



Development Incentives Revisited: A Guide for Nevada Legislators

Background

Governor Sandoval called a special session in December 2015 to consider a development incentive package for Faraday Future, which has decided to locate in North Las Vegas. The goal of this policy brief is to (1) identify best practices for crafting development incentive programs, and (2) offer a set of recommendations for improving Nevada's return on investment (ROI) on the proposed Faraday Future incentive package.

What issues should Nevada's Legislators consider?

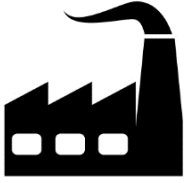
- Greater Accountability: Is our current system of accountability and evaluation sufficiently rigorous?
- Demands on Existing Infrastructure and the Cost of New Infrastructure: Has Nevada identified sufficient revenue streams to respond to an increased demand on infrastructure and for public services?
- Job Creation: How can Nevada ensure that companies hire locally and how can the State strengthen workforce development efforts?

Recommendations for Improving Nevada's Return on Investment

- Support the proposed recapture (clawback) provision in incentive package: The proposal indicates that Faraday will pay taxes into an account and will receive rebates only after the \$1 billion investment has been made.
- Include performance-based measures in the incentive contract with Faraday: As with Tesla, Nevada should include specific employee hiring targets to ensure Faraday utilizes local resources.
- Create a workforce development training program: Nevada needs a formal, collaborative partnership to train and supply a highly skilled workforce to meet the needs of Faraday Future.
- Identify the specific impact of Faraday Future on current and proposed highway projects: Nevada needs to build up the infrastructure near the proposed facility. The Governor's Office of Economic Development (GOED) and the Nevada Department of Transportation need to specify the impact of Faraday on current/proposed highway projects.
- Establish a government commission to monitor incentive contracts and performance targets: Comprised of various stakeholders, this committee could assess and evaluate economic impacts and performance measures.
- Encourage GOED to conduct a school facilities impact: Property tax abatements can significantly affect school districts and leave them unable to respond to business related-enrollment growth. GOED should conduct a school facilities impact report and develop a funding plan that identifies existing or new funding mechanisms to address future facility needs.
- Strengthen accountability and disclosure mechanisms and standardize reporting: GOED should standardize reporting requirements that include the range of costs and benefits.

Conclusion

While there are real costs to the State, the Faraday Future deal supports the State's goal to diversify its economy with advanced manufacturing. Jointly, Tesla Motors and Faraday, once fully operational, will provide Nevada with a critical mass of advanced manufacturing knowledge and capabilities. Additionally, the Faraday Future project provides an opportunity to jumpstart the economy of North Las Vegas, thereby minimizing the need for greater State financial assistance (e.g. social programs, etc.).



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Introduction

On December 10, 2015, Nevada Governor Brian Sandoval announced that Faraday Future would locate its manufacturing facility in North Las Vegas, Nevada (Clark County). He stated that he would seek to have Nevada extend \$335 million (\$217 million in direct tax benefits) to Faraday Future to build its \$1 billion, 600-acre plant at the Apex Industrial site.

The Faraday Future deal will be reviewed by Nevada's lawmakers in the 29th Special Session that will commence on December 16, 2015.¹ Governor Sandoval is calling a special session because several of items included in the proposed incentive package are not allowed under existing law.²

The goal of this policy brief is to (1) identify best practices for increasing the return on the State's proposed investment, (2) identify lessons learned from the Tesla Motors incentive package; (3) and offer a set of recommendations for improving the ROI of the proposed Faraday Future incentive package.

What are the components of the proposed Faraday Future deal?

Faraday Future is a Chinese conglomerate-backed start-up whose founder has built his fortunes in technology and media companies. Currently based in Gardena, California where it has been developing its first model, Faraday Future plans to roll out its line of electric cars in 2017.³ Faraday Future's business model rests on building an electric car with built-in connectivity whereby car owners can purchase

¹ Over the course of Nevada's legislative history, special sessions have been called only 28 times. Most recently, a special session was called in September 2014 to consider a \$1.3 billion package of tax credits and incentives. In 2013, a special session was called to address "several issues that remained unresolved when the regular session ended, including legislative approval for an increase in the Clark County Sales and Use Tax, economic development, class-size reduction, charter schools, and an appropriation for the Millennium Scholarship" (Nevada Legislature, http://www.leg.state.nv.us/Division/Research/Publications/Factsheets/SpecialSessions_Summary.pdf). Five out of the last seven special sessions have lasted a single day. Prior to 2014, 1984 was the last time that a special session had been called for the explicit purpose of addressing a development incentive package for businesses. In 1984, then Governor Richard Bryan called the 15th Special Session to change the banking laws to allow for the establishment of a Citicorp call center (expected to result in 1,000 jobs).

² In 2014 during the 28th Special Session to consider an incentive package for Tesla Motors, the Nevada Legislature revised existing legislation to extend tax credits and abatements to companies that "invest[ed] at least \$3.5 billion in this State within the 10-year period" (Nevada Revised Statute 360.945). Now, the Legislature must revisit that law and lower the investment threshold in order to allow Faraday Future, who is projected to invest \$1.0 billion, to apply for relevant tax abatements. Additionally, under the current tax abatement program, businesses are eligible for a 50 percent break on property and modified business taxes and a partial abatement on sales and use taxes for equipment purchases for a limited time. However, the proposed Faraday Future deal abates 100 percent of sales and use taxes and 75 percent of property and payroll taxes for an extended period of time (10-15 years).

³ David Welch. "Chinese-Backed Startup Targets Tesla With \$1 Billion U.S. Plant," *Bloomberg News*. November 5, 2015. <http://www.bloomberg.com/news/articles/2015-11-05/chinese-backed-startup-targets-tesla-with-1-billion-u-s-plant>

"subscriptions for connective services, apps, and other infotainment."^{4,5} While the company intends to compete with Tesla, Faraday Future, unlike Tesla, has not yet unveiled a product. Faraday Future selected the North Las Vegas site after considering locations in Georgia, Louisiana, and California.

