THE INCENTIVES PROGRAM

Canada

DEPARTMENT OF REGIONAL ECONOMIC EXPANSION

OTTAWA, APRIL, 1972

INTRODUCTION

The Department of Regional Economic Expansion was created in April 1969 in order to bring together and strengthen the federal effort to reduce regional economic disparities. In broad terms, the objective of the Department is to bring the level of economic opportunity in slow-growth regions as close as possible to that existing in the rest of the country. The general objective has been translated into three specific aims: to reduce inter-regional gaps in unemployment rates; to improve labour force participation rates in the slow-growth regions; and to narrow income differentials between regions.

In pursuing these aims, the Department is using a number of programs designed to stimulate industrial development and other forms of economic activity, both urban and rural, and to facilitate much-needed and complementary forms of social adjustment.

The purpose of this paper is to describe briefly the program of industrial incentives, which represents the principal direct means of encouraging industrial development in slow-growth regions.

PRINCIPAL FEATURES

General

Under the program of industrial incentives, grants are available to companies willing to locate, expand or modernize manufacturing facilities in broad regions and special areas designated by the Governor in Council following consultation with the provincial governments. Loan guarantees are also available for such projects and, in defined circumstances, for certain types of commercial projects.

The currently designated regions cover broad segments of the country. The special areas, of which there are now 23, represent more limited focal points of potential development. Generally speaking, they are eligible, not only for industrial incentives, but also for various forms of infrastructure assistance authorized under federal-provincial agreements. A map of Canada showing the designated regions and special areas is attached as Appendix A.

Statutory authority for the program, as it applies in the designated regions of the country, stems from the Regional Development Incentives Act (RDIA), which came into force on August 7, 1969. In the special areas, it stems from the Department of Regional Economic Expansion Act, which in 1970 superseded the Government Organization Act of 1969.

A fair amount of residual activity under the program still derives from the Area Development Incentives Act (ADIA), which was replaced by the Regional Development Incentives Act. Applications were accepted under ADIA until December 31, 1969, on the understanding that assisted projects would be in commercial production by March 31, 1971. Because of the time-lag between the start of commercial production and final payment on approved grants, some activity under ADIA is likely to continue until 1974.

INCENTIVE TYPES AND LEVELS

There are two types of RDIA incentives: grants and loan guarantees. Either or both may be offered, in defined circumstances, to assist projects that are shown, on the basis of individual analyses, to meet reasonable standards of viability and net economic benefit.

The size of an incentive grant may be varied, within statutory limits, to meet the requirements of a particular project. In the case of a new plant or the expansion of an existing plant into new product lines, it is based on approved capital costs and (if considered appropriate) the number of jobs to be created. In the case of a plant modernization or an expansion that does not involve a new product, only approved capital costs can be considered.

The maximum available grant depends on location and the type of project, as is shown in the following table:

Location	*Type of Project*	
	Modernization or Ordinary Expansion	*New Plant or New Product Expansion*
Region A (Atlantic Provinces)	30% of capital cost	35% of capital cost plus $7,000 per direct job created
Region B (Standard Designated Regions)	20% of capital cost	25% of capital cost plus $5,000 per direct job created
Region C (Special Designated Region - S.W. Quebec & S.E. Ontario)	10% of capital cost	10% of capital cost plus $2,000 per direct job created

Overriding maxima are also prescribed. These, depending on location and type of project, are $30,000 per direct job created or one-half of the capital to be employed in the project.

Loan guarantees, which are intended to offset difficulties that investors frequently encounter in obtaining loan funds for investment in slow-growth regions, may not exceed 90 per cent of the total advances made by a lender plus the interest involved or 80 per cent of the total capital costs.

Eligibility Conditions

To be eligible for an RDIA incentive grant, a project must involve manufacturing or processing and be located in a designated region or special area. Only loan guarantees are available to commercial facilities - and these must be new rather than expanded or modernized facilities.

In addition to these basic requirements, a project must be of a certain minimum size in order to qualify either for a grant or a loan guarantee. In the case of a modernization or ordinary expansion, approved capital costs must total at least $30,000. In the case of a new plant or an expansion into new product lines, approved capital costs must normally total $60,000 or more. In order to qualify for a loan guarantee, a commercial facility must involve capital costs in excess of $2,500,000 if the intended location is Metropolitan Montreal, $500,000 if it is Quebec City or Winnipeg, and $250,000 if it is elsewhere.

