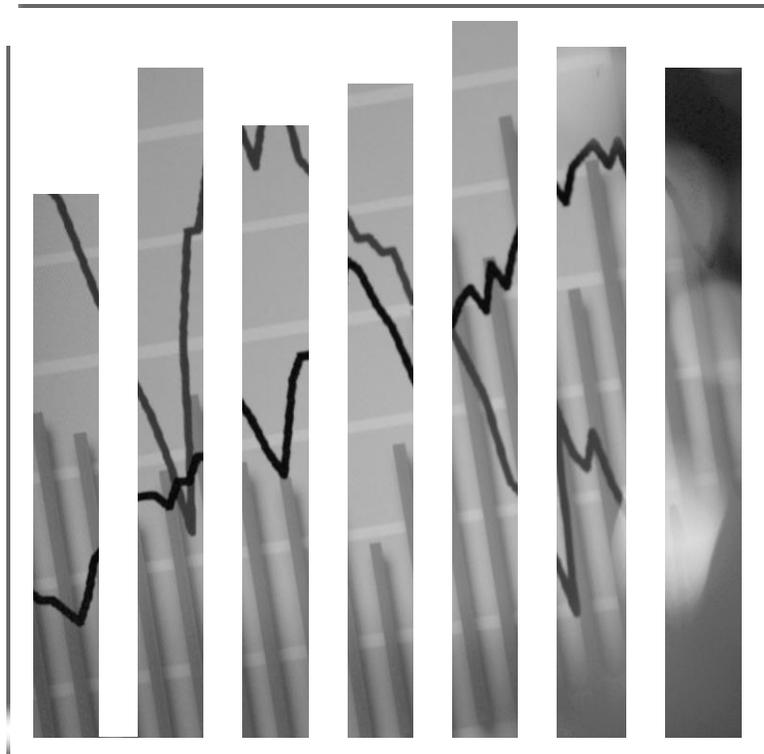


White Paper

Nevada Assembly Bill 239:

Evaluating Economic and Fiscal Impacts for the Purpose of Approving Incentives for Energy-Related Projects in the State of Nevada



Prepared for: Nevada Association of Counties

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INTRODUCTION

The practice of granting tax incentives or abatements by state and local government entities to the private sector has long been used to encourage development that is considered beneficial to the common good. The encouragement of specific types of development occurs when governing bodies desire to promote an activity that may not be the most profitable option for a developer, as is the case with many renewable energy projects. Sound fiscal policy for government entities that grant tax incentives or abatements should include a consideration of whether the benefits of a proposed project outweigh the costs to the public. In the case of renewable energy in Nevada, a recent legislative change now allows local county officials to determine whether the benefits of a project (net of abatements) outweigh the costs (or loss of revenue) incurred by the county, and to base a recommendation for approval or denial on such grounds.

Specifically, Nevada Assembly Bill 239 (AB 239) was introduced during the 2013 Legislative Session and approved by Governor Brian Sandoval on June 11, 2013. In addition to authorizing the Director of the Office of Energy (the "Director") to charge and collect fees from applicants for certain energy-related tax incentives, AB 239 revised provisions relating to the eligibility for and approval of applicants for certain energy-related tax incentives, among other changes related to energy policy in the state of Nevada. Nevada Revised Statutes (NRS) 701A.360, which was already in effect at the time AB 239 was enacted, allows for the partial abatement of local sales and use taxes as well as property taxes imposed pursuant to NRS 361 for renewable energy facilities meeting certain criteria.

Explicitly pertaining to Nevada county-level governments, Section 4 of AB 239 revised the requirements surrounding the approval process for economic development incentives provided under NRS 701A.360 by the board of county commissioners of the county in which a proposed energy project intends to locate.

