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| To: | Honorable Members of the Joint Legislative Committee on the Budget |
| From: | Greg Albrecht, Chief Economist, Legislative Fiscal Office GVA<br>John D. Carpenter, Legislative Fiscal Officer JDC |
| Date: | September 18, 2015 |
| Subject: | Act 704 of 2014 Evaluation, Monster Moto LLC |

Act 704 of the 2014 Regular Session requires a standard set of economic and financial information be submitted to the Joint Legislative Committee on the Budget (JLCB) for projects that involve a state commitment in excess of $10 million over the term of a project. The Act requires the Legislative Fiscal Office to provide an evaluation of the submitted project's economic and fiscal impact assessment.

**Act 704 of 2014 Provisions**

a) State Commitment: The estimated benefits provided to Monster Moto over a ten-year projection horizon (2016 – 2025) are $10.7 million; composed of $10.3 million of Competitive Project Payroll Incentive Program payments, and $420,000 of FastStart program costs.

b) Analytical Model and Inputs: Estimates of the economic impact in Louisiana of the operations of Monster Moto were provided by Professor Dek Terrell (Executive Director) and Stephen Barnes (Director), of the LSU Division of Economic Development, in their report dated June 18, 2015. They utilized a state level IMPLAN input-output model of Louisiana. This is a commercially available and widely used economic impact analysis model. According to the LSU impact analysis, the main source of input data for the resulting economic impacts is the draft Cooperative Endeavor Agreement for the Competitive Projects Payroll Incentive Program, in which the firm declares its hiring and investment intentions to Louisiana state officials. Direct operational employment and salaries were provided. Direct employment ramps up over the ten-year period from 32 and $1.5 million of salaries in 2016 to 287 and $16 million in 2025. Monetary values in 2025 are adjusted to 2015 dollar values by discounting future nominal dollar values by a 2.3% factor reflecting the annual average yield curve of 10-year U.S. Treasury bond yields at the time of the impact analysis (April 23, 2015).

c) Economic Impacts:

   i) Value Added is estimated for each of the ten years throughout the projection horizon, and for 8 major industry sectors as of the final year 2025. Value added is estimated at $10.1 million in 2016, growing to $58 million in 2025 nominal dollars. Over the ten-year period, cumulative nominal value added is estimated at $391.6 million, and $344.8 million in 2015 constant dollars. Value added is the difference between an industry's or establishment's total output and the costs of its intermediate inputs, the sum of which is gross domestic product, the broad headline measure of economic activity, although it includes components that do not necessarily reflect economic impacts on the households of the economy.

   ii) Household Earnings are estimated for each of the ten years throughout the projection horizon, and for 8 major industry sectors as of the final year 2025. Household earnings are estimated at $6.2 million in 2016, growing to $37.6 million in 2025 nominal dollars. Over the ten-year period, cumulative nominal household earnings are estimated at $250.6 million, and $220.5 million in 2015 constant dollars. For the final projection year of 2025, nearly 43% of total earnings are the direct salaries of Monster Moto, with the balance attributable to it's purchases, the purchases of it's suppliers, and the induced consumption effects of the purchases of employees and general consumers in the economy. Household earnings are composed of all forms of employment income and benefits, including proprietor income. This concept is the most important reflection of economic impact on the population of the economy.

iii) Employment is estimated for each of the ten years throughout the projection horizon, and for 8 major industry sectors as of the final year 2025. However, other than the direct employment ramp-up reported by the firm itself, the analysis does not provide a table of explicit estimates of each year's total employment, except for the final projection year of 2025. A column graph of each year's employment results is provided, though, so rough estimates of total employment can be visually discerned. In 2016, total employment might be some 120, of which 32 are directly employed by the firm. By 2025, total employment levels are estimated at 779, of which 287 are directly employed by the firm. Employment is defined as the annual average of monthly jobs. A job lasting 12 months is equal to 2 jobs lasting 6 months each or 3 jobs lasting 4 months each etc. A job can be either full-time or part-time, and no distinction is made. This concept of employment is consistent with the standard concepts utilized by the U.S. Department of Labor.

d) Impacts By Industry: Value added, household earnings, and employment are estimated for 8 industry sectors for the last year of the analysis, 2025. For all three metrics, the large bulk of economic impact (93% - 95%) occurs in 3 sectors; manufacturing, services, and trade. While the analysis does not explain this distribution of impact, large portions of impact obviously occur in the manufacturing sector within which the firm and many of its suppliers operates. Induced consumption effects will typically be strong in the service and trade sectors. Impacts step down significantly across the remaining sectors and, at least with respect to value added and household earnings, are estimated to be slightly negative in the agriculture sector.

