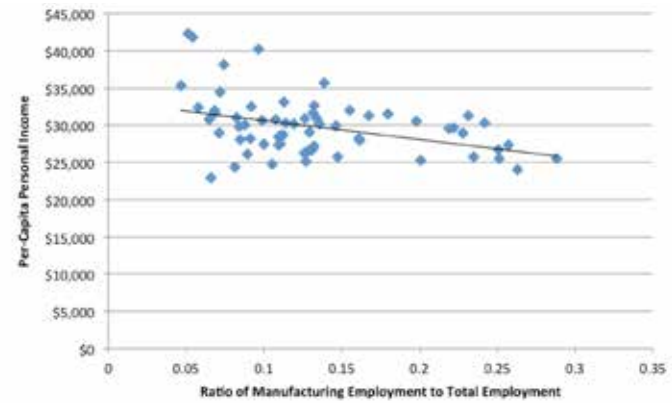
Figure 8.5: Correlation between Ratio of Manufacturing Employment to Total Employment and Unemployment Rate: 2010



Source: Bureau of Economic Analysis

An alternative claim for a focus on manufacturing is that it provides high paying jobs. **Figure 8.6** plots the same ratio against 2010 per-capita personal income for the counties and shows a slightly *negative* relationship between the two.

Figure 8.6: Correlation between Ratio of Manufacturing Employment to Total Employment and Per-Capita Income (2010)



Source: Bureau of Economic Analysis

As a matter of policy, Alabama has clearly devoted considerable resources to the recruitment of firms promising to invest in large-scale facilities with the intention of strengthening its already well-established manufacturing sector. These general historical statistics suggest that these programs may have contributed to the continued above-average size of the manufacturing sector in the state, though they also provide evidence that Alabama's dependence on manufacturing has always been high relative to the national average. The following section provides a more detailed discussion of some high profile incentive packages within the state.

4. Tax Packages in Alabama

Alabama has a long history of using tax incentives to attract high-profile businesses to the state. This section analyzes the effect on local employment of five recent tax deals: Mercedes-Benz (1993), Honda (1999 & 2002), Hyundai (2002), National Alabama Corporation (2007), and ThyssenKrupp (2007). Each of these packages was designed to recruit a high-profile manufacturing company with no previous connection to the state. The specific incentives included in each package are detailed, as reported in primary sources (i.e. the original agreements or memorandums of understanding between Alabama and the corporation), media reports, Alabama state agencies, and the corporations' own press releases. Data on employment, earnings, and other economic variables are from the Bureau of Economic Analysis[35] and the Alabama Department of Industrial Relations.[36]

Mercedes-Benz, Tuscaloosa County, 1993

Widely considered the deal which put Alabama on the map in terms of manufacturing (with the automotive industry in particular), the state's 1993 recruitment of Mercedes-Benz's first American manufacturing facility was a monumental event in its development policy. The initial agreement called for Mercedes-Benz to make a $300 million investment, eventually employing 1,500 workers. The deal proved that Alabama could attract high-profile multinational firms, and suggested that the aggressive use of tax incentives was an effective tool in recruiting a targeted company. The deal is widely viewed as a success, as the plant has been in continual operation since 1997, and currently employs some 3,000 workers.[37] Its success has been cited as the reason why other foreign car manufacturers would choose to make Alabama their American home in the future.

The Mercedes-Benz incentive package visibly served as the blueprint for subsequent tax deals. The package included a variety of tax breaks, promises to provide services, and direct payments for things such as construction costs. The state Alabama agreed to waive or reimburse all fees (where it is legal to do so) and provide assistance with securing the necessary permits and licenses, ensure that Mercedes-Benz has minimal franchise tax liability, and receives all tax exemptions and credits to which it is legally entitled. These incentives include ten-year abatements of state and local non-educational real and personal property taxes and sales taxes, plus abatements of any deed or mortgage taxes. The training facility located at the project site is exempt from real estate property taxes as well.

Alabama offered other non-tax incentives including provision of necessary environmental impact analyses, economic impact studies, and indemnified Mercedes-Benz for any penalties related to violations of environmental laws at the site. The state also secured the land for the plant and conveyed it to the company at essentially no cost. The agreement included a promises to maintain a fleet of Mercedes-Benz vehicles and that the University of Alabama will provide German language classes, and an offer to rename a nearby highway the "Mercedes-Benz Autobahn."

The state was largely responsible for paying for the construction of the facility. The agreement called for Alabama to pay for preparation of the site, at an estimated cost of $12.4 million. The government was also responsible for providing and improving infrastructure, including roads estimated at $50 million, water and sewer services, rail lines, access to other utilities, zoning, space at the Port of Mobile, and construction of a $600,000 fire station nearby. Finally, Alabama and the Tuscaloosa County Industrial Development Authority paid $42.6 million and $11 million respectively (financed from bonds) towards construction of the plant.

The state agreed to pay for the construction of a training facility, and $5 million per year for its operation. Additional start-up training costs, including airfare, hotels, and per diems for executives coming from as far away as Germany, and a temporary training facility were also provided. In all, the agreement called for the state to pay between $60 and $90 million for training services.

