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Sharon Cantillon / Buffalo News

Sweet deals lure major data centers

Power cost discounts, big tax breaks offered

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Politicians and economic development officials have given hundreds of companies millions of dollars in subsidies over the years, but those incentives are chump change compared with what's being offered in an effort to lure data centers to the region.

Yahoo opened a data center in Lockport in August that involves some \$200 million in tax breaks -- including no property tax payments for 10 years -- plus \$58 million in electricity discounts from the state Power Authority and a \$10 million federal stimulus grant.

All that to create 125 jobs, which works out to \$2.1 million per job.

A package to attract Verizon to what is now a soybean field in the Town of Somerset in Niagara County is even richer.

Sales and property tax rebates would come to a projected \$518 million and discounted power would save Verizon an estimated \$96 million over 15 years.

The price tag is \$3.1 million for each of the 200 jobs involved.

The offers to Yahoo and Verizon are "a very generous and compelling package -- without a doubt," said Jack Boyd, president of a site selection company based in New Jersey.

And also "a colossal misuse of resources," said Allison Duwe, executive director of the Coalition for Economic Justice, a nonprofit research and advocacy organization.

"Any rational person should question if this is the right way to do economic development and bring about a shared recovery," she said.

Proponents of these deals maintain that big subsidies reflect the huge capital investment. Verizon, for example, would spend \$500 million on a facility and more than \$3.4 billion over 10 years on computer servers and other equipment.

Advocates also note that the data centers pay well, with salaries upward of \$85,000, and that they're a good way to parlay some of the region's natural assets, starting with climate and hydropower.

Economic development officials regard data centers as a way to help change the region's economic image now associated with smokestacks and as an opportunity to gain a toehold in the high-tech economy.

"We're targeting data centers because they provide a big investment and good-paying jobs, and it helps to change the region's image with site selectors," said Thomas Kucharski, president of Buffalo Niagara Enterprise, the region's business marketing arm.

Data centers are not regarded as significant economic engines, however.

Models that economic planners use to project the spin-off impacts of different types of business development put data centers at the lower end of the spectrum. One data center job spins off about two other jobs, while the typical call center or back-office operation generates three to four jobs and a manufacturing plant, four to six.

"It's just electricity in and electrons out, there's no warehouses, no trucking, no parts, and therefore limited ripple effects," said Greg LeRoy, a national expert on economic development subsidy programs and executive director of Good Jobs First.

While the Yahoo and Verizon deals would result in \$120 million in added property tax revenues over the next 20 years for Niagara County and several towns and school boards, they amount to the two companies paying only about 15 cents on the dollar in their property and sales taxes.

George Palumbo, an economics professor at Canisius College, said he doesn't like the use of tax breaks and other incentives, but "we're stuck with them until we have a more rational policy."

"If you abate taxes on improvements that you had no chance of getting without the abatements, what have you lost?" he said.

Competition growing

Data centers are the factories of the digital age, albeit much less labor-intensive.

They're essentially buildings that house computer servers that process everything from Google searches and Facebook status updates to electronic bank transactions and medical retrieval records.

While much of the economy has stalled the past few years, the demand for digital services has grown.

"It's probably the fastest-growing sector in the high-tech field," said Boyd, president of the Boyd Company, whose clients include Fortune 500 companies.

Data giants like Microsoft, Google and Yahoo once built their server farms largely without government assistance. But in recent years, they've taken followed other corporations and pitted economic development officials against each other to extract subsidies in exchange for locating their operations in communities.

"There's a second war between the states for these data centers," Boyd said. "Companies want it all, they want everything. They want low-cost power, they want tax incentives."

Government officials are obliging.

With the economy in the doldrums, they're eager to cut whatever deals they can, and data centers carry with them a high-tech cachet. Boyd refers to them as "trophy data centers."

Economic development officials in Western New York were not in the hunt until the Yahoo deal came along. Since then, Buffalo Niagara Enterprise has added data centers to its list of targeted industries.

The region is a good fit in many ways, starting with cheap hydropower generated by the New York State Power Authority in Lewiston. About one-third of the power plant's generating capacity is earmarked for industry in the region, and about 20 percent of that power has gone begging for customers.

Data centers are energy hogs, accounting for more than 50 percent of operating costs. Cheap power is therefore essential, and electricity from renewal sources such as hydro is especially coveted.

"Power costs tend to dominate the equation," Boyd said.

Yahoo and Verizon have secured deals for power that costs 1.7 cents a kilowatt at the wholesale rate, less than half that of current market rates and one-third of average power rates over the past five years.

"Anything under 2 cents per kilowatt is extraordinary," Boyd said. "That's your trump card."

The region's advantages don't end there.

Servers generate a lot of heat and require a lot of energy to cool them. Our cold winters and moderate summers provide a good climate. The proximity to the cooling waters of the Great Lakes is another selling point.

Another plus: no hurricanes. And the region is far from major fault lines, so earthquakes are not a major concern.

Finally, data centers are usually located in remote, secure locations, and the region has plenty of wide open spaces close to population centers.

With these assets in hand, local officials have gone out to make deals.