Before a project can be considered eligible, the applicant must be willing to provide a specific amount of equity capital. In the case of a new plant, this cannot be less than 20 per cent of approved capital costs. In the case of an expansion or modernization, it cannot be less than 20 per cent of approved capital costs and the book value of the assets of the existing facility at the time of the application. The minimum equity of the borrower must also be 20 per cent in the case of a loan guarantee for commercial facilities.

The conditions described must be met before incentive assistance in the form of a grant or loan guarantee is provided. The fact that they have been met does not of course guarantee that assistance will be provided. The Department must, in addition, be satisfied that the project will make a significant contribution to economic development and social adjustment in the designated region or special area where it is to be located. It must also be satisfied that the project is unlikely to go forward in the intended location without assistance.

ADMINISTRATION

Responsibility for the program rests of course with the Minister. He is advised by a board which is chaired by the Deputy Minister and which includes in its membership senior officials from several government departments and a number of knowledgeable individuals from the business community and labour movement.

Day-to-day administrative responsibility is carried by the Incentives Division of the Department, which reports through an Assistant Deputy Minister to the Deputy Minister. In March 1972, the Division employed about 250 people, of whom about 150 were financial analysts, chartered accountants and other professional personnel.

The Division is engaged in various types of work, almost all of which can be classified under three main headings: promotion; evaluation; and inspection and payment.

Promotion

Incentive grants and loan guarantees are offered only to assist proposed projects that are the subject of specific applications. In this sense, the program is responsive to applications. But a good deal of effort is expended in making the program known to potential investors and in helping communities in the slow-growth areas to identify and exploit their potential for industrial development.

Promotional activity takes a variety of forms, including general advertising, direct mailing campaigns, speaking engagements, the provision of descriptive literature and visual aids, prospecting missions to selected centres in Canada and abroad, and participation in industrial opportunity studies. Up to March 1972, this activity had generated over 10,000 inquiries.

Activity designed to stimulate community participation in industrial development is also important. Up to March 1972, assistance in this field had been provided on an individual basis to 120 communities; 35 seminars on the role of the community in industrial development had been conducted; and 14 industrial development courses, each lasting three days, had been completed in co-operation with provincial and municipal authorities.

Evaluation

As might be expected, most of the resources of the Incentives Division are devoted to the evaluation of applications for incentive assistance.

Each application is assigned to an officer who, in normal circumstances, stays with the case until the work of evaluation is completed. His task is to ensure that the necessary information is obtained and carefully analysed, that there is liaison with other government departments concerned and that an appropriate recommendation is made. His analysis and recommendation are subjected to at least two levels of review before a decision is made.

Information used in the evaluation process is obtained from the applicant and from a variety of government and business sources. It relates to a number of factors, including:

- capital costs;
- jobs to be created (in each of the three years after commercial production is achieved);
- profitability;
- sources and methods of financing;
- sources and availability of machinery, equipment and raw materials;
- character and size of markets;
- quality of management;
- possible environmental effects.

Analysis of the relevant information is designed to determine whether the proposed project is eligible, whether it stands a good chance of achieving long-term viability, what net economic and social benefits it is apt to offer to the area concerned and the country as a whole and whether it requires assistance in order to proceed. If the evaluation to this point is positive, attention then turns to the appropriate form and level of assistance that should be offered. Judgments on this subject must take into account a number of considerations, including a comparison between the prospective rate of return on investment in the proposed location and in other possible locations.

Evaluation decisions result in letters of rejection or letters of offer. Letters containing offers of incentive assistance always set forth a number of conditions based on provisions in the governing statute or regulations. They may also set forth one or more special conditions resulting from the evaluation that has been made. Where special conditions are included, they are normally designed to provide additional assurance of viability or to enhance the expected net economic and social benefit.

Inspection and Payment

An offer made lapses unless accepted within 90 days. If it is accepted, the case concerned moves into the inspection stage (unless it involves only a loan guarantee).

The process of inspection is the basis for approving payment of an incentive grant. It is designed to ensure that a given project in fact meets the requirements of the law and regulations and the conditions of the relevant offer of assistance.