The estimated total cost to taxpayers of the Mercedes-Benz incentive package, including the tax abatements, was at least $253 million.[38] Since the original agreement in 1993, several expansions at the Mercedes-Benz facility have been subsidized by additional tax incentives and subsidies including $119 million in 2000 and $11 million in further abated property taxes in 2009.[39]

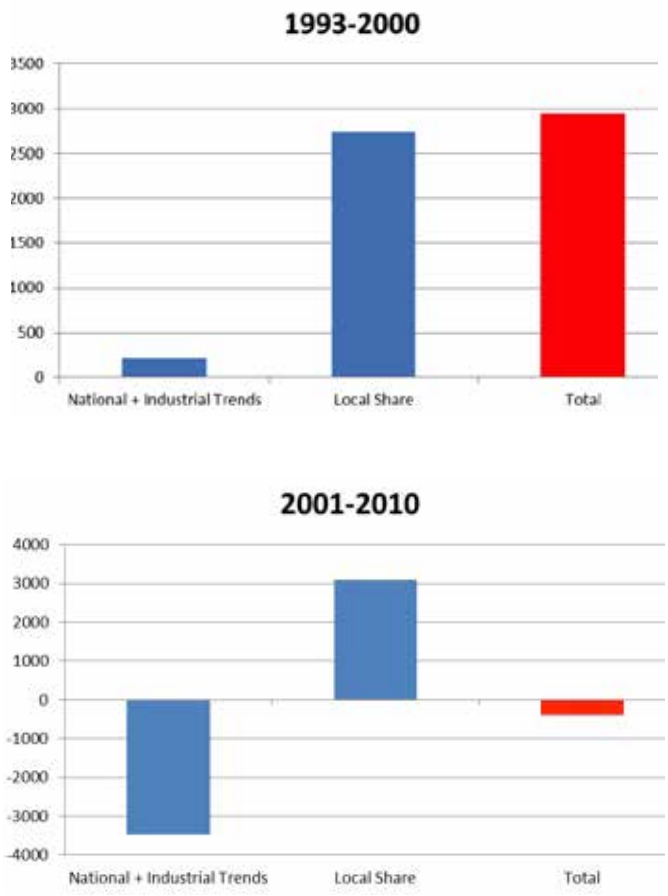
For the initial agreement of 1,500 workers, taxpayers paid $170,000 per directly-created job over the lifetime of the tax breaks, with the average manufacturing job in Tuscaloosa County earning $43,000 per year in 1997, the year the plant began production.[40] Given the average individual income tax rate in Alabama of just under 5% (the highest marginal rate of 5% is placed on all income over $3,000) these jobs generated just over $2,000 each in state income tax revenue that year.

The Mercedes-Benz U.S. official website touts an annual economic impact of $1.5 billion, roughly 3,000 employees, and claims responsibility for more than 22,000 direct and indirect jobs in the region.[41] A 2002 report in the *Savannah Morning News* on the impact of the Mercedes-Benz facility on the town of Vance (where the plant is located) found that much of this return accrued outside of the immediate vicinity of the plant; after an initial period of excitement following the beginning of construction, little to no benefits were felt there. The majority of workers at the plant commute from nearby (and much larger) Tuscaloosa, where Mercedes-Benz workers represent only a small percentage of the population.[42]

Because, as noted above, employment in the manufacturing sector is on the decline nationwide, simply looking at the gain or loss of manufacturing jobs across the country as the result of a large manufacturer starting a business in a particular region may be misleading. To differentiate regional changes in employment from those that are the result of a national trend, shift-share analysis can be used.[43] While it lacks a strong foundation in economic theory, the shift-share approach is a useful back-of-the-envelope accounting tool for approaching how changes in employment in a given region compare to the averages for the nation as well as the industry itself. In other words, it attempts to separate out the portion of a change in employment in a region that is due to national trends (both overall as swell as within the industry) from the portion that is due to factors unique to the region. The shift-share technique breaks down a change in local employment in a given industry into several components: changes due to overall national economic growth (the "national" component), changes due to national trends within each industry (the "industrial mix" component), and changes that are due to factors unique to the local economy (the "competitive shift" or "local share" component).[44] This approach provides a simple, intuitive look at how a local industry is performing relative to national averages. A positive local share component indicates the local economy is relatively specialized in an industry, and is outpacing the sector's nationwide performance. Importantly, however, shift-share analysis does not speak to any causes or explanations for that growth or relative specialization, and only serves to identify local industries which are performing better (or worse) than would be expected based on national averages.

The Mercedes-Benz deal has almost certainly increased manufacturing employment in Tuscaloosa County, which increased by 3,000 jobs or 30% between 1993 and 2000. This is remarkable given that manufacturing employment grew by only 2% nationwide over the same time period, and that employment in Alabama in the sector fell by 7%. From 2001-2010, manufacturing shrank by about 3% in the county, with a loss of nearly 400 jobs.[45] Again, however, this relatively small loss is noteworthy given that the manufacturing sector shrank nearly 30% nationwide during the same decade. As **Figure 8.7** shows, the summary of the shift-share decomposition for the manufacturing industry confirms that the local characteristics of the county accounted for nearly all (2,700) of the jobs created from 1993-2000 and significantly offset the losses associated with the overall national decline in manufacturing from 2001-2010.

Figure 8.7: Changes in Manufacturing Employment in Tuscaloosa County



From a tax revenue perspective, results are mixed **(Figure 8.8)**. Data from the Alabama Department of Revenue's annual report show that over the past decade (2001-2010) property tax revenue growth in Tuscaloosa county, which averaged 7.3% annually, was higher than in the state as a whole (5.4% average annually). The difference in sales tax revenue growth is less significant, with Tuscaloosa County averaging growth of 3.2% annually, while the state averaged 2.2% annual growth from 1997-2010. Evidence of a significant increase in investment in the county is lacking. From 1997-2010, Tuscaloosa County experienced an average annual growth rate of 6.4% in the taxable assessed value of property in the county, while Alabama as a whole saw average annual growth of 6.1%. In the years following the deal (1997-2001) income tax revenue in the county grew at an average rate of 3.4 % annually, identical to growth in the state as a whole over the same time period.

