CABINET FOR ECONOMIC DEVELOPMENT

Ernie Fletcher
Governor

Old Capitol Annex
300 West Broadway
Frankfort, Kentucky 40601
ThinkKentucky.com

John E. Hindman
Secretary

June 19, 2007

The Honorable Ernie Fletcher
Governor of Kentucky
The Capitol
700 Capitol Avenue
Frankfort, Kentucky 40601

Dear Governor Fletcher:

You have asked me to address the following question: Can the current statutory economic development incentive programs provide meaningful incentives to a $1 Billion to $3 Billion alternative fuel facility?

In the bill draft that was shared with the Cabinet for Economic Development on Monday, June 11, an alternative fuel facility was defined as one that produces fuels for sale using coal as its primary resource. Our immediate reaction was that any such facility would be ineligible for any existing Economic Development tax incentives. By definition, coal or mineral processing are explicitly excluded from all of the primary tools available to the Cabinet for the recruitment or retention of a potential applicant.

The definition of "eligible company" for the Kentucky Rural Economic Development Act (KREDA) and the Kentucky Industrial Development Act (KIDA) states that the project must be engaged in manufacturing, electric generation, or agribusiness. The statutory definition of "manufacturing" in both programs specifically states "...manufacturing shall not include mining, coal or mineral processing, or extraction of minerals." Due to that language, none of the facilities, as described to us in general terms by the Office of Energy Policy, could qualify under those programs.

The Kentucky Jobs Development Act (KJDA) requires that the applicant fall within certain NAICS codes to qualify. These alternative fuel projects do not fall within the allowable NAICS codes. The Kentucky Enterprise Initiative (KEIA) requires that projects qualify for one of the other programs mentioned above in order to be eligible. Therefore, these projects are not eligible for that incentive. None of the loan/grant programs have available funding for a project of this magnitude even if the projects were eligible.

Even if the definitions above were not an issue, and we were somehow able to approve applicants engaging in this activity, based on the information we have received to date from the Office of Energy Policy, it is highly unlikely that these programs would produce enough inducement to influence the location decisions for these facilities. By our normal standards, awards by the Kentucky Economic Development Finance Authority (KEDFA) generally fall within a range of $20,000 to $30,000 per job. At 190 jobs (estimated) the potential approved cost would be $3.8 million to $5.7 million dollars. For a facility that is projected to entail a capital investment between $1.0 and $3.0 billion, the incentives from our existing credits would not even be 1% of the capital investment. Given the incentive packages offered by other similarly situated states, it is extremely unlikely that our existing incentives would be of a magnitude capable of attracting this level of economic activity.

Moreover, only full time employees working at the facility are included in the per job calculations for CED incentives. The workers employed as contractors and subcontractors as part of the construction and installation process could not be used in negotiating the award amount under existing programs. It is our understanding, based on information from the Office of Energy Policy, that because of the highly-advanced technologies employed in alternative fuel facilities, the mix of capital and labor is highly skewed toward advanced technologies. This fact, coupled with the fact that existing economic development credits are calibrated to a recoverable dollar per job standard, renders the current arsenal of credits ineffective in recruiting alternative fuel facilities.

Finally, neither the staff at CED nor the KEDFA board members have the expertise needed for the analysis of these projects. There will need to be analysis of environmental impact, both general and resident-specific. The agency or body that considers these projects will need to have the expertise to balance potential state investment to potential benefit while including in that analysis any environmental risk. That expertise does not currently exist within CED. The current programs do not require environmental analysis as that has not previously been an issue so there is no clear statutory authorization to obtain the information required for that purpose.

Note that while all the definitional analysis may not prohibit approval of biodiesel projects, ethanol projects or electric generation facilities, the other issues stated above would still be applicable.

Therefore, given the capital-intensive nature of the alternative fuels business model as conveyed to us by the Office of Energy Policy, and given the necessary restrictions in the existing laws, it is not practical to extend existing Economic Development incentive programs to alternative fuel facilities. Even if the language could be statutorily amended or expanded to accommodate these large fuel facilities, the expanded language would not be consistent with current economic development policy.

Please do not hesitate to contact me directly if I can be of assistance in this analysis.

Sincerely,

John E. Hindman
Secretary