Governor Sandoval has proposed \$335 million in tax incentives and credits, and additional infrastructure investments, making this tax incentive package approximately one-quarter the size of the \$1.3 billion incentive package offered to Tesla Motors in 2014, which, at the time of approval, was ranked as one of the top 10 biggest mega-tax incentive deals in the country.⁶

Benefits to Faraday Future (Direct and Indirect Costs to Nevada)

The components of the deal include roughly \$335 million in direct and indirect benefits, including state tax incentives and infrastructure investments.⁷ The value of direct tax incentives is roughly \$217 million. If the incentive package is approved, Faraday Future would receive:

- \$175 million in direct sales, payroll, and property tax abatements over 10 to 15 years; and
- \$38 million in the form of transferable tax credits, worth \$9,500 per employee for up to 4,000 jobs. The average wage of jobs must be \$22 per hour to qualify.

The current Faraday tax incentive proposal contains recapture provisions that are stronger than those included in the Tesla Motors tax package. As proposed, Faraday Future will receive the standard abatements and will pay taxes into a fund (or escrow account) that will be rebated *only after* the \$1 billion investment target has been achieved.⁸

Additionally, the State will provide 25 megawatts (MW) of electricity (over a ten year period) through its Economic Development Rate Rider Program, which provides a discounted base tariff rate. Based on a similar deal offered to Tesla Motors, the value of this item could amount to \$8 million.

Currently, the Apex Industrial park lacks the infrastructure to supply power, water and gas. As part of the incentive package, Nevada will invest roughly \$120 million in new infrastructure development. As proposed, Nevada will use \$50 million in Nevada Highway Trust Fund monies to widen a five-mile stretch of U.S. Highway 93 near the park and construct a "flyover" section of road in order to improve access to the site. Nevada will allocate another \$70 million (raised through bonds) to "ensure a municipal water infrastructure system is available at the project site" and to construct "a rail port and associated rail infrastructure."⁹

⁴ David Welch. "Chinese-Backed Startup Targets Tesla With \$1 Billion U.S. Plant," *Bloomberg News*. November 5, 2015. <http://www.bloomberg.com/news/articles/2015-11-05/chinese-backed-startup-targets-tesla-with-1-billion-u-s-plant>. According to founder Jia Yueting, "[Faraday Future] plan[s] to revolutionize the automobile industry by creating an integrated, intelligent mobility system that protects the earth and improves the living environment of mankind, so that everyone can breathe clean air and enjoy a seamlessly connected lifestyle." Source: Joann Muller. "Chinese Billionaire Confirms He's Behind Electric Car Company Planning \$1B Factory Near Las Vegas," *Forbes*. December 9, 2015. <http://www.forbes.com/sites/joannmuller/2015/12/09/chinese-billionaire-confirms-he-plans-1-billion-electric-car-factory-near-las-vegas/>

⁵ "Faraday Future is Mysterious Automaker Taking on Tesla," November 16, 2015.

<http://www.automotive.ventures/faraday-future-is-mysterious-automaker-taking-on-tesla/>

⁶ Ryan Frank. "Nevada's tax deal for Tesla would be one of the largest in U.S. history." *Las Vegas Sun*. September 4, 2014. <http://www.lasvegassun.com/news/2014/sep/04/nevadas-tax-deal-tesla-would-be-one-largest-us-his/>

⁷ Megan Messerly and Daniel Rothberg. "Lawmakers to consider \$335 million in incentives for Faraday Future," *Las Vegas Sun*, December 10, 2015. <http://lasvegassun.com/news/2015/dec/10/lawmakers-to-consider-335-million-in-incentives-fo/>

⁸ Nevada Governor's Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

⁹ Nevada Governor's Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

Additionally, Governor Sandoval has proposed roughly \$3 million for a new workforce grant program, the Workforce Innovations for the New Agenda (WINN) Fund, to support the workforce needs of Faraday Future. The purpose of WINN is to develop a robust, collaborative program that would provide training for up to 4,000 automobile assembly workers at the facility.

Table 1. Components of proposed Faraday Future benefit package

Incentives	Amount
Sales and Use Tax, Property Tax, Modified Business Tax Abatements	\$175M
Transferable Tax Credits	\$38M
Discounted Energy Rates (Economic Development Rate Rider program)	~\$8M*
Workforce Development Fund (WINN)	\$3M
Infrastructure Investment Benefits	\$120M
Total Benefits to Faraday Future	~\$335M

* Value based on the Tesla Motors deal, which was similar in structure (10 years, 25MW of electricity)

Benefits to Nevada

Political leaders and policymakers across the Silver State have emphasized the huge gains – both direct and indirect – that Faraday Future will bring to Nevada, particularly Southern Nevada and North Las Vegas. Among the benefits of the Faraday Future \$1 billion electric car manufacturing facility are:

- 3,000 construction and installation jobs at peak construction (short-term);
- 4,500 people on site once the factory is up and running with an “average wage in excess of \$22 per hour and full benefits package”;
- \$1 billion investment on the site within the first 10 years;
- 3 million square foot automobile manufacturing facility;
- 9,000 indirect jobs; and
- \$6.0 million direct donation to K-12 education (\$1.0 million annually for six years, beginning in 2018-2019).¹⁰

Faraday has committed to ensuring that at least 50 percent of the workers are residents of Nevada. Additionally, Faraday and private landowners have committed to investing \$70 million of their own money to develop the land and will provide wastewater and storm drainage systems, and additional water infrastructure, as needed.¹¹

The anticipated job growth is promising given that the unemployment rate in Clark County stands at 6.3 percent, which remains above the national average (5.0 percent).¹² Moreover, it is anticipated that the 4,500 direct hires will earn an average wage of \$22.00 per hour, which is slightly higher than the regional average hourly wage of \$20.10.¹³

Estimates suggest that the fiscal benefits (new revenues, new expenditures) of the project are projected to reach \$760 million over 20 years, while the economic benefits (resulting from spin-off effects, wages, greater consumer spending, etc.) could amount to \$85 billion. Additionally, Faraday could boost gross regional product by up to 4 percent.¹⁴

¹⁰ Nevada Governor’s Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

¹¹ Ken Ritter and Michelle Rindels. “Nevada Governor Outlines \$335M Deal to Draw \$1B Carmaker,” *ABCnews.com*, December 10, 2015. <http://abcnews.go.com/Technology/wireStory/nevada-governor-unveils-335-million-deal-draw-carmaker-35698250>

¹² Bureau of Labor Statistics, October 2015.