e) Fiscal Costs: Competitive Project Payroll Incentive Program (R.S. 51:3121) benefits provided to the firm over the ten-year projection period are reported by the Department of Economic Development to total $10.3 million. Benefits are projected to start at $200,000 in 2016 and increase to $1.8 million in 2025. These benefits are unappropriated direct payments to the firm from current tax collections remitted by all taxpayers, and are 11% of the firm's eligible payroll. The program provides for a maximum payment of 15% of eligible payroll. The Department also reports LED FastStart program costs for various videos, business analysis, staffing plans, and course development for the firm of $420,000 during 2016 – 2018. These expenditures are appropriated within the LED budget. LED also indicates that the firm has filed an advance notification for participation in the Industrial Tax Exemption Program, which abates local property taxes. While LED did not indicate the firm's participation in any other state incentive programs, participants in the Competitive Projects Payroll Incentive Program are also eligible to receive the state sales tax rebates or the state capital expense rebates of the Enterprise Zone Program (R.S. 51:1787) and local sales tax rebates, if the participant meets the hiring requirements and all other limitations, procedures, and requirements of that program. To the extent the firm participates in additional state incentive programs, state fiscal costs would be greater than those included in the analysis submitted for this review.

f) Incentive Significance: LED indicates that the firm ultimately was choosing locations between Texas and Louisiana, with the Texas site near its original headquarters but similar to the Louisiana site. LED refers to the 2014 edition of Competitive Alternatives, a KPMG report which analyzes costs for different types of business operations across multiple geographic locations based on KPMG's proprietary cost model, which indicated that the two locations were essentially the same in regards to transportation and logistics, since both were located along the I-20 corridor, but that Louisiana had a slight advantage in overall business costs. According to LED, the availability of the Competitive Projects Payroll Incentive Program was a key factor in influencing the firm's final decision to locate in Louisiana.

g) Fiscal Cost/Benefits: The impact analysis provides an estimate of total state tax receipts attributable to the project in each year of the projection period. Tax receipts are estimated to be $400,000 in 2016, ramping up to $2.7 million in 2025. Cumulative nominal dollar receipts over the entire ten-year period are $17.8 million, and $15.7 million in 2015 constant dollars. No explanation of how these estimates are generated is provided. However, they are within a range of 6.5% - 7.0% of the household earnings estimates, and appear reasonable in light of actual state experience with regard to total state household earnings-related tax receipts and total labor & proprietor income in the state during the last few years.

These state tax receipt estimates are compared to the fiscal cost estimates of the payroll subsidy payments and FastStart costs to generate total net state fiscal revenue in excess of state fiscal costs of $7.1 million over the ten-year period. Positive annual excess revenue occurs in all years ranging from $60,000 in 2016, then stepping up to $460,000 in 2018, and stepping up again to the $800,000 to $1 million range in years 2019 to 2025.

General Evaluation

The absolute levels of economic impacts estimated from input/output models should be taken with considerable caution. These are based on somewhat dated relationships between national industries, although the IMPLAN model does make effort to incorporate more current national and state level information of various economic variables. In addition, input/output analysis is static and linear. New firms are assumed to purchase inputs from in-state industries to the same degree that average purchases in the new firm's industry are exhibited. Economic impacts in the state tend to be overstated for this reason and due to inadequate accounting for substitution effects in consumption patterns.

The economic results of the input/output analysis are essentially mechanical, and are driven by the inputs of direct hiring and wages paid, as reported by the project itself. Those inputs should be examined in any analysis based on them. The direct hiring and wage information provided for the operational component of the project analysis is much more stable on an annual average wage basis, starting at $83,366 in 2014 and rising to nearly $117,000 by 2025; a 1.945% per year compound annual average nominal wage growth. For the last three years or so, monthly consumer price index inflation has averaged an annual pace of a little below 2%. Should this pace of inflation be sustained into the future, essentially no real buying power wage gains are anticipated in current project input data.

The analysis does not account for the state's balanced budget requirement. This omission is a common flaw in impact analysis, and means that the $10.7 million total fiscal cost of the incentives, that have to be paid for elsewhere in the state budget, are not considered in the analysis. Use of these public resources to support this project results in lower government expenditures elsewhere in the economy. This is a negative spending change that has its own multiplier effects that work to dampen the positive effect of the presence of the project in the economy. Thus, total economic and fiscal benefits are overstated and, consequently, the net excess of state revenue over state costs are overstated, as well.

Finally, it is notable that the estimated net fiscal benefits are relatively small; $60,000 in the first year and no more than $1 million in the eight year. Given the uncertain nature of the absolute levels of economic impacts that result from input/output analysis, the likely upward bias of that analytical tool, the omission of the state's balanced budge requirement in the analysis, and the possibility that the firm could participate in additional incentive programs it is possible that net positive fiscal benefits will not occur, and it is even possible that net negative fiscal costs result.

**Correction**

The discussion in section (e) above concerning the possibility of the firm participating in other incentive programs is in error. The cooperative endeavor agreement prohibits the firm from receiving the Facility Sales and Use Tax Rebate or the Facility Expense Rebate under the Competitive Projects Payroll Incentive (CPPIP), as well as any other incentive administered by LED directly for any new payroll of associated new jobs for which the company has received a rebate under the CPPIP, and shall not be eligible for benefits under the Enterprise Zone Program.