



State Rep. Melissa Hortman, Brooklyn Park Mayor Jeff Lunde, and Brooklyn Park City Manager Jamie Verbrugge

Using subsidies to attract businesses can benefit community

A Civic Caucus Focus on Competitiveness Interview

November 22, 2013

Present

Dave Broden (vice chair), Janis Clay, Pat Davies, Paul Gilje (coordinator), Rep. Melissa Hortman, Sallie Kemper, Dan Loritz (chair), Paul Ostrow, Dana Schroeder, Clarence Shallbetter. By phone: Jamie Verbrugge and Jeffrey Lunde.

Summary

Offering businesses subsidies to locate or expand in a community has become an integral part of economic development strategy, say state Rep. Melissa Hortman, Brooklyn Park Mayor Jeff Lunde and Brooklyn Park City Manager Jamie Verbrugge. But the local, national and global competition for high-end business development potentially allows companies to pit communities against each other in offering the best incentives, which can drive up offers, Verbrugge says.

The three officials reflect on their experience with Brooklyn Park's just-completed successful effort to attract Baxter International, Inc., a biopharmaceutical company, to an empty biologics facility in the city. The city competed internationally in trying to attract the company, Lunde says, and put together a successful deal with Baxter that combines both state and local subsidies. The total publicly-funded incentive package for the \$200 million project could cost \$10 million to \$12 million and includes money from the Minnesota Investment Fund, a state sales tax exemption, locally raised tax-increment financing funds and a 10- to 20-year property tax abatement from the city. In exchange for the subsidies, the officials point out, Baxter will have to meet certain performance requirements, including creating a certain number of highly skilled, high-wage jobs.

A recent survey shows that more than three-quarters of Brooklyn Park residents approve of the use of incentives to attract economic development. Hortman believes the Baxter deal is good for the city's residents because it increases the tax base, brings in new jobs and raises the values of existing homes.

Background

Melissa Hortman (DFL-Brooklyn Park) is Minnesota state representative in District 36B, which includes the City of Brooklyn Park and part of the City of Coon Rapids. First elected in 2004, Hortman is chair of the Energy Policy Committee and a member of the following committees: Civil Law, Commerce and Consumer Protection Finance and Policy, Health and Human Services Finance, Judiciary Finance and Policy, and Rules and Legislative Administration and of the Data Practices Subcommittee. She is an attorney in the Hennepin County Attorney's office. She has a B.A. degree in political science and philosophy from Boston University and a J.D. from the University of Minnesota.

Jeffrey Lunde is mayor of the City of Brooklyn Park, a position he has held since a special election in 2011. Previously, he was a city council member for the city's East District. Lunde has lived in Brooklyn Park for the past 15 years. He works as a Senior Technical Account Manager for VMware Inc., a leading virtualization and cloud technology company. He is responsible for managing technical services for VMware at Medtronic and Best Buy. Lunde has served on Brooklyn Park's Planning Commission and Human Relations Commission and on the Northwest Hennepin Human Services Commission. He was a member of the Hennepin County Library Board, the SourceOne Federal Credit Union Board of Directors and the Anoka-Hennepin School District Parent Legislative Team. He holds a Master's Degree from Minnesota State University - Mankato and a Bachelor's Degree in Political Science from North Dakota State University.

Jamie Verbrugge has been city manager of the City of Brooklyn Park since 2008. Prior to holding that position, he was city administrator of the City of Rosemount for five years. Since 1993, he has served local governments in the cities of Richfield and Eagan, in Minnesota's Stearns County and in Washington's Franklin County Emergency Management. He has a B.A. degree in history/political science from St. Cloud State University and an M.A. degree in public administration from Hamline University in St. Paul.