¹³ Nevada Governor’s Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

¹⁴ Nevada Governor’s Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

Comparison of Faraday Future and Tesla Development Incentive Packages

Comparisons have been made between the Faraday Future proposed development incentive package and the Tesla Motors incentive package, approved in the 28th Special Session of the Nevada Legislature (September 2014). Table 2 compares the development incentive packages and projected economic and fiscal benefits.

Table 2. Comparison of Tesla Motors and Faraday Future development incentives packages

Incentives	Tesla	Faraday
Sales Tax Abatement	\$725M over 20 years; 100 percent abatement	Total of \$175M; 15 years for sales and use tax; 10 years for property tax and modified business tax (MBT); 75 percent abatement of property and MBT taxes
Property Tax Abatement	\$332M over 10 years; 100 percent abatement	
Modified Business Tax Abatement	\$27M over 10 years; 100 percent abatement	
Transferable Tax Credits	\$120M	\$38M
Energy Rate Rider Program	\$8M	\$8M ¹⁵
Credits for Jobs	\$75M	0
Infrastructure Investment Benefits	\$43M	\$120M
Workforce Development Fund	0	\$3M
Total Benefits	\$1287M	\$335M
(Short-Term) construction jobs	3,000	3,000
Direct Jobs	6,500	4,500
Indirect Jobs	16,000	9,000
Total Long-Term Jobs	22,500	13,500
(Incentive) Cost per Direct Job	\$198,000 per direct job¹⁶	\$74,444 per direct job
Benefits	Tesla	Faraday
Fiscal Benefits	\$1.9M billion over 20 years	\$760 million over 20 years
Economic Benefits	\$40 to \$100 billion	\$85 billion over 20 years
Investment in Education	\$37.5 million over 5 years, plus \$1M to UNLV for battery research	\$6 million over 6 years

¹⁵ Estimate based on the same parameters in the Tesla Motors deal.

¹⁶ Per Table 2, the cost per job at Faraday amounts to \$74,500 per worker; the Tesla Motors tax package of \$1.3 billion amounts to an average cost of almost \$200,000 per direct hire. As points of comparison: the \$89 million Apple incentive package resulted in 310 new jobs (as of 2012), reflecting an average cost of \$287,000 per job; Catalyst Fund's initial investment of \$10 million helped create roughly 3,800 jobs for an average cost of \$2,600 per job. (<https://www.leg.state.nv.us/App/NELIS/REL/78th2015/ExhibitDocument/OpenExhibitDocument?exhibitId=16031&fileDownloadName=Senate%20Committee%20on%20Finance%20and%20Assembly%20Committee%20on%20Ways%20and%20Means%20Closing%20List%202%20May%202015%202015.pdf>)

How can Nevada increase its return on investment?¹⁷

Nevada's extension of development or tax incentives is part of a widely used and long-standing economic development strategy. Cities and states frequently offer development incentives as a tool to encourage businesses to expand within and/or relocate to their jurisdictions.

However the impact of development incentives is mixed and "existing studies do not allow for clear conclusions on the cost-effectiveness of business tax credits."¹⁸ Many economists and policy analysts acknowledge that "business tax credits do lead to new revenues for state government, but not enough to completely offset the initial costs."^{19,20}

The challenge then is for state and local policymakers to "find ways to make their jurisdictions attractive without giving away the tax base, and to use incentives selectively and responsibly."²¹ While political leaders and decision-makers recognize that tax incentives are an inherent cost of doing business, a growing number of states are attempting to offer incentives more selectively, improve accountability, and employ more rigorous measures for assessing the costs (benefits) of the incentives and evaluating their impact.

In order to increase Nevada's return on investment on this economic development strategy, we identify best practices, which are based on comparative research and informed by recent experiences with Tesla Motors in northern Nevada.

Sound Incentives

Many governments offer packages that are a combination of several types of incentives including abatements and credits. Research indicates that transferable credits, including those offered to Faraday Future (and Tesla Motors) do not fare well when measured against principles of simplicity. Briefly, transferable credits are those that a business can sell to another firm, which can then apply the credit to its own tax liability.²² But these credits can be complicated to administer and they usually sell at a discount.

For instance, when the recipient company sells its credits to other taxpayers, it is difficult for policymakers to determine who receives the benefits. Because there is no requirement that the recipient company must sell its credit to a company in the same industry, transferable credits may subsidize activity that is unrelated to the original strategic nature of the development incentive. In addition, transferable credits usually sell at a discount, meaning that the selling firm receives less than their full value. The state, however, still forgoes the entire original amount.

Accountability Provisions

Often, state and local governments have laws in place requiring accountability provisions in the development incentives packages. The most common of these is called a clawback or recapture

¹⁷ This section draws heavily from the Guinn Center 2014 report, "Development Incentives: A Guide for Nevada Legislators." <http://guinncenter.org/wp-content/uploads/2014/09/Development-Incentives-Final.pdf>

¹⁸ Jennifer Weiner. 2009. State Business Tax Incentives: Examining Evidence of their Effectiveness. New England Public Policy Center Discussion Paper 09-3. <https://www.bostonfed.org/economic/neppc/dp/2009/neppcdp0903.pdf>
As noted in the study, the lack of transparency in previous studies have methodological limitations.

¹⁹ Ibid.

²⁰ For a review of the studies, see Alan Peters and Peter Fisher, "The Failures of Economic Development Incentives," *Journal of the American Planning Association* 70 (2004): 27–37.

²¹ Bill Schweke. 2009. Business Incentives Reform. Corporation for Enterprise Development: Washington, D.C. http://cfed.org/assets/pdfs/business_incentives_reform.pdf

²² Jennifer Weiner, Federal Reserve Bank of Boston. "State Business Tax Incentives: Examining Evidence of their Effectiveness." <https://www.bostonfed.org/economic/neppc/dp/2009/neppcdp0903.pdf>

provision.^{23,24} Clawbacks are clauses in subsidy laws that require a company to return all or part of the value of a subsidy if the company fails to meet the obligations agreed to as a condition of receiving the incentive package.

