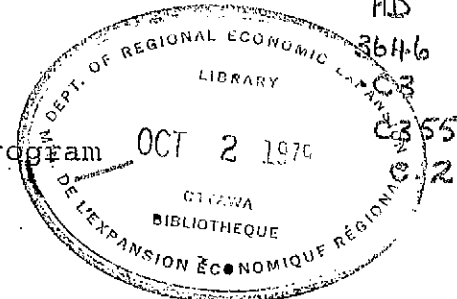


Coordinator's Report
To Directors of Incentives
Regarding the On-going Review of
The Regional Development
Incentives Program

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A. Purpose of Report

The purpose of this report is to summarize the findings of the four working groups which were established by the Directors of Incentives to examine the operation of the incentives program in relation to the pursuit of departmental objectives. For a more complete appreciation of the variety of ideas and views expressed by individual group members, the reports of the four working groups should be read in detail. In reading these reports two particular points should be kept in mind: (a) group members were drawn from different disciplines and different offices and therefore their views do not necessarily reflect the opinions of their own departmental organizations nor are they unanimous in all respects, and (b) the limited time frame for completion of each report was observed by most working groups and precluded examination of proposals in maximum depth.

B. Methodology of the Review

The terms of reference for the four working groups were established by the Directors of Incentives in such a way that, broadly speaking,

- (a) one group (Group A) examined the objectives and goals of a program of incentives to industry for the different regions of Canada,
- (b) two groups (Groups B and C) examined the types of individual incentives or sets of incentives that could be employed to achieve those objectives, with Group B considering the appropriateness of grant and related type incentives while Group C reviewed the value of profitability, cost and re-investment incentives, and
- (c) the fourth group (Group D) examined various mechanisms for enhancing the use of an incentives program by entrepreneurs and other interested parties.

The integration of the activities of the four groups was achieved through formal and informal discussions between members of various groups, through a series of meetings convened by the coordinator with group leaders and, of course, through the endorsement by the group leaders of the combined views expressed in this report.

C. Overview of the Four Reports

Does DREE need an incentives to industry program to help achieve its objectives and, if so, can the present program be improved? The answer to each of these questions is a resounding "yes".

Since its creation seven years ago, DREE has striven to identify and improve the development of economic and social opportunities in the various regions of Canada and to reduce regional imbalances in employment and income levels. It is now clearer than ever that the whole issue of regional disparities is a very complex one that requires the application of a range of policy instruments and the efforts of more than one level of government, as well as the full involvement of the private sector. It is equally clear that an incentives to industry program is a key and essential element of any regional development strategies. The nature or content of a program that can best perform this elemental role is less clear.

It can be argued that, ideally, programs such as RDIA and the various IT&C industrial incentives programs should be elements of a cohesive national industrial policy designed to address simultaneously national, regional and socio-economic concerns. Though commendable as a goal, a national industrial policy that would at the same time be national, regional, and industry oriented in scope, would be very difficult to design and implement. What is feasible, however, is the implementation of a general industrial strategy framework against which specific policies and programs designed to achieve well defined goals

(e.g. change the industrial structure in a given region or provide better quality employment opportunities) could be checked for consistency. DREE has a definite responsibility to contribute to the formulation of such an industrial strategy or strategies for the federal government and to shape its own program or programs of incentives to industry accordingly. Needless to say, provincial views and priorities as well as the anticipated impact of activity under GDAs must also be taken into account in any such consideration.

Irrespective of whether it is for regional development or for industrial development, any governmental strategy designed to achieve specific objectives must recognize and state clearly the essential contribution to be made by the private sector. This contribution can be to policy development or program implementation or both. Previous and current regional development industrial programs have vacillated on the role to be played by the private sector in identifying and developing initiatives that will contribute to the economic growth of disadvantaged regions. In addition the private sector's potential has not been optimally tapped by the presentation of a set of mechanisms and tools which are at once attention-catching and attention-sustaining. DREE must recognize these needs in reshaping the RDIA program.

D. Report of Group A

Group A makes it clear that Canada is in fierce international competition for industry. Experience in Canada and elsewhere suggests that regional development policies must be long term in nature and must be integrated into regional strategies. Insofar as incentives to industry are concerned, in large measure they need to be simply constructed and easily administered, well publicized and relatively free from periodic change in geographic coverage as well as in program provisions and incentives rates.

Toward this end recommendations are advanced for establishing regional needs and priorities, clarifying the objectives and goals of the program as well as the assumptions underlying these objectives and goals, identifying the constraints

under which the program operates, and estimating the costs of effecting changes. Recommendations are also made for short term changes to the program which include modifying the emphasis on new facilities over expansions, encouraging local entrepreneurship over ownership of similar activities by other Canadians and foreigners, and increasing departmental commitment to the program by financial and other means.

E. Reports of Groups B and C

These groups look carefully at the range of incentive tools available to attract industry to designated regions. In keeping with the overview of the total program, they conclude that outright grants continue to represent the major appeal to most private entrepreneurs with repayable grants and loan guarantees being useful tools for more limited and specialized purposes.