When considering an application for tax incentives for approval and recommendation to the Director, the board of county commissioners may deny such a request if either of the following two conditions is found to be true based on relevant information:

- 1) The projected cost of the services that the local government is required to provide to the facility will exceed the amount of tax revenue that the local government is projected to receive as a result of the abatement; or
- 2) The projected financial benefits that will result to the county from the employment by the facility of the residents of the state of Nevada and from capital investments by the facility in the county will not exceed the projected loss of tax revenue that will result from the abatement.

If cost of services > tax revenue (net of abatements), then possible grounds for denial of request exist

If financial benefits < loss of tax revenue, then possible grounds for denial of request exist

This *white paper* offers a well-defined set of procedures such that an affected county may undertake the required evaluation of the two conditions described above (the "concluding analyses") and make an appropriate recommendation to the Director. These procedures are outlined in the sections that follow.

REQUIRED INPUTS AND FRAMEWORK FOR REPORTING AND SUBMITTAL

Prior to commencing the evaluation procedures outlined in the following sections, a financial model in the form of an MS Excel-based template (the “model”) will be developed that allows for input of all required information as described herein. Upon input of the necessary data, the model will be designed such that it provides all necessary calculations and prepares the preliminary, concluding analyses automatically. Required inputs to the model would include the following:

Provided by applicant:

- Facility location (i.e., Nevada county)
- Description of facility (e.g., type of renewable energy source used in energy generation)
- Underlying land cost
- Construction data for the new project
 - Total capital investment amount
 - Split between materials and labor as percent of total investment (e.g., 80/20, or 80 percent materials and 20 percent labor)
 - Construction employment (in person-years, that is, one person employed for one year)
 - Percentage of construction employees that are residents of the Nevada county in which the facility intends to locate
 - Prevailing average wage data
 - Percentage of non-labor cost of investment to be retained in-county
 - Construction period (years)
- Operating data for the new project
 - Number of employees expected to be required to operate facility
 - Percentage of operating employees that will be residents of the Nevada county in which the facility intends to locate

- Budgeted salaries/wages for ongoing operations
- Ongoing taxable maintenance and equipment expenses

- Capital contributions made by the developer on behalf of the county, including funds for the construction of roads, parks, police and fire stations, or other infrastructure and improvements

Provided by county officials:

- Estimated cost of services to the new project provided by the county, as these are assumed to be unique for each project
 - One-time expenses related to development and/or construction of the project
 - Ongoing expenses for general county services (e.g., police, fire, roads, and parks)

Upon input of required information, the model will generate a pro forma financial statement including selected financial metrics. The pro forma financial statement will be used to derive calculations necessary for the concluding analyses; that is, the two conditions outlined in AB 239 that serve as potential grounds for denial of an application for abatements/incentives. The model will incorporate a summary of the concluding analyses on a single page within the model that can be easily exported or simply printed to PDF and used for reporting and submittal purposes.

It is important to note that the model is intended to function as a starting point; essentially, it will provide a general idea of whether grounds for denial of an application for tax incentives may exist. That said, every project is unique, and county officials may determine that adjustments to the baseline impact may be required where mitigating circumstances exist. Qualitative considerations may also be important for a particular project, given the environmental significance of renewable energy policy decisions.

OUTLINE OF EVALUATION PROCEDURES

OBTAIN AND INPUT DATA RELATIVE TO THE CONSTRUCTION AND OPERATION OF THE NEW PROJECT

The input of cost data relative to the construction of the new project is necessary to estimate the one-time economic and fiscal benefits of the project, including jobs and sales tax generated by the construction phase, as well as the ongoing fiscal benefits related to property tax generated through the construction of improvements on land that may otherwise have little taxable value.

Likewise, cost data relative to the operations of the new project is necessary to estimate the ongoing economic and fiscal benefits of the project, including operational jobs and sales tax generated by ongoing taxable maintenance, supplies and equipment purchases. As mentioned in the preceding subsection, ongoing property tax collections may be derived based on the initial capital investment.