Performance-Based Contracts

Closely tied to recapture provisions are performance-based contracts, which means that the recipient company does not receive agreed upon benefits until it has satisfied program requirements.²⁵ In Florida, the state is protecting “the taxpayers’ investment by structuring incentive deals so that the company has to perform, wholly or partly, [...] before all or a pro-rata portion of the incentive value is realized.” Also, in Florida and North Carolina, states hold incentive grants in an escrow account until performance goals are met by the company.

Following evidence-based best practice, the Nevada Legislature included recapture or clawback and performance-based provisions in the Tesla Motors development incentive package.²⁶ For example, Tesla must uphold a number of conditions, including a minimum capital investment of \$3.5 billion and a commitment to ensure that at least 50 percent of its workers are from Nevada, or the State can recapture some share of its transferable credits and abatements (see Section 5 on Recapture Provisions in the Tesla Incentive Agreement).²⁷

While the Tesla Motors incentive package contains strong recapture provisions and performance-based benchmarks, the Faraday Future incentive package contains *even stronger* provisions. Following Florida and North Carolina, Nevada would require Faraday Future to pay taxes into a fund (or account) that will be rebated *only after* the \$1 billion investment target has been achieved.²⁸

Requiring Utilization of Local Resources

States that extend development incentives to businesses have an expectation that these businesses will hire local workers and goods from local manufacturers/suppliers. There are a number of ways that local and state governments can improve the likelihood that businesses receiving tax incentives will hire locally and use local resources. The first type of provision sets a threshold job creation requirement as a condition for receiving public assistance, which is also an example of performance-based contracting. The second provision offers a specific amount of incentive on a per-job basis, and does not provide any funds to the company until the job has been created. The advantage of “back-loading” incentives and linking them to job creation is that it provides a degree of protection to governments in the event that the company fails or falls behind in its hiring schedule.

Several states have included guidelines in their incentive packages that require businesses who receive subsidies to make “good faith efforts” to hire workers from within city (state) limits. For instance, officials can specify job marketing, solicitation, and training provisions in the contracts, including a requirement that the subsidized business advertise jobs through particular agencies.

²³ Bill Schweke. 2009. Business Incentives Reform. Corporation for Enterprise Development: Washington, D.C.

http://cfed.org/assets/pdfs/business_incentives_reform.pdf

²⁴ Good Jobs First. Key Reforms: Clawbacks. <http://www.goodjobsfirst.org/accountable-development/key-reforms-clawbacks>

²⁵ Ibid.

²⁶ Nevada Legislature. Senate Bill 1. 28th Special Session (2014).

http://www.leg.state.nv.us/Session/28th2014Special/Bills/SB/SB1_EN.pdf (Section 16)

²⁷ Nevada Governor’s Office of Economic Development. Tesla Motors Incentive Agreement. October 2014.

http://www.diversifynevada.com/uploads/reports/Tesla_-_Incentive_Agreement_-_Execution_Package.pdf

²⁸ Nevada Governor’s Office of Economic Development. Faraday Future in Nevada. December 2015.

http://diversifynevada.com/documents/Faraday_Deal_Summary_PDF.pdf

Contracts can also require a business to interview candidates referred from a specific source, such as a network of placement and training community agencies and to post job vacancies to the network's database. Governments can also obligate businesses to provide periodic hiring reports, and to retain a specific level of new hires over the life span of the incentive, and can then impose penalties for falling short in reaching hiring target goals. Development incentive contracts can also require firms to work with employment and training agencies that have been pre-qualified by the state and local decision makers.

The incentive deal with Tesla Motors required that at least 50 percent of short-term and long-term employees are Nevada residents. Tesla Motors reports quarterly to GOED and provides information on the number of Nevada residents the company has employed.²⁹ As of October 2015, almost 70 percent of construction workers hired by Tesla Motors are residents of Nevada.³⁰

Faraday Future has signaled a commitment to ensure that at least 50 percent of its workers are Nevada residents. Nevada lawmakers must leverage the success of the Tesla Motors incentive deal and include specific hiring targets for local workers. Additionally, Nevada State Legislators, working with GOED, should explore additional ways to ensure that Faraday hires residents of North Las Vegas. One policy option might entail Faraday to recruit from job connection centers located within a 10 mile radius of the Apex Industrial park.

Non-tax incentives

Increasingly, policymakers are including non-tax incentives, particularly employment-based incentives. Some governments offer job creation or employee training/retraining tax credits, and/or provide employment screening and customized training. The advantage of focusing on employee-based incentives is that even if a business fails or relocates to another state, the government has invested in building a skilled workforce and knowledge base.

Governor Sandoval's proposal to launch the WINN Fund is an example of a non-tax, employee-based incentive. Ideally, the WINN could train workers in a wide range of advanced manufacturing specialties.

Improved Accountability, Monitoring and Evaluation

State and local political leaders understand that development incentives are a critical component of an effective economic development strategy. But, given the mixed economic impact, state and local public leaders are thinking more strategically about how to deploy their incentive packages.³¹ As such, policymakers are introducing measures that improve accountability and evaluations of deals (with the goal of measuring cost and impact). Among the policies to improve accountability are:

- Provide and publish information on incentive packages and conduct assessments;
- Use rigorous and standardized approaches for calculating the costs of each job created or retained;
- Establish a strategic and ongoing schedule to review ("sunset review") and assess the appropriateness, effectiveness, and efficiency of tax and non-tax incentives;
- Establish benchmark "return on investment" targets; and
- Establish an independent body or commission that evaluates progress on established benchmarks for each incentive package.

Four states—Arizona, Iowa, Oregon, and Washington—have integrated evaluation of their major tax incentives into the policy process, ensuring that those investments are regularly reviewed. In Oregon, new legislation has tax credits automatically expiring after six years unless legislators vote to extend them. In

²⁹ GOED. Tesla Report, Q3 2015.

http://www.diversifynevada.com/uploads/reports/Tesla_Gigafactory_Q3_2015_Report.pdf

³⁰ GOED. Tesla Compliance Audit Report October 2015.