Honda, Talladega County, 1999 & 2002

Alabama's continued efforts to recruit foreign auto manufacturers resulted in a May 1999 agreement with Honda chose Alabama as the site of its first American production facility, with plans to invest $300 million and employ 1,500 workers. When compared to the Mercedes-Benz incentive package, the initial Honda agreement was relatively small at only an estimated $158 million, but was subsequently followed by a second agreement in 2002, which was itself subsequently amended in 2008 with additional incentives.[46] As with the Mercedes-Benz package, the Honda deal includes a waiver of fees and licenses, and assistance in securing all available tax credits and exemptions. The state also promised to provide access to nontaxable bonds, produce the necessary environmental and economic impact reports, and assist in securing other sources of credit.

The tax incentives are similar as well, with Honda receiving abatements of all real and personal property taxes designated for non-educational purposes, as well as taxes related to deeds and mortgages. The state also exempts the facility from real estate property taxation, and also purchased the land for the project. The agreement required Alabama to provide some $20.5 million in site preparation, as well as infrastructure improvements including roads, water/sewer, fire protection, rail, and other utilities. The agreement also required the state to pay $10 million for construction of a training facility, and $30 million for start-up training.[47]

In 2002 when Honda announced intentions to expand production by 2,000 employees through $425 million in additional investment, Alabama once again offered a variety of incentives. All previous abatements were renewed in the 2002 agreement, with the state also promising an additional $9.5 million for site preparation and $1 million for improvements in the area's water supply. Finally, an additional $45 million for training was included in the 2002 agreement. According to Good Jobs First, the total value of these incentives and abatements can be estimated at $90 million. The agreement was modified once again in 2008 to allow for an additional $600,000 payment by the state for road projects, $4 million for additional water services, and an additional $1 million for training.

Today, Honda claims 4,000 employees and a total investment in Alabama of $2 billion on its official website.[48] Manufacturing employment declined in Talladega County between 2001 (a year between the two agreements discussed here) and 2010 by nearly 8%, which is substantially less than the overall contraction of the national manufacturing sector of nearly 30% (see **Figure 8.9**). The positive local share suggests factors unique to the local economy (including the Honda deal) helped mitigate what would have otherwise been a large loss of manufacturing jobs.

Figure 8.8: Growth in Tax Revenue in Tuscaloosa County (Annual Growth Rate, 2003-2010)

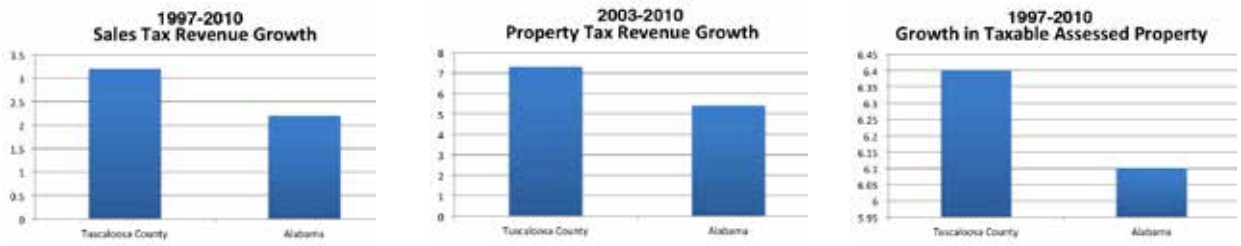


Figure 8.9: Changes in Manufacturing Employment in Talladega County (2001-2010)

Alabama Department of Revenue data shows total property tax revenues in Talladega County grew on average by 6.6% annually from 2003-2010 compared to average annual growth of 5.4% in the state as a whole (**Figure 8.10**). State sales tax revenues collected in the county grew on average 4.3% annually over the same time period, compared to average annual growth of 4% across the state. One significant observable difference is that in the years following the Honda deal (2003-2010) the assessed value of property in Talladega County grew at an average of roughly 8% annually compared to average annual growth of only 5.2% across the state. This may indicate significant increases in investment within the county, though the lack of a similarly large difference in property tax revenue growth is likely due to the various tax abatements in place.

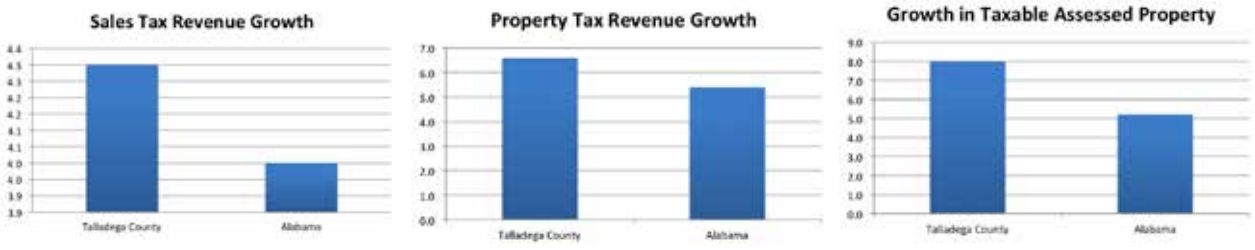
Hyundai, Montgomery County, 2002

The most recent high-profile automotive manufacturer drawn to the state through industrial recruitment was Hyundai, with an April 2002 agreement to invest $1 billion in a manufacturing facility. By this time, nearly a decade after the Mercedes-Benz deal, a standard set of incentives designed to attract automotive manufactures had been established, and the Hyundai package looked very similar to those that had come before it.

