

The Value in Strategically Distributing PILOT Funds to Drive Economic Development Initiatives

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August 29, 2024

Introduction: The Strategic Value of PILOT Programs

Payment in Lieu of Tax (PILOT) programs are vital economic development tools used by cities and counties to attract and retain businesses. They provide communities with the mechanisms needed to secure investments and remain competitive in the global marketplace. This, in turn, creates jobs, stimulates economic growth, and brings in new capital expenditures. Furthermore, PILOT agreements have the potential to create new funding avenues for important community initiatives. Although PILOT programs typically reduce or eliminate tax liabilities for businesses, economic development organizations often design their agreements to distribute payments in lieu of tax in the same manner as traditional tax revenues, with proportional amounts going to the city and the county. However, Gallatin's Economic Development Agency and Industrial Development Board have begun crafting agreements that allow for more strategic allocation of funds that have potential to create lasting impacts within the community. Instead of just feeding municipal general funds, PILOT monies will now directly finance projects that strengthen the workforce, enhance the education system, and foster business growth. By optimizing the distribution of PILOT funds, Gallatin's economic development organizations can manage some of the capital needed to enhance small business growth, existing industry retention, workforce development, business recruitment, and infrastructure.

Overview of PILOT Program Implementation

PILOT programs are implemented through structured agreements between government authorities, local economic development agencies, and businesses seeking incentives. These agreements allow businesses to forgo property taxes in exchange for making payments that are typically less than the tax liability, lowering the cost of doing business and serving as financial incentives. Each PILOT agreement has a defined expiration date, typically ranging from 5 to 20

years, depending on the scope and scale of the project. Throughout the course of the PILOT program, payments in lieu of tax are collected and distributed according to the agreement. In Gallatin, these checks are paid to the Industrial Development Board, and until recently, would have then been disbursed in their entirety to the City of Gallatin and Sumner County. Upon better analysis of the current constraints, an opportunity emerged to change PILOT agreement procedures. With precise language in the contract earmarking a portion of the payments for specific initiatives, there is an opportunity to better financially support programs and projects that strategically align with economic development goals.

In Gallatin, the PILOT program is overseen by the Industrial Development Board and the Economic Development Agency. The Industrial Development Board is empowered by state law T.C.A. § 7-53-305 to acquire, own, lease, and dispose of properties to promote industry and trade development. As a non-profit corporation, the Industrial Development Board can allow companies tax abatements by holding their properties throughout the span of a PILOT agreement. The Economic Development Agency, a department of city government, works on behalf of the city to recruit, retain, and attract new businesses. While the Gallatin Economic Development Agency focuses on broader economic development strategies, the Gallatin Industrial Development Board is ultimately responsible for signing the contracts and holding the properties until the agreements are fulfilled. When deciding whether to grant business incentives, both entities work together to review key aspects of PILOT applications and determine their potential impact on the local economy. Before an application can be approved, a cost-benefit analysis is conducted to ensure that the proposed tax abatement offers value to the community. Key factors such as the number and quality of jobs created, capital investments, and overall community benefits are considered when deciding whether to move forward with the incentive.

The cost-benefit analysis must demonstrate sufficient community value to justify the abatement of taxes and any associated revenue loss.

Gallatin's Approach to PILOT Agreements

Every industrial development corporation is authorized by the municipality that created it, whether it be a city, county, or a combination of both. Since the Gallatin Industrial Development Board was established by the city, the City Council must grant approval for each PILOT agreement that the Industrial Development Board authorizes. Gallatin stands out because, in 2008, the Economic Development Agency proposed a resolution to adopt a tiered PILOT Program featuring four levels of incentives with different qualifiers based on job numbers, investment amounts, and average wage rates. This resolution granted the Industrial Development Board the authority to execute all future PILOT agreements that fell within the parameters of the tiered incentive program, thereby fulfilling the approval requirement for most agreements. It was successfully adopted, simplifying the process and enabling economic development organizations to act decisively in securing investments for Gallatin. For twelve years following the adoption of the tiered PILOT Program, the Industrial Development Board and the Economic Development Agency continued to write PILOT agreements without assessment of existing distribution rules and whether they were successful practices. The Gallatin Industrial Development Board continued the tradition of dividing payments in lieu of tax between the city and county based on the abated ad valorem tax and keeping only a small payment to cover administrative costs. The Gallatin Industrial Development Board and the Economic Development Agency were not fully capitalizing on the opportunities these agreements offered nor were they taking advantage of the resource the payments could be in supporting economic development programs.

