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Sowing the Seeds

State Incentives Grow Local Companies
by Gaylen Webb

26 January 2011—

This is the place—to do business. At least that's the message that the Governor's Office of Economic Development (GOED) is trying to broadcast far and wide. GOED has an aggressive incentive program to help woo businesses to either locate or expand in the Beehive State. From fiscal year 2008 through fiscal year 2010, GOED offered \$319 million in financial incentives to businesses.

With such numbers, one might ask, is Utah spending millions to recruit out-of-state businesses, while neglecting homegrown companies? Not so, says GOED Executive Director Spencer Eccles. In 2009, more than 70 percent of those incentives were offered to Utah companies. In 2008, Utah companies received more than 60 percent of the incentives awarded.

Next question: Are such incentives corporate welfare? Spending \$319 million to receive more than \$1 billion in new state revenue certainly doesn't smell like corporate welfare. Rather, it smells like a rosy return on investment, especially when one factors in the \$2.5 billion in capital investments the incentive awardees will make, and the new jobs they will create—generating state wages of more than \$10.2 billion.

A Win-Win

The state's incentive program recently played a key role in keeping life sciences company Nelson Laboratories in the state—and helping it to grow and add jobs.

Jeffery R. Nelson, president and CEO of Nelson Laboratories, learned about the program by chance at a BIO International Convention. When foot traffic was slow at the convention, Nelson sat down to chat with Derek Miller, former deputy director of GOED, and Jeff Edwards, president and CEO of the Economic Development Corporation of Utah (EDCUtah).

At the time, Nelson was contemplating a major expansion of his company. He wasn't, however, looking for a financial incentive from the state. In fact, he didn't even know the state had an incentive program. Miller, who managed GOED's corporate recruitment and incentives program, took some time to explain how incentives can help homegrown businesses like Nelson Labs expand in the Beehive State.

Not long after their chat, the state of Missouri tendered an incentive offer for Nelson's company to expand there. Nonetheless, the initial conversation between Nelson and Miller eventually led to a post-performance tax incentive award from GOED totaling \$1,996,000 for Nelson Labs, which currently employs 360 people, to expand in Utah.

"The incentive program feels more like a self-funding job creation and retention system," says Nelson. "On one side, we receive tax relief for creating jobs, and on the other side, the state receives new tax revenue. That looks like a win-win program to me. It's a smart way to grow businesses and actually add to the tax base."

Was the incentive the only factor in Nelson's decision to stay in Utah? Absolutely not, says Nelson. "But it did make it easier for us to keep the jobs in Utah. We wanted to keep the jobs here to begin with, and the Governor's Office of Economic Development helped us find a way to do that."

In addition to Nelson Laboratories, other home-grown Utah companies that have received tax incentives for their expansion efforts include Merit Medical Systems, Inc. and Peterson Inc.

The tax incentive offered to Peterson Inc. is the first award under a new alternative energy incentive program approved by the Utah Legislature in 2009. Thanks to a five-year tax credit of up to \$344,209, Peterson will add 53 jobs over the next two years as it begins to manufacture fuel assemblies for the nuclear industry.

Petersen currently has a combined 420 employees in a 580,000-square-foot facility west of Ogden and a 204,000-square-foot facility in Pocatello, Idaho. The project is expected to produce more than \$10.6 million in new state wages over five years and more than \$900,000 in new state revenue during the same period.

The Cluster Effect

The conditions that influence a company's relocation or expansion plans may vary widely; however, government-sponsored incentives have become crucial to recruitment, as cities and states compete to woo new businesses in order to bolster their struggling economies.

In Utah, however, the state is equally as interested in retaining and expanding homegrown businesses as it is in recruiting new businesses to locate here. In fact, Gov. Gary R. Herbert has given GOED a mandate to help accelerate the expansion of Utah businesses—especially those businesses working in eight specific industry clusters that have high growth potential and pay higher than average wages. Those industry clusters are:

- Software and information technology
- Defense and homeland security
- Aviation and aerospace
- Corporate headquarters
- Energy and natural resources
- Financial services
- Life sciences
- Outdoor products and recreation

Why is the corporate recruitment and incentive program limited to these eight specific industries? Simply put—because of their high growth potential and high wages. Utah's cluster industries have generated 8.1 percent of the job growth since 2005, compared to overall employment in Utah, which grew 0.5 percent during the same period, according to GOED figures. What's more, the average wage earned by an employee in one of Utah's cluster-related industries is 62 percent higher than the state average monthly salary.

Eccles says the incentives are generally awarded to companies that create new, high-paying jobs that help improve the standard of living, diversify the state economy, increase the tax base, attract and retain top-level management, and encourage graduates of in-state universities to remain in Utah.