Alabama once again abated state and local non-educational property taxes, sales taxes, and mortgages taxes for the maximum period allowed by law (at the time) of ten years. In addition to these abatements, the state provided assistance with securing permits, minimized business privilege tax liability, and ensured receipt of all exemptions and credits, including the capital investment credit. In a slight twist on the incentive structure, Hyundai's business license tax liability can be reduced by the amount of taxes paid by qualifying suppliers locating in the state, a clear attempt to get Hyundai to do its own industrial recruitment for Alabama. The Hyundai agreement also contains explicit language preventing harm to the company should tax incentive laws change (the company is allowed to renegotiate).

Once again, Alabama secured land for the site and conveyed it to the company at essentially no charge. The state provided for an economic impact report, but the agreement allowed Hyundai to comment and suggest revisions. Enterprise and foreign trade zones, each with their own set of tax incentives, were expanded to include the Hyundai facility, and the agreement explicitly states that the company is under no obligation to hire Alabamians. The state also paid for site preparation, which amounted to $12.5 million, with any charges above that amount paid by the company. The 'standard' infrastructure improvements must be made by Alabama as well.

Figure 8.10: Growth in Tax Revenue in Talladega County (Annual Growth Rate, 2003-2010)



The Hyundai agreement includes specific provisions of penalties (in the form of refunded payments) should certain hiring thresholds not be met. Non-tax incentives included a $7 million training facility and $54.8 million in operating funds, residency waivers for employees and their families for use at state universities, visa assistance, temporary living quarters, $10 million dollars of advertising provided by the RSA, and a requirement that the state pay for the groundbreaking ceremony. All told, the incentives and abatements total roughly $252 million.

The official Hyundai Motor Manufacturing Alabama (HMMA) website notes that their Montgomery facility had 3,700 employees as of 2011, with an annual payroll of $223 million. The same web page also notes that an economic impact study conducted by Auburn economics professor M. Keivan Deravi found that HMMA and its suppliers generated 2% of the state's GDP.[50] The data in **Figure 8.11** support these claims: from 2002-2010, employment in Montgomery County's manufacturing sector increased by nearly 12% while the manufacturing sector shrank by 22% in both Alabama and the rest of the U.S.

Figure 8.11: Changes in Manufacturing Employment in Montgomery County (2002-2010)

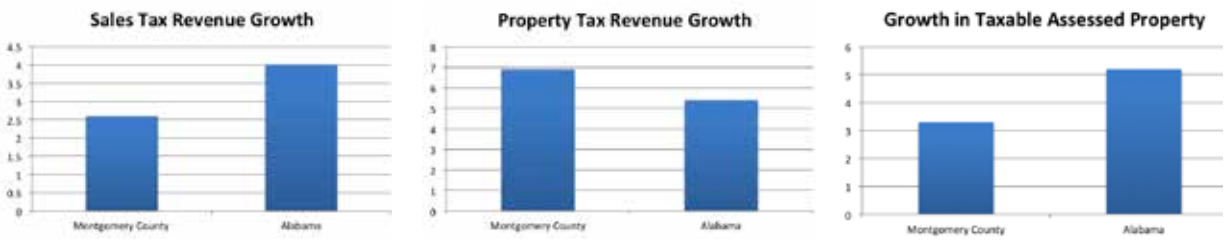
Tax data shows that in the years following the tax deal (2003-2010), average annual property tax revenue growth in Montgomery County outpaced the state as a whole at 6.9% compared to 5.4% (**Figure 8.12**). Sales tax revenue data shows average annual growth of revenues in the county of only 2.6% compared to 4% statewide. Taxable assessed value of property in the county grew at an average rate of 3.3% from 2003-2010 in Montgomery County, compared to growth of 5.2% in Alabama as a whole. In the years prior to the tax incentive (1997-2001), however, average growth in assessed property value in the county was roughly 3% annually compared to 7.5% statewide. In other words, while statewide growth in property value slowed significantly between the pre and post incentive years, the rate of annual growth in assessed value of property in Montgomery County remained constant.

National Alabama Corporation, Colbert County 2009

The National Alabama Corporation, a subsidiary of a Canadian rail car manufacturer, entered into an agreement with the state of Alabama in July 2007 to build a manufacturing facility in Colbert County, with the intention of eventually having as many as 1,800 employees. According to the agreement, the state provided incentives to National Alabama including provision of all the necessary environmental impact analyses, economic impact report, as well as a promise to help the company obtain "the full benefit of all statutory tax incentives for which the Company is legally eligible." Specific incentives provided by the state include abatement of the non-educational portion of state and local real and personal property taxes (for a period of ten years) and sales taxes levied on certain types of construction or manufacturing equipment. The estimated value of these abatements (as stated in the report) totals roughly $11 million. The agreement also stipulates that the new facility would qualify for special income tax credits and not be subjected to taxation on inventory. The state also agreed to introduce 'special tax legislation' designed to extend tax credits on behalf of National Alabama at a later date.

In addition to these tax abatements and incentives, Alabama agreed to pay National Alabama $20 million ($1 million per

Figure 8.12: Growth in Tax Revenue in Montgomery County (Annual Growth Rate, 2003-2010)



year over twenty years) for partial reimbursement of its costs related to improvements required to make the project site suitable for plant construction. The agreement also includes several conditions related to the possibility of Colbert County being included in the Gulf Opportunity Zone. When this did not happen, a portion of the agreement requiring the state to pay National Alabama an additional $53 million and Colbert County to pay $25 million came into effect. Of this, Alabama was required to pay $13.25 million and Colbert County $2 million upon commencement of construction of the facility. In sum, cash payments owed by the state and local governments to National Alabama totaled about $35 million.