As described previously in the context of required inputs, construction and operational data obtained from the applicant should be input into the model via a summary input page. In the case that certain information is unavailable, county officials may need to develop estimates for specific inputs by consulting with the applicant to develop good faith estimates, or by basing estimates on the county's experience with prior, similar projects. In addition, county officials may find it useful to consult with other Nevada counties that have undergone similar analyses.

ESTIMATE THE ECONOMIC BENEFITS OF THE PROJECT, INCLUDING DIRECT EMPLOYMENT IMPACTS

Economic impact assessment examines the economic implications of a proposed development in terms of employment, wages and output (i.e., production). Impacts are often differentiated by time; for example, construction-phase impacts are generally short-term effects, while

operation-phase impacts are long-term consequences generated by the operation of the project. Within each phase are several types of impacts, including employment impacts that encompass both on-site and off-site employment, and expenditure impacts that extend to both vendors and suppliers of a project and consumptive spending by employees, as well as the ripple effects of these expenditures throughout the region.¹

In the case of a proposed renewable energy facility, the economic benefits of the project may be sourced to both the construction phase and the operations phase of the project in question. The model will be designed to calculate and present the economic benefits of the project, including the employment impacts, separately for the construction phase and operations phase.

Based upon the provided description of the facility, the user of the model may select a facility type (i.e., energy type) from among a list included in the model. At this time, energy generation is the only industry category included in the model, as transmission facilities have been eliminated from the list of qualifying facility types by AB 239. Direct, indirect and induced economics impacts – including employment, wages and salaries, and economic output – would be generated by the model based on a set of input-output variables generated by IMPLAN (Impact Analysis for Planning).² An overview of the three types of economic impacts is provided below:

- Direct impacts measure the effects of the specific impacting force being considered. In this case, for example, construction or operations jobs required for constructing and operating a proposed energy project are considered direct jobs and the wages and salaries those employees are paid are considered direct personal income.

¹ See also, Burchell, Robert W., David Listokin, et al. *Development Impact Assessment Handbook*. Washington, D.C.: ULI-the Urban Land Institute, 1994.

² IMPLAN is one of the nationally recognized economic impact analysis software tools and has been utilized for over 35 years by governmental agencies and private sector businesses.

Direct impacts = employees directly hired by project + wages paid directly by project + output produced directly by project

- *Indirect impacts* consider how other businesses respond to the impacting condition. Employees of the proposed energy project's suppliers, for example, are considered indirect employees to the extent their jobs are dependent, in full or in part, on the suppliers' revenue generated by the proposed project's purchases.

Indirect impacts = employees supported by vendor/supplier purchases by the project + wages paid to vendors/suppliers + output produced directly by vendors/suppliers

- *Induced impacts* measure the effects of increased (or decreased) consumer expenditures resulting from wage and salary payments sourced to an impacting condition. In this case, for example, if a new person were to be employed by the proposed project, he/she might be expected to spend a portion of his/her monthly salary at the supermarket or the local movie theater. Induced effects capture the impacts of this spending as it "ripples" through the local economy.

Induced impacts = jobs supported by project employee spending within the community + wages earned by those supported by project employee spending + output generated by project employee consumption

To identify the interrelationships in a regional economy, the IMPLAN software, databases, and methodology may be used when estimating the economic impacts generated by the new project. IMPLAN is one of three generally accepted applications that are used to model how industries within an economy are interrelated. The model attempts to demonstrate mathematically how the outputs of one industry become the inputs of other industries.

IMPLAN employs a regional social accounting system that is used to generate a set of balanced accounts and

multipliers. The social accounting system is an extension of input-output analysis. Input-output analysis has been expanded beyond market-based transaction accounting to include non-market financial market flows by using a social accounting matrix framework. The model is designed to describe the transfer of money between industries and institutions (e.g., households) and contains both market-based and non-market financial flows, such as inter-institutional transfers. IMPLAN uses regional purchase coefficients generated by complex econometric equations that predict local purchases based on a region's characteristics. In this case, the region would be the county in which the proposed project plans to locate.