Incentive amounts and durations are decided by the GOED Board and executive director, based upon statutory guidelines and evaluation criteria that includes the financial strength and historical stability of the

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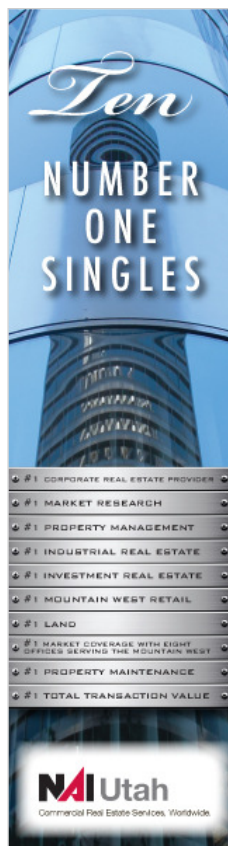
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company, the number and salary of jobs created, amount of new state tax revenue, long-term capital investment, competition with other locations and whether the company is in a targeted industry.

Despite its importance to economic development, Utah's tax incentive program may be an enigma to some Utah businesses. GOED would like to change that, to help even more businesses expand in the state. Eccles says a variety of incentives are available; however, the two most common incentive programs used to retain or recruit businesses are Economic Development Tax Increment Financing (EDTIF) tax credits and Industrial Assistance Fund (IAF) grants.

EDTIF incentives are post-performance, refundable tax credits for up to 30 percent of new state revenues, including state corporate, sales and withholding taxes, over the life of the project, which is typically five to 10 years. IAF incentives, on the other hand, are post-performance grants for the creation of high-paying jobs. GOED has the flexibility to offer either of the incentive types or a blend of both.

"Obviously, certain requirements have to be met before we award an incentive," says Miller. "We aren't giving away free land or free money. The incentives come in the form of grants or tax relief, but they are always performance-based, meaning a company must add jobs and create economic development for the state before receiving any benefit."

A Strong ROI

The corporate recruitment and incentive program was not designed to support the natural or organic growth of a business. Rather, the incentive program is intended to be the impetus to foster something that isn't happening (retaining or creating jobs) but can happen. And the fact that all state incentives are awarded on a post-performance basis ensures a positive return on investment to the state of Utah and its residents, Eccles says.

For example, to receive its total tax incentive, Nelson Labs must create more than 350 new full-time positions over a 10-year period, with wages that average 125 percent of the Salt Lake County average. Since the county's average wage is \$41,000, Nelson Labs must pay average wages of \$51,250. The new jobs will generate wages in excess of \$157 million and new state tax revenue in excess of \$9.9 million over the 10-year period. The state's ROI for the incentive award is approximately 20 percent. In addition, the company will invest \$13 million to expand its Taylorsville facility and purchase new equipment.

To receive its full incentive, Peterson Inc. must invest more than \$2.5 million in capital improvements and pay average wages in excess of 125 percent of the Weber County average, including company contributed health benefits. Meanwhile, Merit Medical must add approximately 392 new jobs, paying \$95 million in wages over the next 10 years in order to receive its full incentive. In return, the company will receive a tax credit of \$4.36 million over 10 years. New state tax revenue generated from the expansion is estimated at more than \$25 million, adding approximately \$8 million to the state's general fund and \$13.5 million to public education over that 10 year period.

"The real genius of the program that Utah has created is that every incentive given is post-performance," says Miller. "It may sound simplistic, but we don't give away one penny in Utah without first receiving one dollar in new tax revenue. Having studied other state-level incentive programs, I truly believe that Utah's incentive program is the best thought-out, best functioning one in existence. It allows us to be competitive in high-value projects while at the same time not mortgaging our future."

Utah's incentive program has proven to be quite effective in helping businesses expand while shifting the risk to the company and away from the state. "If the company doesn't perform to the agreed upon benchmarks, the incentive is never given," Miller adds.

Applying for an incentive can be a fairly lengthy process; however, both GOED and EDCUtah offer support to businesses interested in pursuing an incentive. Nelson says there is substantial paperwork involved, plus a variety of legal reviews. Still, he says the length of the process was mediated more by his time and availability than anything else. "I ended up being the inhibitor," he explains.

Nelson Labs actually contracted with a firm to assist with its incentive application. In retrospect, Nelson says that was a mistake. "After seeing how helpful both GOED and EDCUtah are, I really didn't need to use the outside firm to apply for the incentive. GOED and EDCUtah are excellent partners to Utah businesses," he adds.

Once the incentives are accepted, GOED continues to work with the companies involved through quarterly and annual report mechanisms, which were designed to maintain the integrity of the incentives program, from both taxpayer and business perspectives. This is the first year Nelson Laboratories is being tracked in the incentive program. Nelson plans to review how many jobs his company has created and the amount of tax relief it can expect to receive. The company originally estimated it would create between 75 – 100 jobs during 2010.

While it is not the only factor involved, Miller says awarding tax incentives to Utah businesses like Nelson Laboratories, Merit Medical and Peterson Inc. is helping fulfill Herbert's mission to see that Utah excels in job creation, innovation, entrepreneurship, global business and workforce quality, and that it offers a stable and sustainable business-friendly environment.

"Utah is fortunate to have many natural incentives, such as a highly educated workforce, some of the lowest tax rates in the country, great quality of life, some of the lowest utility costs in the nation and a low cost of living. These natural incentives, combined with financial incentives, help make Utah the best state for business, and we are committed to helping home-grown Utah businesses achieve their full potential," Miller says.