Discussion

Baxter International's possible interest in locating in Brooklyn Park came through a relocation consultant as a blind request. State Rep. Melissa Hortman (DFL-Brooklyn Park) explained that Brooklyn Park's proposal for incentives to attract Baxter International, Inc., a biopharmaceutical company, came to her attention when the city asked if she would chief author a bill supporting the incentives in the 2013 legislative session. She agreed. "My job is to support my cities when they're working on economic development," she said. At that time, neither Brooklyn Park nor Hortman knew the name of the company involved.

Brooklyn Park City Manager Jamie Verbrugge noted that the city's staff business developer works closely with Minnesota's Department of Employment and Economic Development (DEED) and with Greater MSP, a nonprofit organization dedicated to growing the economy of the 16-county

Minneapolis-St. Paul region. "She's networked in when they see proposals of companies looking at coming into or expanding in Minnesota," he said.

"Baxter came through DEED as a blind request," he continued. "Deloitte Consulting did the site selection process for Baxter. We only knew we were working with Deloitte and we didn't know what company. Deloitte outlined the scale of the project and what kind of industry it was and then asked communities what kind of incentives they could provide." Verbrugge said Deloitte was looking for incentives, the overall business climate in the city, and the process and timing for the city's development review.

"We put a package together in the blind, which is not unusual for us," he said. Brooklyn Park Mayor Jeff Lunde met with Deloitte in November 2012. "The project was code-named 'Project Fern,'" Verbrugge said. "It was top secret. The company wanted to get a feel for personalities, as well. They wanted strong staff support, political support and strong community support. We knew this was a competitive process where they were looking at other sites around the country and around the world."

Brooklyn Park had 10-year-old empty biologics manufacturing and office facility built by PDL BioPharma, Inc., the only facility of its kind in Minnesota. "It was a state-of-the-art facility for biotech design and manufacturing," Verbrugge said. When PDL's product did not get FDA approval, the company sold the facility to Genmab, a biotechnology company. Genmab closed the Brooklyn Park facility after two years, due to the recession. "So we had a state-of-the-art facility sitting there dark," he said.

"Baxter was looking at retrofitting this existing facility," Verbrugge continued, "comparing that to the cost of building in Asia, where land costs and labor costs are less and the permitting process is less cumbersome. We have to be competitive on a global scale." He said the company, still not identified to the city, said in November 2012 that they were walking away from the project. But in January 2013, they said they were back on again.

"At that time," Verbrugge said, "the development manager for DEED was working closely with Deloitte and told us we had to indicate our commitment at a meeting to be held somewhere in the world and it would be on a week's notice. It turned out to be a flight to Chicago and then we learned it was Baxter."

Major decisions are frequently made not knowing who the potential user is . "We want to be competitive globally, knowing that sometimes we take a risk by not knowing who we're dealing with," Verbrugge said. "I appreciate that Rep. Hortman stuck her neck out on this, too, because she didn't know who it was. When the Legislature is talking about incentives, that can be a difficult thing, given Minnesota's reputation for transparency and open government." He said it was "a little bit tough when operating in the blind. They didn't tell us a dollar amount we had to hit."

Lunde said Brooklyn Park was not competing with anybody locally on the Baxter deal, because the former PDF facility is unique in the metro area. The competition was global and the competitors were Singapore, a Chinese province and somewhere in Europe.

The company was interested in the training available for biopharmaceutical jobs. An interviewer asked where in the process Deloitte described what kind of workforce skills and what mix of workforce would be employed in the facility. Mayor Jeff Lunde responded that during negotiations in the fall of

2012, the city met with Deloitte, the Minnesota State Colleges and Universities system (MnSCU) and North Hennepin Community College and talked about training for biopharmaceutical jobs. Lunde said at one point during the negotiations, the city's competition in China was offering free training for everyone.

Baxter is part of a new industry in the U.S. called biosimilar processing. Lunde said the facility would be used primarily for very technical manufacturing and for research and development. Verbrugge said Baxter is in the business of biosimilar processing, which he likened to manufacturing generic drugs. Instead, they're making biological products that are biosimilar, or interchangeable, with already approved, FDA-licensed biological products.