Other incentives instruments are considered necessary either to complement the provision of outright grants or to serve as an alternative in selected situations. Group C in particular believes that the profitability incentive would be a very influential means of attracting certain major firms and undertakings to designated regions where they could have a significant economic impact. Group B, on the other hand, is of the view that the attractiveness of such an incentive is lessened by certain administrative and other considerations.

F. Report of Group D

Group D makes a vigorous presentation in favour of what it calls a "market-oriented development activity". The case is strong for a substantially enhanced departmental role in industrial search, industrial development, promotion and related activities. Specific recommendations are advanced for restructuring the development organization in the department to better reflect its proposed new role.

G. Recommendations

The recommendations which follow are a composite of the major recommendations of the four working groups and they have been framed within the context described primarily in section C above.

To summarize that context again, a regional development incentives program (and thus improvements of the RDIA program) is a key tool available to policy makers for realizing regional potentials and reducing regional imbalances, should not be inconsistent with an overall federal industrial strategy, should recognize the validity of the GDA approach in identifying principal regional and provincial needs and priorities, and should recognize the need to involve the private sector in a meaningful way in regional economic policy formulation and in bringing economic opportunities to fruition through appropriate program provisions and other inducements.

- (a) Canada has need of a strong and influential incentives program in order to stay competitive with other countries for industrial investment and should allocate a significant portion of its budget for this purpose.
- (b) DREE should aspire to create an increasing number of jobs of more significance in strengthening regional economies than in the past and, while further study is required to determine a more specific magnitude of costs and jobs, a budget in the order of \$160 million per annum should be provided initially based on 16,000 direct jobs annually at a cost of \$10,000 per job.
- (c) To meet the most generally accepted objectives of the incentives program (see Working Group A report, page 7) incentives should continue to be provided in the form of grants and loan guarantees; outright grants should be the basic inducement available to industry with repayable grants and loan guarantees available to meet particular circumstances; loan and particularly special interest subsidies may be of value in certain situations but they are not regarded as preferred incentives tools.

- (c) To meet certain higher priority objectives, inducements should be made available in the form of profitability, cost and reinvestment incentives; particular attention should be addressed to profitability incentives which have particular value for larger undertakings with significant economic benefit; cost incentives should be available for selective use with a smaller number of major projects. The combining of these incentives with the more conventional grants could be of special value.
- (d) Priorities should be better established between and within regions for purposes of program coverage (i.e. designation) and budget allocation. These priorities should be based on both the need and opportunity to grow (established with reference to unemployment rates, levels of income, real participation or attained levels of economic diversification, geographic location, linkages and available infrastructure).
- (e) Priorities should be set for encouraging new industrial development in the various regions and sub-regions of Canada, since different levels of industrial activity carry with them different types and levels of economic impact.
- (f) The objectives and goals of the program, as well as the underlying criteria or premises on which the objectives and goals are based, should be made widely known in order to ensure public awareness and understanding of the program's role within the federal government's industrial and regional development strategies. Particular attention should be addressed to widely held misconceptions about the program.
- (g) DREE should undertake an aggressive and selective marketing program designed to induce industries to locate, expand and modernize their operations in the designated regions.
- (h) This program should consist of four main elements:
- industrial research and analysis whose purpose would be to identify for entrepreneurs opportunities for development in designated regions

- advertising and promotion of the program on both a general and selective basis
- industrial search and related activities such as information-gathering, the purpose of which would be to identify, locate, contact and attract desirable industrial prospects to designated regions
- coordination with related departmental activities such as regional industrial development and the identification and development of major economic opportunities.

(i) The development organizations within the Department should be restructured along more functional lines in order to undertake, in conjunction with their present initiatives, the formulation and implementation of the new incentives marketing program.

(j) Many specific improvements should be made to the present program, including the following:

- local entrepreneurs should be favoured over other Canadian or foreign entrepreneurs on similar activities;
- the statutory dollar limitations which have applied to grant levels since 1969 should be increased;
- project analysis should recognize more fully provincial priorities as well as other elements of industrial development strategy such as industrial selectivity, available infrastructure, and manpower training and mobility;
- areas of discretionary authority should be increased or strengthened for better and quicker decision making on such matters as an applicant's need for an incentive;
- the negative impact of the loss of capital cost allowances on grant payments should be removed in order to make the grant more effective and to provide the public with truer costing.

H. Conclusion

This review of the on-going operation of the regional development incentives program has served to clarify many of its strengths and weaknesses. It has also brought forward many ideas as to how the program, as a key instrument of departmental policy for realizing regional potentials and reducing regional imbalances, can be improved. It is hoped that, following the distillation of the ideas and views summarized in this report and expressed in detail in the reports of the four working groups, immediate steps will be taken to effect desirable changes because, while many changes can be made promptly, others will require a lead time of up to two years to become effective. As an aid to consideration, the attached Appendix has been prepared to categorize the major recommendations emerging from the review into suggested time frames for implementation.

APPENDIX

On-going Review of the
Regional Development Incentives Program

NOTE: Following each recommendation below there is a reference, shown in brackets, to the source and a fuller explanation of that recommendation. For example, (A7) means page 7 of the report for working group A, and (CB11) means page B11 of the report for working group C.