The Promise of Facebook and New Political Challenges

In Rosemary Bates' TCED Capstone Project titled "Problems Can Lead to Prosperity with a Strategic Plan: A Collaborative, Targeted Approach to Business Recruitment in Gallatin" from March 2021, she recounts the Gallatin Economic Development Agency's decision to focus on recruiting technology-focused companies to align with the city's broader plan to grow the economic base with new, competitive markets. The agency's strategic plan ultimately led to the pursuit of a data center which landed Project Wool Hawk in 2017 and was later revealed as Facebook. Despite not seeking state incentives, Facebook was motivated in their new location by the city's PILOT program and submitted their application. With the promise of an initial capital investment of over \$800 million and at least one-hundred jobs with wages significantly over the average median income, they were approved for a five-year agreement.

Coincidentally, just as Facebook was considering Gallatin, the COVID-19 pandemic was bringing an influx of new residents to Middle Tennessee, leading to an explosion of growth in the city. The resulting backlash from some community members was marked by resistance to newcomers and opposition to any programs that might make Gallatin attractive to outsiders. This sentiment even began to influence several elected officials, many of whom sat on the Sumner County Commission and the Gallatin City Council. Fortunately, the tiered PILOT Program resolution previously adopted by the city ensured that the approval process for qualifying tax incentives remained unaffected by this so-called "anti-growth coalition." However, the funds to be distributed through PILOT agreements and subsequently managed by this new coalition needed re-examination. Some in charge of the city and county finances were eager to cut funding to governmental departments, schools, and community programs, posing a danger to economic development initiatives. In consideration of the financial constraints that could negatively affect

the future of the community, the Economic Development Agency and the Industrial Development Board chose to take a more proactive approach and amend the language for future PILOT agreements. As a result of this, Facebook’s agreement was different from previous contracts and left more ambiguity concerning the exact distribution of funds. Despite the ambiguity, both organizations agreed that the school’s portion of the county tax should always be paid out and now it would be given directly to the school system to ensure they received the benefit.

Responding to Challenges: Revising PILOT Distribution

This new method of distribution left the Industrial Development Board responsible for deciding how much of the PILOT monies would be paid out to municipal governments and how much they would control. Even without the “anti-growth coalition” in control of government budgets, the allocated monies had never been earmarked for economic development initiatives and were simply added to general fund that paid for day-to-day operations and services. The Industrial Development Board could have continued to distribute funds as before – about 35% to Gallatin and 65% to Sumner County (with 60% of the county’s portion going to schools) – or it could have taken a more proactive approach to supporting economic development initiatives that are vital to the economic health of the community.

In 2023, Facebook began making payments on its PILOT agreement with the completion of its first building. Subsequent buildings will each begin payment upon their individual completion and continue for four years thereafter. When the agreement concludes and Facebook is back on the tax payroll, it will be the largest taxpayer in Sumner County, and the value of the payments-in-lieu-of-tax reflect this significant corporate investment. Currently, the Industrial Development Board holds over a million dollars, and that number will only increase as more

buildings are completed and Facebook fulfills all its yearly payment requirements. As the Industrial Development Board, with assistance from the Economic Development Agency, begins to formulate a strategy on how to use these funds effectively and transparently, several considerations must be addressed, including projects and programs that bridge gaps in infrastructure, business and community programs, and workforce development. Examining how other communities handle in-lieu payment distribution provides valuable insight into the opportunities and challenges these agreements can present.