[http://www.diversifynevada.com/uploads/reports/Tesla_Gigafactory_Compliance_Audit_Report_\(FY15\).pdf](http://www.diversifynevada.com/uploads/reports/Tesla_Gigafactory_Compliance_Audit_Report_(FY15).pdf)

³¹ Kenan Fikri. "States Smarten Up on Economic Development Incentives." *New Republic*. May 7, 2012.

Washington, policymakers are reviewing every tax incentive the state offers. There, nonpartisan analysts work with a citizen commission and legislative auditor to annually review and evaluate the state's incentives.³² In 2010, Missouri created a Tax Credit Review Commission, comprised of business, community, and legislative leaders, whose sole charge is to critically analyze the return on investment of tax incentives.

What issues should Nevada's legislators consider?

Below we outline a number of questions that Nevada's legislators should consider as they head into the special session to discuss the Faraday Future incentive package.

A. Improved Accountability

- Is our current system of accountability and evaluation sufficiently rigorous?
- Can Nevada create a standard template for monitoring and evaluating performance and impact that can be used across all incentive projects?

The Tesla Motors development incentive package contained explicit requirements of public accountability never before included in previous tax incentive packages. However, while there have been positive regional indicators, there is a public concern that "the promised transparency of the tax incentive has lagged."³³

Per legislation, Tesla Motors is required to submit quarterly reports to GOED. Quarterly reports total 1-2 pages in length and information is not organized systematically, making it difficult to track employment, investment, and impact over the course of the project. Additionally, legislation required Tesla Motors to submit an audit of its record on job creation and investment by October 1, 2015. With no requirement for a public hearing, Tesla Motors received an extension and the audit was submitted on December 15, 2015.³⁴ Additionally, Storey County has yet to conduct a complete the required analysis of the impact of the development project on public services in the county. In short, while Nevada has tightened accountability by requiring regular reporting and conducting audits and assessments, officials may want to consider ways to standardize reporting across all tax incentive projects.

B. Demands on Existing Infrastructure and the Cost of New Infrastructure

- Has Nevada identified sufficient revenue streams to respond to increased demand for infrastructure (e.g., roads, schools) and services?
- How will the State prioritize highway projects given the infrastructure requirements of Faraday?

The Faraday Future advanced manufacturing facility is projected to have tremendous fiscal and economic benefits for southern Nevada, particularly North Las Vegas, which was battered by the Great Recession and whose economic recovery continues to be anemic. But there are also costs. While Faraday Future's presence will spur economic growth and increase tax revenues, Nevada's lawmakers must consider whether county and local governments have sufficient resources to cover the increased need for public services.

The biggest components of the deal are sales, property, and payroll tax abatements. The combined tax abatement package for Faraday is estimated at \$175 million over 10-15 years. Under the existing tax

³² Pew Center on the States. Evidence Counts: Evaluating State Tax Incentives for Jobs and Growth." April 2012. <http://www.pewstates.org/research/reports/evidence-counts-85899378806>. ITEP. "Five Steps Toward a Better Tax Expenditure Debate." October 1, 2012. http://itep.org/itep_reports/2012/10/five-steps-toward-a-better-tax-expenditure-debate.php

³³ Anjeanette Damon. "Tesla gigafactory one year later: Economic boost but lagging transparency," Reno Gazette Journal, December 10, 2015. <http://www.rgj.com/story/news/2015/12/06/tesla-gigafactory-one-year-later-economic-boost-but-lagging-transparency/76638958/>

³⁴ GOED. Tesla Compliance Audit Report October 2015. [http://www.diversifynevada.com/uploads/reports/Tesla_Gigafactory_Compliance_Audit_Report_\(FY15\).pdf](http://www.diversifynevada.com/uploads/reports/Tesla_Gigafactory_Compliance_Audit_Report_(FY15).pdf)

abatement program, businesses are eligible for a 50 percent break on property and modified business taxes and a partial abatement on sales and use taxes for equipment purchases for a limited time.³⁵ The proposed Faraday deal abates 100 percent of sales and use tax and 75 percent of payroll and property taxes for an extended period of time (10 to 15 years, depending on the tax).³⁶ While abatements do not have a direct impact to the state's bottom line (they are simply foregone revenue), they should be factored into the impact of the tax incentive package. Here we sketch the potential impact of these development incentives.

Sales and Use Tax Abatements

School districts and local governments rely on sales and property tax revenues for a substantial part of their budgets. Tables 3a and 3b shows the breakdown of revenue for the county government and school district in Clark County.

Table 3a. Sources of Revenue in Clark County³⁷

2014-15 General Fund Clark County		
Revenue	Amount	% of Total
Property Taxes	\$ 270,912,167	22%
Sales Taxes (estimated)	\$ 289,013,670	24%
Consolidated Taxes less Sales Tax	\$ 43,052,842	4%
Licenses and Permits	\$ 226,400,000	19%
Intergovernmental Revenue	\$ 4,537,831	0%
Charges for Services	\$ 70,626,623	6%
Fines	\$ 21,500,000	2%
Miscellaneous	\$ 3,000,000	0%
Other Financing Sources	\$ 293,620,093	24%
Total Revenue	\$ 1,222,663,226	100%

Note: Sales tax amount estimated based on the percentage of sales tax in Clark County's consolidated tax revenue.