Verbrugge said the biosimilar industry is new in the U.S. The Affordable Care Act created an abbreviated licensure pathway for biosimilar biological products, while in Europe, biosimilars have been approved for a number of years. "For us," he said, "it's an opportunity to get a foot in the door with an industry that's untapped here in the U.S. and that we think will be a pretty expansive growth industry."

The final financial package for Baxter is a state and local partnership. An interviewer asked what the final financial package was and why state legislation was needed. Verbrugge replied that the city alone wouldn't have been able to provide an incentive package that "met Baxter's total needs." He said the state contribution came through the Minnesota Investment Fund and a sales tax exemption on construction materials. The city share involved tax-increment financing (TIF) and property tax abatements. Several years ago, he said, the Legislature gave cities the flexibility to pool excess increments that are collected from a number of TIF districts in a city.

(Tax-increment financing (TIF) is an economic development tool available to Minnesota cities under state law. Cities may create TIF districts for economic development, housing, redevelopment or pollution cleanup. The TIF districts, which take in the area slated for development, redevelopment or cleanup, generate revenues to help pay the costs of those activities. The revenues, known as the *increment*, are the property taxes generated each year on the *increase in taxable value* within the district. So TIF revenues depend on the taxable value increasing over the life of the TIF district to generate the increment. The TIF increment revenues are *captured* to help pay for various improvements in the TIF district and are not available during the life of the district as general revenue for the city, the county, the school district or any special taxing districts in which the TIF district is located.)

According to Verbrugge, the state and city financial package for Baxter includes:

- \$1.5 million of pooled TIF funds from the city;
- \$3 million to \$5 million in state money from the Minnesota Investment Fund, with the amount dependent on whether Baxter expands the facility and creates additional jobs in a second phase of the development;
- Up to \$1.86 million in city property tax abatements over 10 years for Phase I and up to another \$1.86 million over 10 years for Phase II; and

- An exemption from state sales taxes on construction materials.

In exchange, Baxter plans to reactivate the biologics facility and bring 190 skilled jobs to Brooklyn Park, with the potential for more jobs in future phases. The 190 Phase I jobs need to have an average salary of \$75,000. Phase II, a possible expansion of the facility, could include employing an additional 190 or more similar workers.

"We tied our incentives to the jobs Baxter was committing to create here in city," Verbrugge said. "They have to deliver on the jobs to qualify for the abatement." He pointed out that Brooklyn Park has a subsidy policy that requires jobs in business projects getting a city subsidy to average compensation three times greater than the minimum wage. "We're very focused on living-wage jobs and higher," he said.

Verbrugge said both PDL and Genmab, the two previous owners of the facility where Baxter will locate, received TIF help from the city. Neither met the city's required performance standards, so there are still TIF funds available that those companies never received. "We were able to extend and revive some of the assistance that had been pledged earlier, because it was tied to the property," he said.

The total state and local investment in the Baxter project could be in the area of \$10 million to \$12 million, out of a total project cost of \$200 million. For a recent \$250 million Baxter project in Georgia, Verbrugge noted, the state, county and city jointly funded over 20 percent of the project costs. "We are far below that number," he said. "That shows you where we are in terms of being competitive on a national scale, not even looking at the global scale."

Brooklyn Park had already used subsidies to attract businesses. Hortman referred to two projects Target has done in Brooklyn Park and said the total tax abatement for the two projects is \$30 million. "When the Baxter deal came along," she said, "this wasn't like a foreign language to us in Brooklyn Park to deal with the moral issue or philosophical issue of whether we should be doing subsidies to get people to come to our community. It was a bridge we had already crossed before and we had really seen it benefit the community with the Target campus. Baxter is doing the work here only because of the package."

Subsidies are part of the economic development game. "As a state legislator, the city asked me to carry this legislation to get money from the Minnesota Investment Fund and to get a state sales tax exemption for construction materials," Hortman said. "I'm not a big fan of subsidies. I wish this was not a game that gets played in economic development, but it is how the game is played. You might not like it, but if you want to participate in the process, that's the game you play. It's not a perfect system."