Comparative Analysis: PILOT Practices in Chattanooga and Clarksville

For several years, the Industrial Development Board for the City of Chattanooga has carefully structured PILOT agreements to ensure that PILOT funds are utilized for economic development purposes. Beginning as far back as 2008 with their Alstom Power PILOT agreement, the Board included language requiring that all funds disbursed to the County and City general funds be used solely for the public purposes of the Industrial Development Board, per the Industrial Development Act. Perhaps having difficulty utilizing money that was no longer under their control, the Board added stipulations on the disbursement of funds in later agreements. In both their 2016 agreement with Yangeng US Automotive Interior Systems and their 2014 agreement with Coca-Cola, the Board included what they called an “economic development payment” based on a percentage of the City taxes that would otherwise have been payable if the company were subject to property taxes.

The economic development payment is given directly to the City of Chattanooga Industrial Development Board and is to be used exclusively for economic development purposes. The Board dedicates a significant portion of these funds to supporting small business incentives. They created a grant program called Growing Small Business which awards small businesses up

to \$10,000 per business per year. Since small businesses often lack the capital investment or job numbers necessary to qualify for traditional PILOT agreements, which are Chattanooga's primary economic development incentive, these grants provide an alternative revenue stream. Much like PILOTs, criteria to qualify includes job numbers and wages. The program has been hugely successful and has awarded dozens of grants since its inception in March 2019.

Additionally, the Chattanooga Industrial Development Board has a long-standing practice of always requiring companies to pay the full portion of what would have been paid to the school system had there been no abatement and always remitting that payment to the schools. Funding is arguably one of the most powerful tools for a strong education system. By making sure that economic growth continues to benefit the school system, they support the pipeline that is vital for maintaining the future workforce.

Not all communities have used PILOT agreements to directly fund economic development. The Clarksville Economic Development Council funds and oversees all the economic development initiatives for Clarksville and Montgomery County. That includes the Chamber of Commerce, Aspire Clarksville Foundation, and Tourism Development. The Clarksville-Montgomery Industrial Development Board serves both the City of Clarksville and Montgomery County and is responsible for managing and executing PILOT agreements within its jurisdiction. Despite the Industrial Development Board's involvement, it neither collects nor distributes payments and receives no direct funding from the agreements. The PILOT program funds are dispersed to the city and county who then decide whether to fund the Clarksville Economic Development Council. This arrangement leaves the entity responsible for business recruitment, expansion, and retention vulnerable to changes in political leadership and economic

development priorities. It also leaves small business programs and marketing programs like those offered by Aspire Foundation and Tourism Development exposed to defunding.

Leveraging PILOT Funds for Economic Development Initiatives

Solving Workforce Challenges

In response to various scenarios, the Gallatin Industrial Development Board, in collaboration with the Gallatin Economic Development Agency, has begun developing a plan for the use of their existing funds, most of which come from Facebook's PILOT agreement. One of the main focuses identified by the economic development organizations is supporting existing industries and their workforce. During his instruction in the TCED Business Retention and Expansion course in March 2023, Laithi Wardi emphasized that business retention is responsible for up to 85% of all jobs and investments in a community and that those programs are significantly more cost-effective than recruitment. Throughout the Gallatin Economic Development Agency's engagements with existing industry partners, several workforce challenges were identified, one of the most pressing being the availability and affordability of childcare. Childcare shortages can lead to lower labor force participation and unreliable employees, which in turn decreases business productivity and can result in downsizing.

Mo Collins, in the TCED Workforce Development Course in August 2022, noted that one of the roles of economic development organizations is to help businesses address barriers to talent attraction and retention. Because childcare shortages were presenting a challenge to local employers, the Gallatin Economic Development Agency applied for and was awarded a grant by the Tennessee Department of Economic and Community Development to construct a new daycare, adding up to 90 new daycare slots in the community. The Industrial Development Board

seized the opportunity to help finance the project, contributing over \$600,000 to the city to cover construction costs. Gallatin Day Care, the non-profit organization managing the new facility, agreed to reserve slots exclusively for industry partners and to provide flexible shifts to meet the needs of manufacturers. The daycare will operate on income-based, sliding scale pricing and will accept state vouchers, providing the most affordable childcare option in Gallatin.