Table 3b. Sources of School District Revenue, Clark County³⁸

2015-16 Clark County School District General Fund		
Revenue	Amount	% of Total
Property Taxes	\$ 425,000,000	20%
Sales and Use Taxes	\$ 943,920,000	45%
Governmental Services Tax	\$ 59,150,000	3%
Other Local Revenue	\$ 32,135,000	2%
State Revenue	\$ 599,885,000	29%
Federal Revenue	\$ 300,000	0%
Other Sources	\$ 34,550,000	2%
Total Revenue	\$ 2,094,940,000	100%

³⁵ Nevada GOED. <http://www.diversifynevada.com/programs-resources/incentives>

³⁶ Anjeanette Damon. "Nevada taxpayers, here's how the Tesla deal affects you." *Reno Gazette Journal*. September 9, 2014. <http://www.rgj.com/story/news/2014/09/08/nevada-taxpayers-tesla-deal-affects/15303711/>

³⁷ Sources: Clark County 2015-16 Budget: See General Fund page 20 and 21
<http://www.clarkcountynv.gov/finance/budget/Documents/Final%20Budget%20FY%2015-16.pdf>

Sales Tax: Estimated using Local Government Finance Projections Part D:
http://tax.nv.gov/LocalGovt/PolicyPub/ArchiveFiles/LGF_Final_Revenue_Projections_2015_2016/

³⁸ Source: [http://www.boarddocs.com/nv/ccsd/v/Board.nsf/files/A4UTZ278390F/\\$file/12.10.15%20Ref.%207.04.pdf](http://www.boarddocs.com/nv/ccsd/v/Board.nsf/files/A4UTZ278390F/$file/12.10.15%20Ref.%207.04.pdf)

The abatements on sales and use tax revenue (resulting in foregone revenue) could have a statewide and regional impact. Faraday Future will likely make purchases throughout the state and could have significant purchases outside the state. As discussed in more detail below, some portions of the sales and use tax are distributed to government agencies in the county where the tax was collected, while other parts of the tax are distributed statewide.

The largest category of sales and use tax is the Local School Support Tax (LSST), which is distributed to school districts where the funds are collected (see Table 4). Use taxes collected for purchases outside the state are deposited in the Distributive School Account and are allocated to school districts statewide. School districts rely heavily on the LSST, which represents 45 percent of Clark County School District revenue.

Table 4: Statewide Sales and Use Tax³⁹

ITEM	Local School Support Tax (LSST)	State Sales Tax	Supplemental City-County Relief Tax (SCCRT)	Basic City-County Relief Tax (BCCRT)	TOTAL
Tax Rate	2.60%	2.00%	1.75%	0.50%	6.85%
Percent (%) of Sales Tax	38%	29%	26%	7%	100%

Property Tax Abatements

While sales have a statewide impact, property taxes are largely treated as local revenue. In Clark County, where the proposed Faraday Future plant would be located, 95 percent of property taxes levied stay within the geographic area and are distributed to local governments. Five percent of the revenue goes to the state Consolidated Bond Interest and Redemption Fund. Table 5a presents the tax rates in Clark County in 2014-15 for each government entity that receives property tax revenue and the percentage of total property tax revenue that each entity receives. Table 5b presents the property tax rates in North Las Vegas. The maximum combined property tax rate is \$3.66 per \$100 in assessed value, which includes a statutory maximum of \$3.64 per \$100 in assessed value, plus \$0.02 per \$100 in assessed value that is outside the statutory cap and is used for the Consolidated Bond Interest and Redemption Fund.

Table 5a: Property Tax Rates in Clark County⁴⁰

ITEM	Schools	County	Maximum Combined Special District Rate	State	Total
Property Tax tax rate	1.3034	0.6541	1.2755	0.17	3.403
Percent (%) of Property Tax	38%	19%	37%	5%	100%

Table 5b: Property Tax Rates in North Las Vegas⁴¹

ITEM	Schools	County	City	Combined Special District Rate	State	Total
Property Tax tax rate	1.3034	0.6541	1.1637	0.0632	0.17	3.3544
Percent (%) of Property Tax	39%	19%	35%	2%	5%	100%

³⁹ Source: Legislative Counsel Bureau: 2015 Revenue Reference Manual

⁴⁰ Source: http://tax.nv.gov/uploadedFiles/taxnvgov/Content/Home/Features/2015-2016_Redbook.pdf

⁴¹ Source: Local Government Finance: Property Tax Rates for Nevada Local Governments FY 2015-2016

In 2014-15, property taxes accounted for 22 percent of Clark County's general fund revenue (see Table 3a), and 20 percent of Clark County School District's revenue (see Table 3b). If the Nevada Legislature approves the proposed property tax abatements, Clark County might have to leverage other sources of revenue to provide additional services resulting from Faraday Future's operations in Clark County.

The Clark County School District would be more significantly impacted by property tax abatements than sales tax abatements. Schools are funded by several sources, including the General Fund, the 2.6 percent LSST, and one-third of the \$0.75 ad valorem property tax under a funding formula known as the Nevada Plan. These revenues are part of the basic support guarantee under the Nevada Plan. However, two-thirds of the \$0.75 property tax revenues are considered outside of the Nevada Plan and are not part of the basic support guarantee. If the amount of LSST and property tax revenue are insufficient to cover any increased demands on the Clark County School District as a result of Faraday, the General Fund would need to make up the difference.

Additionally, since property taxes are the principal source of funds for school facility needs, these abatements could have a substantial impact on the ability of the Clark County School District to respond to student population growth that might result from Faraday Future.

C. Job Creation

- How can Nevada ensure that local Nevadans are hired?
- How can Nevada strengthen workforce development programs to ensure that Nevadans are well positioned to fill jobs at Faraday Future (or similar advanced manufacturing companies)?

Many state and local governments are beginning to design 'performance-based' contracts, which means that the recipient company (e.g. Faraday Future) would not receive some portion of the benefits until targets – such as employment and capital investment – had been met. As recently reported, to be eligible for the tax incentives, Faraday Future must invest at least \$1.0 billion in Nevada.⁴² At full operation, Faraday Future is expected to employ 4,500 skilled workers in its advanced manufacturing facility.

Although Faraday has signaled its commitment to employ locally, the Nevada Legislature should require that specific hiring targets are included in the incentive contract. As with Tesla Motors, the Nevada Legislature could require that at least 50 percent of its workers are Nevada residents.

Even with specific requirements in place, there is some concern that Nevada currently does not have an adequate supply of skilled workers to fill permanent positions at the advanced manufacturing plant. These concerns are not unfounded. For instance, National Security Technologies, a science and technology firm engaged in security and defense applications, has to venture outside the state to hire many of its workers.⁴³

Recognizing Nevada's workforce challenges, members of the Nevada System of Higher Education (NSHE), the Nevada Department of Education, Training and Rehabilitation (DETR), and the Governor's Office of Economic Development (GOED) have traveled regularly to speak with Tesla Motors officials about the skill requirements of its prospective workers at the Nevada facility. Through the course of conversations, Nevada's leaders have recognized that the State could benefit from having a more formal structure or system in place to identify, train, and assess Nevadans who might work at Faraday.

