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## Company Responsibility

*Community Commitment and Corporate Responsibility*  
By: Ed McCallum

A hot topic in site selection these days is “corporate responsibilities to communities.” The media has been quick to exploit the controversy surrounding this topic, especially when it is focused on incentives. It seems every time a company negotiates a substantial incentive package, the critics jump out of the woodwork. Both the company and the granting agency are called into question, most of the time for no good reason except that it is popular to do so. The company is criticized for requesting, and then accepting, the incentive, while the granting agency is questioned for offering incentives. Some critics have even proposed that state and local incentives should be abolished altogether.

What should a company do when faced with this dilemma? The answer, at least in my mind, is very straight forward: This is business in a free-market economy and both the company and the state/community should get the best deal possible! As with every deal, however, there are mutual performance expectations and obligations that should govern both parties.

### A Free-Market Economy

A free-market economy, by its very nature, is predicated on trading goods and services at a fair and equitable price – a price which the market usually dictates. There is not a single transaction in a free-market economy where an incentive is not being offered. In some cases it is simply quality and reliability. In others, it is a discounted sales price or a buy-one-get-one-free offer. In yet others, it is an externality such as the feeling of well-being or sense of security. The value proposition is a host of variables that the consumer defines and evaluates, then selects to purchase based on this mix of preferences. This is how our economy, and those of our trading partners work. It will continue to work this way until civilization evolves to a utopia of endless benevolence and sharing. Maybe I am wrong, but from what I can see we are quite a way from this state of affairs.

Also, let’s not forget that the company has a fiduciary responsibility to both its shareholders and its employees to be as successful as possible on their behalf. This would be analogous to an extended family whose livelihood and welfare are not separate and apart; instead, they are interconnected and depend on each other.

The company has a duty to make sure that the shareholder investors make an acceptable return on their investment. Similarly, the company is also obligated to make sure that the employees are adequately compensated with a job that is secure and stable. In both cases, selecting the best possible place to do business is not a matter of choice, it is a mandate of conscience and duty to the shareholders, the employees and ultimately to any prospective candidate community.

### Line of Reasoning Extended

Now let’s extend this line of reasoning to states and communities, and even countries. Some have geographic advantages such as climate, ports, rivers, natural resources or vast amounts of real estate, while others have vibrant economies, excellent universities or a large population of workers. Obviously, they are all different; and, because they are different, there is an inherent inequality among them. This inequality, regardless of the reason, provides an advantage to some and a challenge to others, and if left alone, would have consistent winners and losers. This hardly seems fair. In fact, no state, community or country will accept the supposed natural order of things when trying to improve economic well being of its citizens...nor should they. Each one will try to leverage their strengths in order to recruit jobs and investment, or create ways to eliminate (or mitigate) weaknesses when faced with a formidable competitor.

There is only one way to do this and that is through incentives, in whatever form or fashion that can be reasonably justified. And guess what? The principles of business apply here in exactly the same manner. When a deal is cut, if the benefit coming in (jobs, tax revenue, multiplier effects, etc) is greater than the cost of incentives going out (i.e. incentives) then it probably makes sense to do it. In contrast, if the benefit does not outweigh the cost, then it does not make sense to do the deal.

### Responsibility

So, what does this basic review of free-market economics have to do with corporate responsibility to the community? Well, to put it bluntly, everything. All parties involved in any business transaction have a responsibility to make sure that their own best interests are taken care of. This means that the business is obligated to find the very best location to produce its goods and/or service at a price that the market will accept. In a similar fashion, the state/community has a responsibility to make sure that the companies they recruit will provide a greater benefit to the citizenry of the respective locale than the cost required landing the deal. Moreover, the decision is not based on conjecture, good feelings, or the hopeful wishes of a good outcome; instead, it is based on quantitative evidence that suggests the deal makes sense and is fiscally responsible.

A common theme for both the business and the community is an understanding of the deal elements. Being able to measure the cost benefit relationship is just as important for the company as it is to the community. There is absolutely no excuse, nor justification, for any party to a transaction (company or community) to pretend that a cost benefit relationship cannot be measured – because it can. Every element to the transaction can be reduced to a dollar value.