ESTIMATE THE FISCAL BENEFITS OF THE PROJECT PRIOR TO POTENTIAL ABATEMENTS/INCENTIVES

At its most basic level, fiscal impact analysis compares the public costs and public revenues associated with residential and/or nonresidential growth.³ If costs exceed revenues, a deficit is incurred; if revenues exceed expenditures, a surplus is generated. While the practice of cost-revenue analysis is commonly conducted to ascertain whether outlays would justify returns, the concept can be applied to the decision of whether to grant tax incentives or abatements, which may be considered a form of expense to a local government as they represent revenue that would otherwise have been received by the government entity.

Similar to the economic benefits generated by the project, the fiscal benefits of the project may be sourced to both the construction phase and the operations phase. The model will be designed to calculate the fiscal benefits of the project for each year over a 20-year time horizon.

Fiscal impacts of the project would be expected to include the following major taxes:

³ See, Burchell, Robert W., David Listokin, et al. *Development Impact Assessment Handbook*. Washington, D.C.: ULI-the Urban Land Institute, 1994.

- Sales taxes
 - Sourced to taxable materials purchased for construction of the project
 - Sourced to ongoing taxable maintenance and/or supplies purchases during the operations phase

Sales taxes inuring to county = local component tax rate x taxable purchases

- Property taxes
 - Sourced to improved value resulting from capital investment; both land and improvements should be included in property tax estimates; note that in the model, in accordance with Nevada's property tax system, property tax rates will be applied to the assessed value of real property, where assessed value is equal to the taxable value (market value less a depreciation factor of 1.5 percent per year) times 35 percent

Property taxes inuring to county = local component tax rate x taxable value x 35 percent

- (Optional) Modified business taxes
 - Sourced to payroll during both construction and operations
 - Modified business taxes do not directly inure to county governments; as such, modified business taxes are not expected to be included in total fiscal benefits for purposes of this analysis
 - Additional capital contributions made by the developer
 - Developer-contributed capital contributions may include roads, parks, police stations, or other improvements built by the developer on behalf of the county as a result of the project

The model will incorporate detailed breakdowns of sales and property tax components respective to each county so that potential tax collections may be determined with a greater degree of accuracy.

CALCULATE POTENTIAL ABATEMENT/INCENTIVE AMOUNT

The potential abatement/incentive amount provided for under NRS 701A.360 is estimated by applying applicable abatement percentages to the estimated fiscal impacts of a proposed project (i.e., tax revenues prior to any abatements or incentives). The model will be designed to automatically calculate potential abatement/incentive amounts based on the previously required inputs and subsequent calculations performed by the model.

NRS 701A.360 allows the following partial tax abatements for qualifying renewable energy facilities:

- Partial abatement of property taxes imposed pursuant to NRS 361, equal to 55 percent of the taxes on real and personal property payable by the facility each year, for a duration of 20 years

Property tax abatement calculation = real and personal property tax due prior to abatement x 55 percent (every year for 20 years)

Amount due county after abatement = 45 percent of amount due prior to abatement (every year for 20 years)

- Partial abatement of local sales and use taxes, equal to the portion of the combined rate of all local sales and use taxes payable by the facility each year which exceeds 0.6 percent (0.25 percent effective July 1, 2015), for 3 years beginning on the date of approval of the application (i.e., the facility is only required to pay a sales and use tax rate of 2.6 percent for the abatement period (2.25 percent effective July 1, 2015))

- Sales and use tax collections are allocated entirely to the Local School Support Tax (LSST) component of the Nevada sales and use tax; the LSST is designed to be distributed to the school district in the county of origin

Prior to July 1, 2015: sales and use tax abatement calculation = sales and use tax due prior to abatement – {taxable purchases x 2.6 percent} (every year for 3 years)