Consequently, as part of the Faraday Future incentive package, Governor Brian Sandoval, with the support of GOED, has proposed a workforce grant program, Workforce Innovations for the New Agenda (WINN)

⁴² Anjeanette Damon. "Nevada taxpayers, here's how the Tesla deal affects you." *Reno Gazette Journal*. September 9, 2014. <http://www.rgj.com/story/news/2014/09/08/nevada-taxpayers-tesla-deal-affects/15303711/>

⁴³ Kristy Totten. "Nevada National Security Site Management company looks to grow its own scientists." *Las Vegas Review Journal*. March 26, 2014. <http://www.reviewjournal.com/news/nevada-national-security-site-management-company-looks-grow-its-own-scientists>

Fund. The purpose of WINN is to develop a program that would provide training for up to 4,000 automobile assembly workers at the facility. Ideally, WINN might involve partnerships between the College of Southern Nevada, the Clark County School District, DETR, and the University of Nevada, Las Vegas.

WINN echoes the recommendation offered in the Guinn Center 2014 report, *Development Incentives*, which suggested that a formal structure or program should be established to identify and build a workforce pipeline. Additionally, the recommendation of establishing the WINN mirrors the successful partnership of the Truckee Meadows Community College (TMCC) Advanced Manufacturing Career Pathway, which involves a partnership between TMCC, the Washoe County School District, DETR, and two industry partners. In this model, juniors in a high school Career and Technical Education (CTE) program, who continue through community college, will earn stackable certifications and credits, which students can transfer towards an advanced degree. Additionally, the WINN models some of the core elements of the Workforce Development Rapid Response Investment Program (SB 496), which was considered (but failed to pass) during the 2015 Legislative Session.⁴⁴

D. Development Incentives and Market Signals

- What signals does the Faraday Future \$335 million incentive package send to other businesses seeking to operate in Nevada?

One of the frequent criticisms of development incentives is that they only help a few businesses and often put governments in the position of choosing winners and losers, as opposed to letting market forces determine efficient investment. Moreover, existing businesses end up subsidizing these new businesses, which are often times their competitors. Scott Drenkard, an economist with the Tax Foundation, testified last year in front of the Indiana Commission on State Tax and Financing Policy stating, "Even though credits lower the tax burden of a particular tax filer, in most cases we see them as poor tax policy. Some businesses might get the benefit of a preference, but other businesses that aren't engaging in whatever activity is deemed "favorable" are stuck paying the full sticker rate of the tax."⁴⁵

As reported, the Faraday Future incentive package will be "funded by an \$8 million reduction each year in the amount Nevada places in its Catalyst Fund."⁴⁶ Approved in the 2011 Legislative Session (NRS 231.1573), the Catalyst Fund provides money to select businesses with the goal of incentivizing their expansion or relocation and helping them create high-quality, primary jobs in Nevada. As of October 2015, the Catalyst Fund has provided support to 17 businesses and created 4,019 jobs. By redirecting the lion's share of Catalyst Funds to Faraday Future, this may limit the ability of the State to support other small businesses.

To address concerns of those who may 'lose' under Nevada's tax incentives, Nevada's political leaders should develop a strategic economic development framework that can articulate the benefits of the various development incentives. Legislators will need to set criteria for offering these subsidies and then restrict the incentive packages to projects that meet these criteria, thereby improving the likelihood that the benefits of the project will exceed the costs.

Recommendations for Improving Nevada's Return on Investment

The Guinn Center for Policy Priorities offers the following recommendations for Nevada's Legislators as they consider extending a \$335 million development incentive package to Faraday Future.

⁴⁴ Nevada State Legislature. 2015 Legislative Session.

<https://www.leg.state.nv.us/Session/78th2015/Bills/SB/SB496.pdf>

⁴⁵ Winners and Losers: The Impact of Government Incentives. MacIver Institute: Wisconsin. January 16, 2014.

<http://www.maciverinstitute.com/2014/01/winners-and-losers-the-impact-of-government-incentives/>

⁴⁶ Jamie Simon, "Faraday Future to build a \$1bn production plant in Nevada," The Waltonian, December 15, 2015.

<http://waltonian.com/2015/12/faraday-future-to-build-a-1bn-production-plant-in-nevada/>

A. Short term

- Support the proposed recapture (clawback) provision in the Faraday incentive package
As outlined by Governor Sandoval and GOED, the current proposal includes a strong recapture provision. Faraday Future will pay property and sales taxes into a fund (escrow account) that will be rebated *only after* the \$1 billion investment target has been achieved. Legislators should support this provision.
- Include performance-based measures in the incentive contract with Faraday
As they did with Tesla Motors, legislators should include specific employee (hiring) targets in the Faraday Future agreement. Tesla Motors is required to hire at least 50 percent of its workforce locally. Although Faraday has expressed a commitment to hire local Nevadans, legislators should require that specific hiring targets be included in the incentive contract. Legislators should also consider extending credits (e.g. energy rates) to Faraday only after employee and capital investment targets have been met.
- Create a workforce development training program
The Nevada Legislature should approve the proposed Workforce Innovations for the New Nevada (WINN). This project was informed by the challenges faced by Nevada's leaders in creating the appropriate training programs, identifying and assessing workers, and building the pipeline to supply the skilled workforce needed by Tesla Motors. Given the lack of supply of a skilled workforce and the growing demand around the state for critical numbers of highly-skilled workers, the State needs to be able to launch and scale up a formal, concerted and coordinated programmatic training effort. WINN should include formal partnerships between the College of Southern Nevada, the Clark County School District, DETR, and UNLV. Over time, WINN could train workers in a number of advanced manufacturing fields. Again, this model has demonstrated success with the TMCC Advanced Manufacturing Career Pathway program. WINN would allow the State to jumpstart a similar program in southern Nevada.
- Identify the specific impact of Faraday on current and proposed highway projects
During the special session, Governor Sandoval will ask the Legislature to consider \$120 million in infrastructure investments. Estimates indicate that development of the highway near the Apex site will cost \$50 million; funds will be taken from the State Highway Fund to pay for this project. GOED officials have suggested that this "roadway improvement project would go to the front of the line, potentially pushing back other projects in the Nevada Department of Transportation's queue."⁴⁷

