"But For" Percentages for Economic Development Incentives: What percentge estimates are plausible based on the research literature?

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ABSTRACT

"This paper reviews the research literature in the United States on effects of state and local "economic development incentives." Such incentives are tax breaks or grants, provided by state or local governments to individual firms, that are intended to affect firms' decisions about business location, expansion, or job retention. Incentives' benefits versus costs depend greatly on what percentage of incented firms would not have made a particular location/expansion/retention decision "but for" the incentive. **Based on a review of 34 estimates of "but for" percentages, from 30 different studies, this paper concludes that typical incentives probably tip somewhere between 2 percent and 25 percent of incented firms toward making a decision favoring the location providing the incentive. In other words, for at least 75 percent of incented firms, the firm would have made a similar location/expansion/retention decision without the incentive.** Many of the current incentive studies are positively biased toward overestimating the "but for" percentage. Better estimates of "but for" percentages depend on developing data that quantitatively measure diverse changes in incentive policies across comparable areas."

This review of the research literature can derive 34 estimates of "but for" percentages from 30 studies. The most common type of study compares incented firms and unincented firms within a single state. Other studies compare counties that differ in incentive usage within a single state. Still other studies are based on surveys that ask firms or economic development experts to estimate "but for" percentages. A final group of studies uses data from multiple states and compares the economic performance of states with different incentives.

The main reason "but for" percentages aren't higher is that there are many other location and cost factors that have more major effects on a firm's costs and profitability. A secondary reason in some studies is that one firm locating in an area may reduce the likelihood of other firms choosing that location.

These other location and cost factors not only are a larger share of costs than typical incentives, but also vary quite a bit across state and local economies. Because these other location and cost factors vary greatly across diverse state and local areas, typical current levels of incentives are only able to tip a location decision toward a particular state or local area in a minority of cases, and probably less than one-quarter of cases

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