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In the case of the corporation, a standard pro-forma analysis is commonly used. The model incorporates a discount rate that quantifies both risk and return parameters to arrive at a Net Present Value (NPV). In a similar fashion, an Economic Impact Analysis (EIA) is a commonly accepted tool to determine the cost-benefit relationship of the deal to the state and community. It too uses an NPV to determine the value of the deal over time.

Both analyses measure the net gain to the respective entity and should be a common practice in any transaction. It is the opinion of this writer that a failure to do so constitutes poor judgment. At the very least, it makes cutting a good deal more a matter of chance than a logical thought process.

#### **Control Destiny**

This author believes, without hesitation, that economic development agencies have control over their destiny. Communities are not forced to do anything by companies. Communities can decline to participate in any deal. Often, the pressure that an economic developer experiences, comes from those within their own organization and not from the company considering their community. The only way to counter irrationality on either side of the fence is to understand the deal and the impact that it could have on the community in an unbiased and analytical fashion. Without a cost-benefit analysis, you might as well stick your head in the sand and hope for the best.

To be fair, however, this author is not holding some corporations blameless either. Companies have a responsibility to the communities in which they locate. Once a company decides to invest resources and people into a community, they are no longer a disinterested third party; instead, they become an integral part of it. They are responsible to make sure that they not only live up to their part of the bargain, but also to make sure that the bargain was a good one for all parties concerned. (I do not know of a single company considering a merger and acquisition that does not first complete a full due diligence investigation into the health of the company they are about to acquire. Similarly, a company should investigate the health of communities in which they are considering making investments.)

It makes good business sense to fully understand the ability of the community to sustain fiscal continuity and stability. First and foremost, your employees live and work there and have just as much at stake as the company. Second, if the community cannot provide the normal services and benefits expected by the company in the future, then perhaps your firm should no longer consider that community. Ultimately the firm will have to compensate for a lack of performance – again, this is good business sense. Third, it is quite possible that the benefit your firm provides the community is drastically underestimated which means that you have negotiated poorly and probably should ask for more. Obviously, it is in your best interest to understand this relationship fully. Finally, sometimes the communities do not have the wherewithal or resources to adequately assess the cost-benefit relationship that may, or may not, ensue due to your investment. If this is the case, then it is more than just the firm's responsibility; it is their moral duty to provide information to both company decision-makers and community leaders.

#### **Obligations**

It goes without saying that companies are obligated, by law, to provide for the health and safety of their employees. Regulatory compliance is not a matter of choice, it is a legal requirement. In the same manner, when companies receive incentives, there is typically some element of formal performance obligation, focused on the amount and timing of investment and jobs. This may come from the legislation behind the incentives and/or a development agreement. In either case, the company "obligations" are specific and the basis for the incentives should not be ignored or taken lightly. When a bargain is struck, all parties must live up to their agreements and act in good faith to achieve them.

#### **Conclusion**

As stated in the first paragraph of this article, this is business in a free-market economy and both the company and the state/community should get the best deal possible! Like it or not, these are the facts. The only way to compete is to have a tool box of incentives to level the playing field. This is true for business and it is no less true for economic development. There are a myriad of incentive types that can be identified and requested. Some incentives are financial such as tax breaks, cash, training, abatements and much more; while others have to do with risk, business climate, schedule, quality of life, etc.

Regardless of incentive type, the benefits of an incentive can be measured and reduced to a number that can be expressed in dollars and cents. Corporations today have a duty to their shareholders, employees and customers to provide the best product or service possible at a fair and reasonable price based on the value proposition offered. This same principle applies to their dealings with states and communities and vice versa. Making the deal is in everyone's best interest as long as all parties benefit and understand what they are giving and receiving. A lack of understanding, and then the execution of a bad deal, is irresponsible – regardless of which side of the table you sit. In business, it never makes sense to abuse a customer or business partner since such action will ultimately come back to haunt you.

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