According to the agreement, the remainder of these payments by the state and county ($28 and $23 million respectively) come due once the facility employs certain numbers of workers, up to the projected maximum of 1,800. An additional $10 million is to be made available for training. Other non-cash incentives paid for by the state include the land for the facility (estimated to be worth $10 million), provision of infrastructure (including roads, water, and sewage treatment), training services, and the establishment of a welding school at Northwest Shoals Community College. The plant was also funded in part by a $350 million loan from the Retirement Systems of Alabama (RSA), Alabama's state pension fund.[51]

The National Alabama plant has failed to live up to expectations. While the agreement was never supposed to produce immediate results (and as of this writing only five years have passed), the sheer magnitude of the failure makes an analysis possible. By 2010, the company was in such financial distress that the RSA stepped in to take complete control of the facility, reportedly paying another $275 million. Months later, the plant employed only 120 workers.[52] At that point, the promised cash incentives already owed by state and local governments amounted to about $300,000 per job created, compared to the total wages per manufacturing job in Colbert County of $47,835.[53] Adding the value of the non-cash incentives related to construction of the facility makes the cost-per-job ratio even worse.

By October 2010, government officials were no longer making the agreed-upon $1 million per year incentive payments.[54] Eventually, National Steel Car's (the parent company of the Alabama plant) CEO was indicted on securities fraud charges related to the RSA's investment in the plant, which were ultimately dismissed after he agreed to pay RSA $21 million in damages.[55] In 2012, the facility was leased to another company, Navistar; as of March 2014, Navistar employed 250 workers at the plant.[56] Navistar, in turn, subleased a portion of the facility to FreightCar America, which recently announced plans to expand its operation and add an additional 150-200 workers to its own existing 500 employees at the site.[57]

ThyssenKrupp, Mobile County, 2007

Alabama engaged in a fierce competition with Louisiana to secure ThyssenKrupp's (TK) first American steel manufacturing plant, a total investment estimated at the time to be nearly $4 billion. The memorandum of understanding between TK and Alabama, dated May 14, 2007, is over 100 pages long, indicative of the largest incentive package offered by the state to date. The TK deal was fundamentally more aggressive than those that have come before it, with a special piece of legislation dubbed the "Mega-Project Tax Incentive" allowing for an expansion of a number of incentives and abatements.

The state agreed to either pay for or reimburse a variety of fees related to necessary permits, and also offered 'preparatory real estate due diligence' in the form of relocating or otherwise mitigating any cemeteries, historic properties, natural resources, or protected species and habitats on the project site. TK was not to be held responsible for any damage done to any sensitive areas on the property.

The list of tax incentives promised to TK is extensive. Upon request, Alabama is required to help the company minimize its income tax liabilities, and in particular ensure that TK receives all tax credits to which it is entitled. Non-educational ad valorem real and personal property taxes, sales taxes, and deed/mortgage taxes, are abated for the length of the project. Additionally, the "Mega-Project Tax Incentive" was enacted, which exempts TK from property taxes for 20 years (compared to the ten-year abatement offered in the past), utility taxes from ten years, and extends the

income tax capital credit from 20 years to 30 years. The total value of these abatements is estimated to be $350 million.[58] The agreement also stipulates that Alabama and Mobile County are responsible for making a $314 million cash grant to TK.

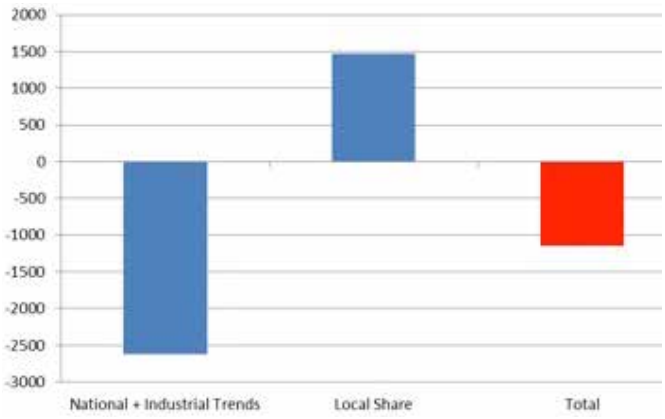
Additional non-tax incentives include the state agreeing to purchase all rights to the land for the facility (estimated at $45 million) and to purchase $100 million worth of title insurance. The state also agreed to remove any noise restrictions, and to purchase and convey to TK a neighboring property which would be adversely affected by the construction. Alabama was also required to make substantial infrastructure improvements, including rail, roads, and utilities. Incentives related to the training of employees include $31 million in reimbursement to TK, construction of a $12 million training center and five years of $5 million in annual operating funds for it, provision of a temporary training space until the permanent facility is completed, and creation of a "Steel Manufacturing Technology Program" at the center, in cooperation with the Alabama College System.