On or after July 1, 2015: sales and use tax abatement calculation = sales and use tax due prior to abatement – {taxable purchases x 2.25 percent} (every year for 3 years)

Amount due county (excluding LSST) after abatement = \$0 (every year for 3 years)

ESTIMATE THE FISCAL BENEFITS OF THE PROJECT AFTER POTENTIAL ABATEMENTS/INCENTIVES

Once the potential abatement/incentive amounts have been calculated according to the preceding procedure, the fiscal benefits of the project after potential abatements/incentives have been deducted can be determined. The model will be designed to automatically calculate the fiscal benefits of the project after potential abatements/incentives.

DEVELOP A SUMMARY OF THE EXPECTED COST OF SERVICES PROVIDED BY THE COUNTY TO THE PROJECT

The final evaluation procedure may require the most judgment from county officials of all the steps required to assess the costs and benefits of a project. County officials must develop a summary of expected costs to the county resulting from the project. Developing an estimate of such service costs may require input from a variety of county departments, including public safety officials; infrastructure departments including roads, water, and sewer; and county finance department officials.

A best-practice may include the development of a service cost estimate per capita or per employee for each county. However, it is worth considering that a project locating where little to no infrastructure presently exists versus a project locating in a relatively populated area of a county may have significantly different demands upon county services, both upfront and on an ongoing basis.

An outlying project may require significant capital investment on the part of the county, including the construction of new roads or a new fire station. Calculations may be further complicated if negotiations have resulted in the developer of the new facility agreeing to be responsible for paying for specific improvements. Note that any capital contributions made by the developer on behalf of the county, including funds for the construction of roads, parks, police and fire stations, or other infrastructure and improvements, would effectively reduce the amount of cost incurred by the county to accommodate the project.

While additional research is merited in this area, the model will preliminarily be developed to require a single dollar amount representing a good faith estimate by county officials relative to both the one-time and recurring expected costs of services provided by the county to the project.

CONCLUDING ANALYSES

After the required inputs have been provided and the evaluation procedures outlined above have been completed, either by the user or through automatic calculation by the model, the concluding analyses will be generated by the model.

COMPARE THE EXPECTED COST OF SERVICES WITH THE FISCAL BENEFITS AFTER POTENTIAL ABATEMENTS/INCENTIVES

The first condition under which a board of county commissioners may deny an application for abatements/incentives is when the projected cost of services that the local government is required to provide to the facility will exceed the amount of tax revenue that the local government is expected to receive as a result of the abatement.

To determine whether this condition has been met, the model will be designed to compare the expected cost of services that the county will provide with the fiscal benefits after potential abatements/incentives; both of these components are described in the preceding sections. Such a calculation may result in a positive or a negative dollar amount.

If cost of services > tax revenue (net of abatements), then possible grounds for denial of request exist

COMPARE FINANCIAL BENEFITS OF THE PROJECT WITH THE ABATEMENT/INCENTIVE AMOUNT RECEIVED BY THE PROJECT

The second condition under which a board of county commissioners may deny an application for abatements/incentives is when the projected financial benefits that will result to the county from the employment by the facility of the residents of the state and from capital investments by the facility in the county will not exceed the projected loss of tax revenue that will result from the abatement.

To determine whether this condition has been met, the model will be designed to compare the direct employment impacts (e.g., wages and salaries paid to employees that will result in a benefit to the county in which the facility intends to locate) and the amount of non-labor capital investment expected to be retained in-county with the abatement/incentive amount received by the project; both of these components are described briefly in the preceding sections. Although not specifically directed under AB 239, the model will also be developed such that it allows an expansion of employment impacts to include indirect and induced wages and salaries (rather than only direct impacts).

If financial benefits < loss of tax revenue, then possible grounds for denial of request exist

The model will incorporate a summary of both concluding analyses on a single page within the model that can be easily exported or simply printed to PDF and used for reporting and submittal purposes.