Once assigned to a case, an inspecting officer keeps in close touch with the company concerned, following the progress of the project and accumulating required information, including a properly completed schedule of anticipated capital costs. When the project in question is legally in commercial production - i.e., when at least half of the assets on which the offer was based have been in continuous operation for at least 30 days - he makes a thorough on-site inspection. As a minimum, he examines: general ledger accounts, fixed asset control accounts, payment procedures, labour and wage records, accounts receivable and payable, invoices, details of any costs that have not been incurred on an arm's length basis, and the location and operating condition of physical assets. In addition, he examines the equity status of the company, its insurance coverage and credit position, and its marketing and sales policies.

When his inspection is completed, the officer makes a report setting forth his findings and a recommendation concerning the appropriate amount of the first payment, which may be less but never more than 80 per cent of the incentive offered. This analysis and recommendation are also subjected to two levels of review before any disbursement is made.

Final payment, which requires at least one more thorough on-site inspection, must be made within a specified maximum period after the date on which commercial production is achieved: 30 months in the case of a grant based on capital costs only; 42 months in the case of a grant based on both capital costs and jobs to be created.

During the period between first and final payment, the inspecting officer makes every effort to monitor the progress of the project, to ensure that the requirements of the law and the governing offer are being met. He also stands ready to assist the company concerned with such advice as may be needed to ensure success of the project.

There is provision for recovery of payments in defined circumstances.

RESULTS

It is too early to assess the results of the incentives program in its present form - if only because some projects associated with early offers made under the RDIA legislation have only recently achieved commercial production and some have yet to do so.

A number of things can be said, however.

The first application for an incentive grant under RDIA was received on August 12, 1969. Between that date and March 31, 1972, some 4,982 applications were received under RDIA and the related special areas legislation.

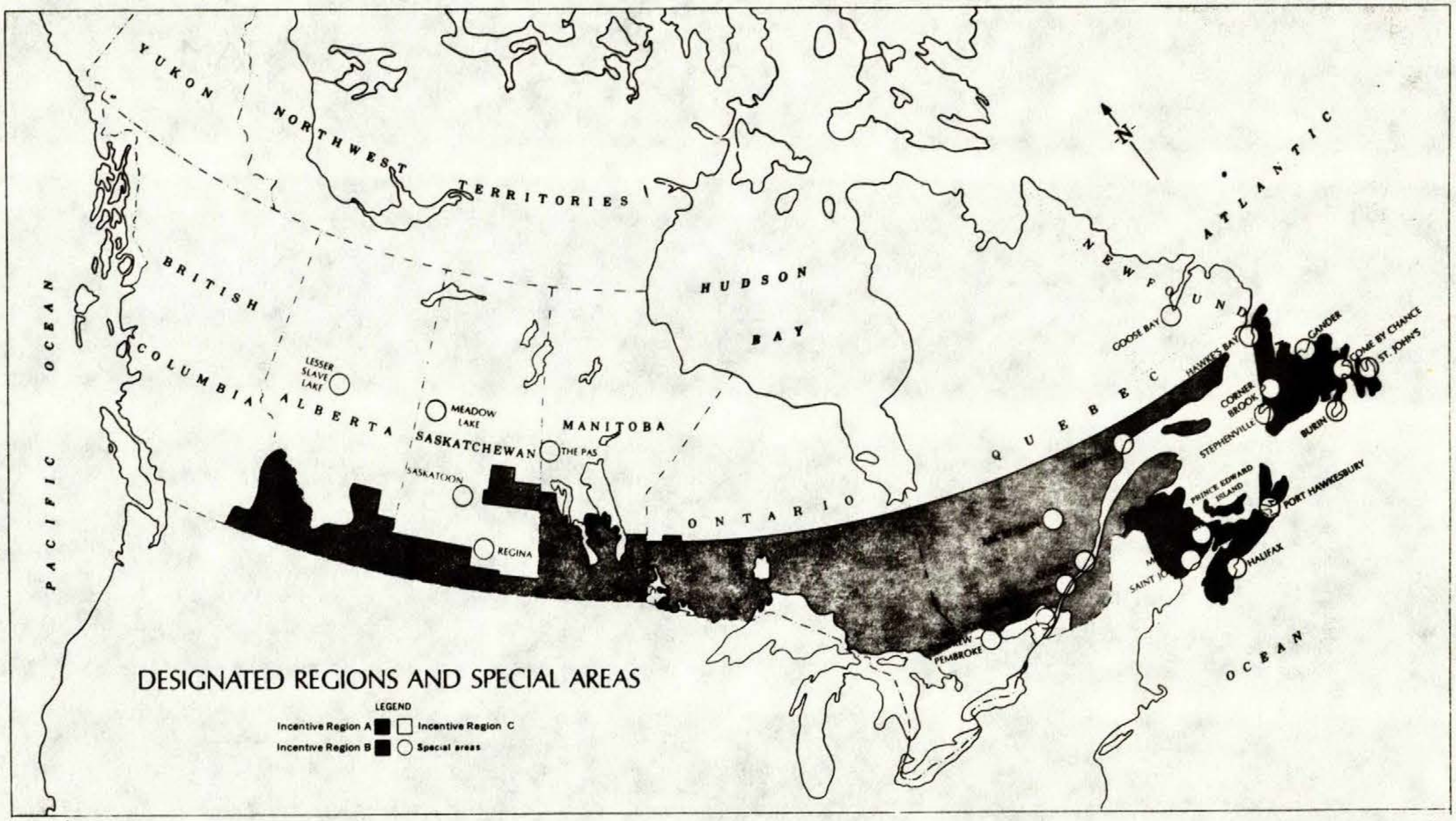
On March 31, 1972, the total number of net accepted offers was 1,334. These offers were associated with projects involving total approved capital costs of about $1,158 million and anticipated direct employment of about 56,000. Incentive commitments totalled $233.3 million, approximately $4,160 per direct job to be created. A provincial breakdown of data relating to the total of net accepted offers is attached as Appendix B.