In sum, estimates of the incentive package's total cost to taxpayers surpass $800 million. The extended (by way of the "Mega-Project" legislation) state income tax capital credit is not included in this figure, and has been estimated to be worth as much as $3.7 billion over the 30-year period.[59] Provisions in the agreement, however, stipulate that TK is only entitled to the entire package if it employs 2,000 workers by the two-year anniversary of the project's commencement. The agreement also requires periodic updates from TK to the state regarding the number of its employees. In 2011, the incentive package was expanded to include an additional estimated $600 million in tax abatements, bringing the total value of the package (not including the potential from the income tax capital credit extension) to over $1 billion. The expansion of the incentive package was in response to a similar expansion in TK's investment, to $5 billion (Amy 2011).[60]

According to the TK Steel USA official website, the facility in Mobile County currently employs 1,800 workers, with continued plans to expand to the promised 2,700.[61] According to the Alabama Department of Industrial Relations, in 2011 wages paid per manufacturing job in Mobile County were roughly $58,000.[62] At the current 1,800 workers, the incentive package breaks down to roughly $555,555 per directly-created job. At full capacity of 2,700 employees, that number falls, but remains high at $370,000 per job. An impact study issued shortly after the signing of the agreement estimated some additional 4,300 indirect jobs.[63] Using this alternative number brings the per-job cost of the project down to $142,857, still almost three years' worth of worker wages. Finally, in late 2012 TK announced its intention to sell the Mobile facility.[64] The sale was completed in late 2013, with international firms ArcelorMittal and Nippon Steel jointly purchasing the plant for $1.55 billion. [65]

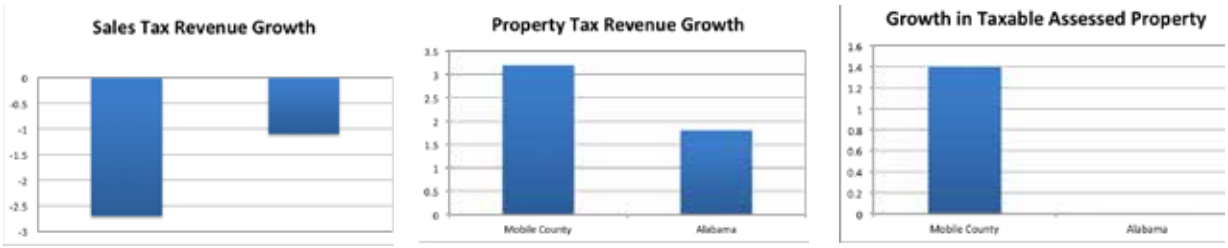
The employment data in Mobile County show a relatively strong manufacturing sector, especially given the extreme downturn in the sector nationally over the period in question (2007-2010). Since the agreement was signed, Mobile County's manufacturing employment fell by almost 7%, much less than the decline of more than 15% across the country as a whole. Indeed, total employment across all sectors has of course fallen nationally during the recent recession. The data in **Figure 8.13** reflect this, with Mobile County's local share indicating almost 1,500 jobs added due to features unique to the local economy, relatively close to the 1,800 workers employed at TK.

Figure 8.13: Changes in Manufacturing Employment in Mobile County (2007-2010)



In the years following the incentive deal (2008-2010) property tax revenues in Mobile County have grown at an average annual rate of 3.2% compared to the statewide average annual growth rate over that same period of 1.8% (**Figure 8.14**). Sales tax revenues, however, have decreased in the county at an average rate of 2.7% compared to a decrease of 1.1% annually statewide. The assessed value of property in Mobile County has grown at an average rate of 1.4% from 2008-2010, compared to virtually no growth statewide over that same period. This may indicate an above-average increase in investment in the county since for the years prior to the incentive package (1997-2006) the average annual rate of growth in property values for Mobile County and

Figure 8.14: Growth in Tax Revenue in Mobile County (Annual Growth Rate, 2008-2010)



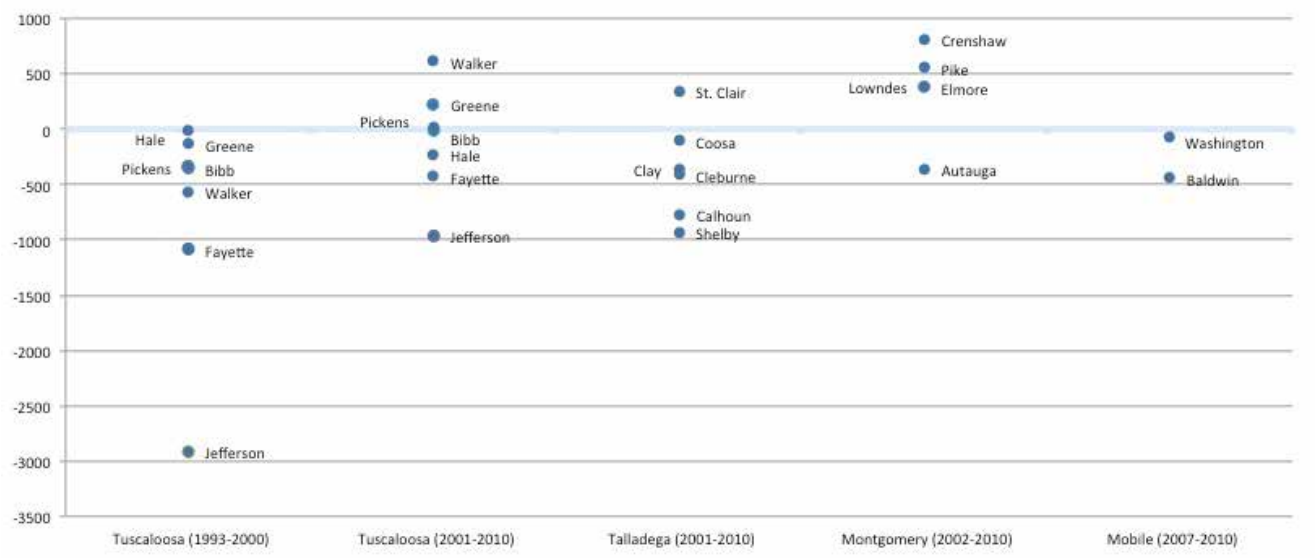
Alabama as a whole were quite similar to one another (8.4% and 7.9% respectively).