"If relocation experts like Deloitte weren't out there doing this and the other jurisdictions in the country weren't playing this game," she continued, "we would not also need to play the game. But looking at the deal for the citizens of Brooklyn Park, I think it is a good deal, because we really need the jobs and we really need the real estate values to go back up."

Verbrugge added, "If there's a criticism of how economic development incentives are used, it's that it potentially allows companies to pit communities against each other. It tends to drive up offers.

Companies receiving subsidies must meet performance standards. Lunde explained that the city "backs in the money." The companies have to perform and the city calculates the number of jobs they actually create. "We are very purposeful in not just handing stuff over," he said. "If they don't perform, they don't get the money. We're willing to participate, but not just to give. There must be a mutual benefit. If the company wins, we win. If a company is not performing, we're pretty ruthless."

Brooklyn Park is in a competitive environment in the metro area. "Look at Brooklyn Park and then look at Maple Grove, Plymouth, Eden Prairie, and Minnetonka," Verbrugge said. "These cities don't have to do much to attract high-value commercial development. Our city is left behind in that equation, unless we can change the conditions to try to attract businesses here. The consequence if we're not participating is that our tax base suffers. It's difficult for us to deliver city services if we don't have a balanced tax base. Having a healthy tax base is a primary reason we're out there trying to woo high-value commercial development."

Verbrugge reported that the city is about to finalize a deal with Olympus Corporation, a medical device maker, to relocate more than 315 employees from Maple Grove to a brand new office and R&D center along Highway 610 in Brooklyn Park. He said the city was competing nationally and locally, because the company was looking to consolidate its operations and expand, instead of being located in five different buildings, as they are in Maple Grove. Several cities in the metro area were being considered, as were Boston, Memphis and Cleveland. "There's a perception that Brooklyn Park is stealing jobs from another community because of a subsidy," he said. "But if they hadn't chosen Brooklyn Park, there's a good chance they would have chosen another state."

Brooklyn Park needs high-end commercial development on its northern side to help meet the challenges of poverty in the city. An interviewer asked if Brooklyn Park has a continuing incentive to get things developed because it has set aside so much land in its northern half for commercial development. Lunde responded that the city is half diverse, with a lot of poverty and an achievement gap between different racial and ethnic groups. "We need tax base on the north side of the city as a counterweight. We're not Eden Prairie or Maple Grove. They don't have the same challenges of poverty that we do. We're more like Minneapolis and St. Paul. We need that tax base."

Verbrugge said Brooklyn Park is 20 percent foreign born and 50 percent nonwhite. "We're trying to negotiate with Target and others on how they can make their presence here a benefit to the entire community, besides just the tax base."

The Legislature must approve payments from the Minnesota Investment Fund (MIF). Hortman said MIF is smaller and more difficult to access, compared to similar funds in some other states. She said the Legislature appropriates \$10 million to \$30 million to it in a biennium and then appropriates payments out of the fund.

Verbrugge added that DEED has the authority to make payments of \$1 million or less out of MIF. Since the Baxter project, the Shutterfly project in Shakopee and the 3M project in Maplewood all needed more than that, special legislation was required to authorize funding for each of them.

Business subsidy deals are part of the political process. An interviewer commented that it seems business subsidies are determined outside of the priorities that the Legislature and city councils set for spending. Hortman replied that both the Legislature and the executive branch have roles in

determining the subsidies. "To some degree we're supporting the functions in DEED that we've already given them authority to do," she said. "We give deference to the agency's work when they come to us for special legislation, because we've given them the budget to do this work."

"It doesn't happen outside the political process," she said. "There's a sense there's a secret back room where these deals get cooked up. No, but the original proposal doesn't get created at a legislative hearing. We did, though, have a very full, very challenging hearing on the Baxter deal."