As of April 2015, the Nevada Department of Transportation (NDOT) was projecting that that Highway Fund would "end the 2015-2017 biennium with a remaining unrestricted balance of \$124.4 million, which is a decrease of approximately \$92.4 million from the unrestricted Highway Fund balance of \$216.8 million as of June 30, 2014."⁴⁸ The Nevada Department of Transportation (NDOT) is currently working on four road projects that are of critical importance to southern Nevada (Project NEON, the Boulder City Bypass) and northern Nevada (USA Parkway and the Carson City Bypass). Legislators should ask NDOT and GOED to provide the exact list of which current or scheduled highway projects would be affected (or postponed) by the funding requirements of the Faraday Future highway project.

- Establish a government commission to monitor the contract and performance targets
This commission (comprised of citizens, nonprofits, legislative auditors, and tax policy experts) would be charged with monitoring the progress of Faraday Future, tracking the incentives and abatements schedule, ensuring that performance targets are met, evaluating Faraday Future's local and state economic and fiscal impacts, assessing the cost-effectiveness of the incentive program, and measuring

⁴⁷ Ritter and Rindels. "Nevada Governor Outlines \$335M Deal to Draw \$1B Carmaker," *ABCnews.com*, December 10, 2015. <http://abcnews.go.com/Technology/wireStory/nevada-governor-unveils-335-million-deal-draw-carmaker-35698250>

⁴⁸ Nevada Legislature. Joint Subcommittee on Public Safety, Natural Resources, and Transportation, Page 8. <https://www.leg.state.nv.us/App/NELIS/REL/78th2015/ExhibitDocument/OpenExhibitDocument?exhibitId=15595&fileDownloadName=NDOT%20closing%20report%20packet.pdf>

actual versus expected performance. The committee would be required to report to the Governor and Nevada Legislature once a year. Additionally, this commission could monitor all incentive deals.

➤ Encourage GOED to conduct a school facilities impact study

School facilities planning should be an integral part of the development incentive approval process. Under current law, GOED has the authority to approve abatements of sales, business, and property taxes for new and expanding businesses for 10 to 20 years (NRS Chapter 360). Since property taxes are the principal source of funds for school facility needs, these abatements can have a substantial impact on the ability of school districts to respond to student population growth that can result from new and expanding businesses. For example, the Tesla Motors project approved in September 2014 will bring an estimated 6,500 employees to Storey County, which could have a significant impact on school enrollment in the surrounding school districts. GOED should consider a formal assessment of school capital needs prior to the approval of development incentives.

Working with the impacted school districts, GOED should conduct a school facilities impact study and develop a funding plan that either uses an existing funding mechanism or proposes a new funding mechanism to address future facility needs.

➤ Strengthen accountability and disclosure

State and local policymakers must adopt policies that strengthen accountability and disclosure of all development incentive packages. GOED should also move to standardize reporting requirements (e.g., provide templates) across incentive packages that allow for comparisons and effective monitoring over the course of the project. Reporting requirements that are standardized across projects and take into account the full range of costs and benefits will enable policy analysts to more accurately measure the cost-effectiveness of each development incentive.

B. Looking ahead

Beyond the proposed \$335 million Faraday Future deal, the Nevada Legislature should consider broader reforms that could improve the cost-effectiveness of development incentives and the state's overall economic development strategy. Below are general recommendations for consideration during the 2017 Legislative session.

➤ Establish a formal, strategic and ongoing process to review all of Nevada's tax incentives

Many states have laws and policies in place that require a formal review of the state's entire portfolio of development incentives. This policy measure can help formalize a process of determining which incentives are meeting the state's strategic economic development goals.

➤ Establish criteria for development incentives

Limiting development incentives (subsidies) to projects that meet certain standards may improve the cost-effectiveness of the incentives. Establishing criteria (e.g. job creation, rural development, under-served areas, disadvantaged populations) also helps mute the criticism that governments are choosing winners and losers.

➤ Consider legislation that would sunset all incentives after a period of time

A number of states (e.g. Arizona and Oregon) retire (or 'sunset') certain development incentives after a specified period of time, unless legislators act to extend them.⁴⁹

➤ Explore the feasibility of placing limits on the number or total dollar value of incentives

The widespread use and popularity of development incentives owes, in part, to the fact that they are unlike direct expenditures, which are subject to annual appropriations. Also, abatements equate to foregone revenues, as opposed to direct grants. Placing limits on the number or total dollar value of incentives could constrain policymakers to more rigorously assess the cost-effectiveness of the development incentives.

⁴⁹ Pew Center on the States. Evidence Counts: Evaluating State Tax Incentives for Jobs and Growth." April 2012.

<http://www.pewstates.org/research/reports/evidence-counts-85899378806>

Conclusion

While the Faraday Future incentive package involves real costs to the State, the motive of bringing an advanced manufacturing facility to Nevada supports the State's goal to diversify its economy. Jointly, Tesla Motors and Faraday, once fully operational, will provide Nevada with a critical mass of advanced manufacturing knowledge and capabilities. Building on the lessons of Tesla Motors, the proposed incentive package contains even stronger recapture provisions. The proposal to establish a long-standing partnership to strengthen the workforce pipeline is a much-needed initiative, which over time could support a number of industry-education college partnerships. Additionally, the Faraday Future project provides an opportunity to jumpstart the economy of North Las Vegas, thereby minimizing the need for greater State financial assistance.

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The Kenny C. Guinn Center for Policy Priorities is a 501(c)(3) nonprofit, independent research center focused on providing fact-based, relevant, and well-reasoned analysis of critical policy issues facing Nevada and the Intermountain West. The Guinn Center engages policy-makers, experts, and the public with innovative, data-driven research and analysis to advance policy solutions, inform the public debate, and expand public engagement.

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