While the above data suggests relatively strong manufacturing sectors in many of the areas where Alabama's tax incentive deals have been implemented, evidence from surrounding areas is less conclusive. **Figure 8.15** presents data on the local share component for manufacturing in the counties surrounding the areas discussed above. With a few exceptions, manufacturing sectors in these counties have a negative local share, indicating they preform worse than national and industry trends would predict. The Mercedes deal in Tuscaloosa County appears to have had no measurable spillover effect on manufacturing in surrounding counties, which averaged a loss of 18% of manufacturing jobs from 1993-2000, and another 17% from 2001-2010. Most striking is that in the years immediately following the Mercedes-Benz deal (1993-2000), manufacturing in neighboring counties contracted at a rate faster than the sector's decline in the U.S. as a whole, indicating a local disadvantage. Turning to the Honda deal in Talladega County, in all but one neighboring county the manufacturing sector shrank at a rate faster than the national average, indicating a local disadvantage.

Similar results are found for the areas surrounding Mobile County. The Hyundai deal in Montgomery County seems to have had the most positive spillover effects, with neighboring economies exhibiting mixed results ranging from manufacturing employment tripling in Crenshaw County to a decrease of 40% in Autauga. The employment surge in Crenshaw County was directly related to the Hyundai deal: SMART Alabama, a major supplier to the Hyundai facility, constructed a large-scale plant of its own in 2003-2004, now employing some 700 workers.[66]

As the data in **Figure 8.15** represents only the local share of employment changes, the largely negative findings indicate local disadvantages in manufacturing. Possible explanations for the relatively weak performance of manufacturing in neighboring areas include that these surrounding counties have a comparative disadvantage in manufacturing, or that they have a higher concentration of poorly-performing industries within their manufacturing sector relative to the 'typical' distribution (which may further speak to the importance of industrial recruitment in the area). Alternatively, these results may provide evidence that the boon to the areas targeted by recruitment efforts adversely affected manufacturing in surrounding areas.

Figure 8.15: Local Share of Changes in Manufacturing Employment in Neighboring Counties



5. Policy Implications

The use of tax incentives to attract high-profile, large-scale manufacturing facilities to Alabama has been pervasive, and recent events suggest it is unlikely to stop in the future. The evidence provided here and elsewhere suggests these tax deals have, in most cases, led to the creation of thousands of manufacturing jobs for Alabamians, and depending on the assumed multiplier effect, many additional indirect jobs as well. These jobs come at a substantial cost to taxpayers, however, with the value of the direct subsidies, tax abatements, and other incentives used likely reaching into the billions of dollars. There is also evidence that even if the local economy which receives the project benefits from it, neighboring economies are not similarly affected. And, in the case of National Alabama, there is no guarantee that a large investment by a corporation will yield any benefits to the community.

From a tax revenue perspective, these incentive deals have an ambiguous effect on the state's pocketbook. First and foremost, the state is (by definition) not collecting many of the taxes that would normally be paid by these corporations due to the various abatements in place. Even in cases where the agreements had explicit ending dates (such as the Mercedes incentive package) additional tax abatements have been negotiated at a later date, effectively extending the length of time the company is exempt from paying certain taxes. Data on property tax collections in the counties examined here seem to indicate a modest increase in the annual growth rate of revenues relative to the state as a whole. On the other hand, while the rate of growth in assessed property values is higher than state average in many of these counties, the various abatements in place mean that property tax revenues do not grow at the same rate.

Ideally, Alabama would be able to be competitive without the use of billions of taxpayer dollars to lure corporations. To do this, policymakers should take steps to simplify Alabama's tax structure and keep rates as low as possible. The sheer number of tax incentives, credits, and exemptions make navigating the tax code an arduous process. The fact that Alabama routinely includes provisions in its formal agreements which stipulate it must help firms locate all tax credits to which they might be entitled suggests companies already have a difficult time making sense of Alabama's tax code. Simplification will help Alabama remain attractive to business, and curb the need for tax incentives in the first place.

Simplification of the tax code will also help get Alabama policymakers out of the practice of picking winners and losers amongst businesses. While it is easy to point to the thousands of jobs created by a company awarded a tax incentive package, the "unseen" potential investment that never occurs because other firms are not able to win the same tax breaks should also be considered. Alabamians must not forget that a project which is only profitable after government intervention is likely not the most efficient use of resources. A tax code based on low rates and simple, broad rules will assure all firms are on a level playing field. If the use of incentives is to continue, Alabama must also consider the impact of such incentives on neighboring economies and potential state-based competitors.

Given their political popularity, Alabama's use of targeted incentives for industrial recruitment will likely continue and expand. A number of steps can be taken to help mitigate the adverse effects of the policy. If incentives are going to be used, Alabama should ensure provisions are in place to protect taxpayers from potential failures. A number of the incentive deals discussed here include certain punishment provisions should a company fail to hire a requisite number of employees. While these are steps in the right direction, further oversight is needed. As Buss suggests, sunset provisions requiring the periodic reauthorization of tax breaks, instead of the broad 10-20 year commitments currently used, would ensure businesses continue to make wise decisions lest they lose their government funding.[67] And in the event a firm fails, the state must be prepared to cut its losses and not fall into the trap of continuing to invest taxpayer money in a lost cause.