- A. Recommendations for immediate implementation, requiring no amendment to the Act or Regulations
1. The Department should reinforce and publicize, to the maximum extent possible,
 - (a) the objectives and various goals established for the program (A7 to 10);
 - (b) the assumptions underlying those objectives and goals (A33 to 38);
 - (c) the limits and constraints imposed on the achievement of the stated objectives and goals (A39).
 2. Reinforcement and emphasis should be given to the following desirable features of the present program:
 - (a) non-repayable incentives must remain the mainstay of the program (B2);
 - (b) grants should continue to be based on a combination of capital cost and employment elements (B2);
 - (c) except for Eastern Quebec and certain deserving cases, standard formula incentive rates for new facilities and new product expansions should remain unchanged for the time being (B2 B3).
 3. A number of administrative improvements should be made, including a simplification of initial inspection procedures in order to expedite payment to the entrepreneur (B3), and classifying the replacement of an existing facility as a modernization/expansion rather than a new facility (B4).
 4. With a view toward possible future program modification, study should be undertaken of the value as an incentive of such tools as (a) an investment reserve system, (b) the provision of venture capital and (c) equity participation (CB11 to CB12).

B. Recommendations for early implementation, requiring more significant policy changes but no amendment to the Act or Regulations

1. Regions and sub-regions should be ranked in terms of priority and designated accordingly for program eligibility and incentive support (A16 to 23).
2. Industries (including service industries) to be encouraged to each region should be identified and relative priorities established (A24 to 29).
3. A range of incentive tools should be made available to meet the different needs of various regions and sub-regions (A31, A46, CA3).
4. Cost-benefit analysis should be employed to determine the appropriate allocation of funds to the program, and thus the number of jobs to be created (it being estimated that the average cost per job will range from a minimum of \$7,500 to in excess of \$10,000 depending upon whether the program continues responsive or becomes more directed) (A74).
5. An aggressive and selective marketing program should be undertaken (D5).
6. The Department's development organization should be re-structured along functional lines in order to undertake, in conjunction with its present initiatives, marketing oriented activities in the following areas:
 - (a) industrial research and analysis (e.g. sector analysis, product studies),
 - (b) advertising and promotion of the program (e.g. client contacts, community participation),
 - (c) industrial search and related activities (e.g. prospect searches, aftercare services),

B.2.

(d) a coordination of departmental development activities carried out in Ottawa, regional and provincial offices (D5).

7. DREE's marketing efforts should be coordinated with other federal departments and provincial and community governments, using its decentralized mode to the fullest advantage (D6).

C. Recommendations for implementation within one or two years depending upon whether amendments to the Regulations, the RDIA, or other Acts are involved

1. The Regulations should be amended for the following specific purposes:
 - (a) to include certain presently ineligible costs (A45).
 - (b) to relate the minimum size of a project involving an expansion or modernization to the size of the existing facility rather than to a fixed minimum amount (B3).
 - (c) to include commercial air services and other transportation and communication facilities as commercial facilities for loan guarantee eligibility (B4).
2. The Act should be amended for the following specific purposes:
 - (a) to give more discretion as to when an incentive is needed to achieve program objectives and goals (A47),
 - (b) to eliminate certain technical and other deterrents to providing incentives in desirable cases (A48),
 - (c) to include selected industries as eligible operations (A49, CA1, CI2),
 - (d) to permit payment for advisory services and the infusion of additional funds in exceptional cases (A50),
 - (e) to increase the dollar limitations applied to grant payments since 1969, e.g. \$30,000 per job to \$50,000 per job (B3),
 - (f) to increase the maximum rate of incentive possible by 5% to 10% to 25% or 30% ACC for expansion and modernization projects (B2),
 - (g) to make loan guarantee assistance available if required after commercial production begins (B4),
 - (h) to base the amount of loan to be guaranteed on total capital employed rather than total capital costs (B4),
 - (i) to make expansions and modernizations of commercial facilities in excess of 25% of the cost of the facility eligible for loan guarantees (B4).

C.2.

3. Authority should be sought for the following purposes:
 - (a) to permit the use of profitability, cost and re-investment incentives in appropriate circumstances (e.g. new industry to an area, multiphase projects, experimental activities) (Cx)
 - (b) to indicate the long term nature of regional development planning and therefore to provide incentives tools for a minimum period of 10 years (CA1),
 - (c) to provide a significantly higher order of incentive for particularly meritorious cases (e.g. to change or reinforce industrial structures, to induce higher risk but highly desirable undertakings) (CA4),
 - (d) to remove the negative impact on the value of incentive grants of lost capital cost allowances (B3)
4. Of the various types of profitability incentives available, a grant calculated as a percentage of profits should be adopted in preference to other forms of incentives such as (a) tax credits, (b) regional income and sales tax rates, (c) tax holidays, and (d) tax allowances (CB2 to CB7).
5. Criteria should be established for and in connection with the use of cost oriented incentives; in particular the selection of costs to be eligible for incentives support be limited and precise (CB8 to CB10).