Another workforce development opportunity presented to the Industrial Development Board is the expansion of the mechatronics program at Volunteer State Community College (VSCC). VSCC, which serves an eleven-state region, has its central hub in Gallatin. The Gallatin Economic Development Agency was instrumental in bringing the mechatronics program to the college in 2017 by advocating for the need to provide a robust workforce pipeline for existing and future manufacturers. The program has been so successful over the past seven years that it is now looking to expand its equipment and offer additional certifications. VSCC will rely on grants and potential funding from the Industrial Development Board to make this expansion a reality. Given the importance of workforce development programs like mechatronics to both current manufacturers and prospective companies, allocating PILOT funds to VSCC aligns perfectly with the City's economic development goals and the mission of the Industrial Development Board.

Supporting Small Businesses

Beyond funding for daycare and the mechatronics program, the Gallatin Industrial Development Board can support a wide range of economic development programs designed to stimulate the economy, attract and retain businesses, and enhance overall quality of life. Like Chattanooga, Gallatin is considering a grant or loan program that would provide capital to small businesses and startups. In recent years, Gallatin has successfully recruited several manufacturers

with fewer than ten initial employees that have since expanded rapidly, investing in equipment and adding more positions. According to the International Economic Development Council, small businesses are more innovative, likely to hire locally, and engaged with community events. They provide a diverse range of employment opportunities and give stability to the local economy, all which brings value when considering a community's prosperity.

Land and Infrastructure Development

Industrial land and utility infrastructure is another funding consideration for the Industrial Development Board. The city sold its last parcel in the Industrial Center in 2021, highlighting the need for a new industrial center. Without city-owned or Industrial Development Board-owned land, Gallatin is at the mercy of private owners for site selection for prospective companies.

Brownfield Redevelopment

The Economic Development Agency is also focusing on brownfield redevelopment, a costly endeavor despite state and federal grants. With the opposition to growth in Sumner County, looking at blighted areas for new development seems like a win-win option. Assistance from the Industrial Development Board in financing the remediation of brownfields could bring new viable land for development that has been previously unconsidered.

Ensuring Long-Term Success with PILOT Distributions

Several communities have successfully used PILOT programs to drive economic growth. Taking those programs a step further and focusing on the benefits of strategic PILOT distribution could lead to new programs that align with economic development goals and make an area more attractive to investors. Nevertheless, the impact of PILOT agreements and payment distribution on the local community should be a primary consideration. Ensuring that these distributions and

the programs they support benefit a broad range of stakeholders, including residents, businesses, and local governments, is essential for long-term success. Engaging stakeholders, including education partners, economic development organizations, and government officials, is critical to achieving buy-in and collaboration.

Going forward, it is important to set clear guidelines and criteria for PILOT agreements, including proper disbursement of funds. While it remains important to allocate some funds to the City, County, and School System, it is equally important for economic development organizations, like the Industrial Development Board, to retain control over a portion of the payments to further economic development goals. It is also crucial to monitor and evaluate the mechanisms being used in both PILOT agreements and fund distribution. Analyzing these mechanisms and verifying that they are achieving the intended objectives is part of developing a successful PILOT program. As with any tax-incentive program, challenges are inevitable, but proper mitigation strategies can help overcome hurdles and resistance. Providing transparency in the PILOT distribution process is key to earning trust with stakeholders and the community. Proper reporting, including documenting challenges and tracking successes, is also critical.

Conclusion: Maximizing the Impact of PILOT Programs

The strategic allocation of payments-in-lieu-of-tax has the potential to drive significant economic development. By elevating workforce development, creating small business programs, improving infrastructure, and enhancing community development, the Industrial Development Board can wisely use its funds as a powerful tool to deliver widespread benefits across the community. In the long term, using PILOT funds for these economic development initiatives can only drive more investments into the community, creating a more sustainable PILOT program that benefits everyone.

Resource Page

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