Transparency needs to be applied to the policymakers' side as well. The current practice of secret meetings and deals with codenames allows the government to spend taxpayer money without voters' knowledge. Without accountability, the process is too susceptible to rent seeking and special interest politics. While some degree of secrecy is likely required during the negotiation process due to the existing competition between state governments, full disclosure once an agreement has been reached should be the rule.

Finally, the exclusive focus on manufacturing firms is detrimental to Alabama. As noted above, there is no evidence that a focus on manufacturing improves employment or income prospects for Alabamians. Manufacturing's share of total employment has been on the decline in the U.S. and the state for at least the last two decades, and specializing in a declining

Sidebar: The State Economic Development Arms Race, By Daniel Sutter

Alabama is not the only state offering tax breaks and development incentives to businesses, so the question we face in the near term is, Should Alabama unilaterally stop using economic development incentives? This raises different issues from the larger question of politically managed economic development. Four arguments together suggest that sitting on the sidelines will cost less than expected.

1. *Natural Cost Advantages*. Businesses will in the absence of any development incentives locate where their costs of operation are lowest. Evidence that incentive packages have a relatively small effect on firm location decisions suggests the magnitude of operating cost differences. Alabama will not lose out on all business location decisions by unilaterally halting development incentives. Furthermore, businesses with higher costs of operating in Alabama than elsewhere attracted through incentive packages will often be in danger of failing without future incentives. Economic development successes can create a fragile state economy.

2. *The Winner's Curse*. The competition between states for businesses resembles pro sports teams' bidding for free agents. Teams decide how much to bid for a free agent based on several factors, notably the player's expected contribution on the field. The team willing to pay the most will often have overestimated a free agent's expected contribution. The team that believes a free agent's performance will not diminish over the term of a lengthy contract will tend to outbid other teams. This phenomenon, known as the "Winner's Curse," extends to economics, business, and also incentive deals for businesses. Alabama and other states will all occasionally overestimate the value of companies to the local economy. Winner's Curse suggests that Alabama will often "win" when we overvalue and possibly overpay for a company, and we will avoid instances of buyer's remorse by sitting out.

3. *Fewer Alabamians than Expected Will Benefit*. Manufacturing companies bringing thousands of jobs to our state will benefit all Alabamians, right? Yet economics suggests that far fewer Alabamians will benefit than one might imagine. Only a portion of the stockholders of the company will be Alabamians, and many persons working at the plant will come from out of state. The new economic activity and the influx of new residents will create generally only very local benefits, and we will have to look carefully to find them. Local businesses, for instance, may not necessarily benefit. Yes, a retail store or restaurant may well enjoy extra business due to new residents, but then end up paying more in rent for their site. Renters in the community will face higher rents for apartments, and streets will have more traffic. The most certain beneficiaries will be the owners of commercial and residential real estate. Local economic activity typically drives up property values. A thriving and dynamic local economy will typically boost property values, and we do not wish to discount this dynamic. Yet using tax dollars to boost the value of some citizens' property is not a legitimate purpose of limited government.

4. *No Deals, or the Best Deal for All?* A refusal to make special deals for individual businesses does not prevent us from improving Alabama's business climate. The business taxes typically waived in an incentive package, for instance, can be repealed. Alabama could combine a comprehensive business tax and regulatory overhaul with abolition of state incentive packages. Such reforms would offer our best deal to all businesses while halting additional benefits like training facilities built at taxpayer expense. Such a "best deal for all" approach may keep Alabama competitive in attracting businesses. The great political challenge Alabama (or any state) would face in foreswearing tailored deals is remorse when losing out to another state. A "best deal for all" approach might make these inevitable moments more palatable to voters and politicians.

industry is a dubious proposition. The decline of manufacturing in the U.S. is indicative of market forces and the process of creative destruction attempting to move resources from inefficient to efficient uses. At present, Alabama is using taxpayer money to prevent market forces from moving resources towards other industries. Manufacturing firms are also highly sought-after by rival states, and pursuit of them leads Alabama to promise a much more aggressive package of subsidies and incentives than other firms might require.

6. Conclusion

Alabama has a long history of using aggressive tax abatements and subsidies to attract high-profile manufacturing firms to the state. Indeed, Alabama has a long record of success in this area, from Mercedes-Benz in 1993 to Airbus in 2012. The success is not without cost, however, as the value of the various incentive packages likely reaches into the billions of taxpayer dollars.

The "seen" effects are clear. With rare exceptions, these firms have invested large amounts of capital, employed thousands of Alabamians, and exported billions of dollars' worth of goods. Depending on the multiplier assumed, the impact extends into many additional indirect jobs. However, policymakers and taxpayers must be wary of "giving away the store" to any large-scale manufacturing firm that is interested in locating in the state. Evidence presented here suggests the economic impacts in terms of employment are limited to the immediate vicinity of the investment, with neighboring economies performing significantly worse than those receiving the incentives discussed above. The process is also highly secretive, largely kept out of the view of voters, and ultimately relies on the government's ability to pick winners and losers.

Ultimately, the more Alabama can rely on its low taxes, and a more simplified tax code to attract business and less on the discretion of policymakers to handout taxpayer money, the better off the state will be. If the use of incentives is here to stay, however, the process could be drastically improved by greater transparency (by all parties), greater accountability, ensuring existing firms are not harmed, and a decreased focus on solely manufacturing.

Notes

1. Louise Story, *As Companies Seek Tax Deals, Governments Pay High Price*, The New York Times (December 1, 2012), http://www.nytimes.com/2012/12/02/us/how-local-taxpayers-bankroll-corporations.html?pagewanted=all.
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