Experience with the loan guarantee element of the program is quite limited, because it took effect (as a result of an amendment to the legislation) well after the basic program was under way. As of March 31, 1972, only seven offers of loan guarantees had been accepted.

It is worth noting that the number of direct jobs anticipated as a result of accepted offers of incentive grants makes no allowance for employment to be saved or created by incentive assistance offered for modernization or expansion of facilities where no new product is involved (although this type of assistance is included in the figures shown for incentive commitments). It makes no allowance either for off-site jobs directly related to assisted projects, or for the indirect or "multiplier" effects on employment of the investments concerned (although economists are generally agreed that these effects are significant).

There has been some public interest in the relationship between employment anticipated at the time when incentive assistance is offered and employment actually realized at the later time when assisted projects have had a chance to get off the ground. In this connection, the results of a recent survey of new facilities assisted under the old ADIA program are encouraging. They indicate that, although some projects exceeded and others fell short of expectations, the difference between total anticipated employment and total actual employment was less than two per cent. There is reason to believe, then, that the current figures on jobs to be created should prove to be reliable.

In any event, there is no doubt that assistance provided under the incentive program is helping the slow-growth regions of the country to realize their potential for industrial development and, in doing so, is providing Canadians in these regions with employment opportunities that would otherwise not exist.



DESIGNATED REGIONS AND SPECIAL AREAS

Appendix B

DISTRIBUTION BY PROVINCE OF NET ACCEPTED OFFERS OF INCENTIVE GRANTS
UNDER THE REGIONAL DEVELOPMENT INCENTIVES ACT FROM ITS INCEPTION
UNTIL MARCH 31, 1972

	Net Accepted Offers[1]	*Amount of Offered Incentives*	*Total Approved Capital Costs*[2]	*Anticipated Employment Involved*	
		$ (000's)	$ (000's)		
		~~$770,200~~	~~840,136~~		
Newfoundland	48	7,137	18,584 202,838	1,926	
Nova Scotia	85	27,014	128,325 202,838	3,377	
Prince Edward Island	27	2,130 56,606	5,951	660	
New Brunswick	101	20,325	49,978	4,236	
Quebec	744 261	113,594	637,318	32,862	10,199
Ontario	81	22,030	118,101	4,098	
Manitoba	141	12,249	43,551	4,485	
Saskatchewan	39	5,537	21,940	1,410	
Alberta	40	19,849	119,426	2,032	
British Columbia	28	3,436	14,838	990	
TOTAL	1,334	233,301	1,158,012	56,076	

1 Net Accepted Offers: the total of offers made and accepted less those subsequently declined or withdrawn.

2 Total Approved Capital Costs: the capital costs for buildings, machinery and equipment eligible under the program.

Total Eastern Region 261 $56,606 $202,838 10,199