Verbrugge said that in the aftermath of the Baxter deal, some city council members asked when the city gets to say no. "The perception for many is that these big corporations come with their hands open. We aren't in a good position to say no. How do we remain competitive within that environment?"

Most Brooklyn Park residents approve of using subsidies for economic development.

Verbrugge said Brooklyn Park does a community survey every two to three years. In the survey done last June, one question asked people about their support for using subsidies or incentives for economic development. "It came in at 77 percent support," he said. "It's off the charts. Our community understands that we have challenges here that are relatively unique in the metro area and our residents want us to be aggressive in resolving them."

Hortman's legislative work generally focuses on the state's foundational structure: getting transportation infrastructure in place and having the higher education infrastructure supported. "As a state legislator, the investment attractiveness piece is one thing I think about and spend time on," she said. "But I have spent the bulk of my legislative energy on foundational competitiveness."

She said Brooklyn Park "is a little bit of a laggard" in development because of the lack of transportation investment there. "Brooklyn Park will take off a little bit more on its own without subsidies when we complete Highway 610," she said. She is fighting for the future Bottineau light-rail transit (LRT) line to terminate at the city's Target campus instead of in Maple Grove. "LRT lines are more real estate development tools than pieces of transportation infrastructure," she said. "They're equally as important in redevelopment as they are in moving people from point A to point B."

Hortman has a very positive impression of DEED. When asked for her impression of DEED, Hortman said she doesn't work a lot with the agency, "but they seem to be very, very active. They're cooking with gas under this administration. I see a very active agency using all the tools in its toolbox. Since [Gov. Mark] Dayton's election, I hear from DEED that we can do it, we're competing, this is a great place to do business, we have a highly educated workforce. We're talking about things that make Minnesota a place to be, rather than talking about the things that make Minnesota not a place to be. I have a very positive impression of DEED."

No one is responsible for ongoing evaluation of whether subsidized business projects have accomplished the city's objectives. An interviewer asked if there is an entity or a person who will monitor the net results of the Baxter transaction and report the results to the citizens. Verbrugge said the state requires an annual report on the city's subsidies, but doesn't ask whether they're actually achieving the city's objectives. "Nobody does that evaluation unless a project fails," he said. Lunde

added, "We are constantly having to assess and reprove why we do this every time the next potential agreement comes up." And Hortman said, "The mayor's political opponents and my political opponents will continue to let us know if it's not successful."

Large amounts of subsidy money could raise ethics concerns. An interviewer asked whether we should be concerned about ethics, with all the money involved in U.S.-wide and worldwide competition. Lunde replied, "Minnesotans pride themselves on being open and honest. We must be constantly talking openly about these deals."

"That's a question that came up in the legislative process," Hortman said. "Is this a special deal for special people? That's the beauty of being anonymous: it doesn't matter who it is. We're looking for whoever would develop this building. It's a transparent process that is open to all competitors of a certain size."

The city offers development opportunities to big and small companies. Verbrugge said it's a legitimate question whether the city should be handing out money to Fortune 100 companies. "Why do they need a few million dollars when they're billion-dollar entities? Is this at the expense of the little guy?" He said through the Brooklyn Park Development Corporation, an independent nonprofit, the city is providing those opportunities for small and large companies. Lunde pointed out that smaller companies need a smaller amount of investment. "We try to service big and small, because they're all important," he said.

Hortman said her family's business, John's Auto parts in Blaine, with 150 employees, has never gone to the city of Blaine for a subsidy. "As a small businessperson, do I think it's fair that John's Auto Parts never got a subsidy from Blaine or from the state to keep our 150 employees employed?" she asked. "You could say that's not fair to incumbent players in the market. But life is not fair. You can't look for perfect justice in government and business."

Conclusion

Hortman concluded by saying, "The relationship between city staff and state leaders is very tight in Brooklyn Park. That allows us to move very quickly when opportunities come up."