Yahoo deal

The Yahoo deal is typical of what's being struck with growing frequency across the nation, exempting the company from paying sales tax on construction materials and equipment purchases for 20 years. The latter is of particular importance because the computer servers are typically replaced every three to five years and the data centers have an expected lifespan of up to 20 years.

A typical deal struck with a regional economic development agency limits sales tax exemptions to the construction and original equipping of the facility. The 20-year waiver granted Yahoo, not unlike what the state provides for the purchase of equipment for traditional manufacturers, will save the company a projected \$181.3 million.

The agreement with the Lockport Industrial Development Agency also waives property tax payments for 10 years, then gradually increases them over the following eight years. That will save Yahoo an estimated \$19.2 million.

The property tax exemption is unusual in two ways.

A typical IDA deal provides tax breaks for less than 20 years. The standard in neighboring Erie County is seven to 10 years. Moreover, companies are typically expected to start paying a portion of their property taxes from the get-go.

Yahoo also received an allocation of 15 megawatts of low-cost hydropower from the New York Power Authority. The discounted power is projected to save the company \$57.7 million over 15 years, according to a Buffalo News calculation.

Uncle Sam sweetened the pot with a \$10 million grant to help the facility's energy efficiency.

The Yahoo deal dwarfed previous packages awarded to expanding or relocating companies. The costliest deal here previously was given to insurance giant GEICO to locate a regional service center to Amherst about three years ago. Tax breaks, power discounts and other incentives totaled about \$110 million, or an average of about \$92,000 for each of the 1,200 jobs the company promised to deliver.

For as rich as the Yahoo deal was, the deal being crafted for Verizon is more lavish.

Dollars for data centers

Comparing costs of the just-opened Yahoo data center and the pending offer to Verizon

| | Yahoo | Verizon |
|------------------------------|---------------------------------|----------------------------------|
| Location | Lockport | Somerset |
| Size | 190,000 square feet on 30 acres | 500,000 square feet on 150 acres |
| Permanent jobs | 125 | 200 |
| Average annual salary | \$60,000 to \$80,000 | \$85,000 |
| Sales tax savings | \$181 million | \$330 million |
| Property tax savings | \$19 million | \$188 million |
| Hydropower savings | \$58 million | \$96 million |
| Grants | \$10 million | None |
| Total savings | \$268 million | \$614 million |
| Cost per job | \$2.1 million | \$3.1 million |

Note: Sales and property tax savings over 20 years; power savings over 15 years

Verizon deal

The tax breaks and other incentives offered to Verizon are bigger in large part because the company is proposing a data center that is 2 1/2 times larger than what Yahoo constructed. Verizon's data center will cost twice as much -- \$500 million -- and the expense of buying and replacing servers over the years is also significantly higher.

Like Yahoo, Verizon would pay no sales tax for 20 years for the cost of building and equipping the center. That would save the company \$330 million, according to documents it has submitted to the Niagara County IDA, which is negotiating the deal.

Verizon also would pay reduced property taxes over 20 years -- only 15 percent of the bill initially, incrementally scaling up to 45 percent the final 10 years. The savings: \$188 million, according to IDA calculations.

An allocation of 25 megawatts of low-cost hydropower would save the company an estimated \$96.1 million over 15 years.

The deal has not been finalized. State officials wouldn't comment when asked if they were contemplating additional incentives, and the Niagara County IDA has yet to vote on the sales and property tax abatement package. A vote could come as soon as Wednesday.

Local officials believe they have the inside track to obtain the center, although other states, which Verizon won't name, are reportedly in the running.

IDA Chairman Henry Sloma said landing Verizon would be a "huge, huge win for Western New York."

Christina Orsi, regional director of Empire State Development Corp., maintains that data centers represent a good economic development strategy for the region, despite the high cost per job.

"You can't use that as your sole measure," she said. "You have to look at the magnitude of the capital investment, the opportunity for local partnerships, the wages these jobs pay and the image-changing effects that these very high-profile, high-tech opportunities bring," she said.

Nevertheless, there are serious questions about just how much of an economic boost data centers can provide and whether local officials are overpaying to secure them.

Tax breaks debated

E.J. McMahon, executive director of the Empire Center for New York State Policy, has long argued for lower taxes. But he said the property tax breaks afforded Yahoo and Verizon concern him.

"Twenty years is a long time to not pay full property taxes," he said. "That's a long time for a very profitable business in a very profitable industry to not be paying on a tax that's a big burden on a lot of other businesses."

Sloma, of the Niagara IDA, isn't troubled. He said the abatements are the price to be paid to secure Verizon. Even with the abatements, Verizon will pay \$110 million in property taxes over 20 years, he said.

"I'm competing against another community. If Verizon goes there, this community gets nothing, no jobs, no tax revenue," he said.

Officials in the state of Washington, which has been at the forefront of attracting data centers, view the matter differently. They abate sales taxes, but not property taxes.

"If there's no benefit to the community in terms of tax revenue, why have them? Because they are not high jobs creators, we know that," said Patric cq Connelly, a commissioner of the Port of Quincy economic development zone, located in the middle of the state.

The port is home to three data centers, two of which are planning expansions, and another center is in the planning stages. All the data centers pay full property taxes, he said, which has lowered the bill for residents. Over the past five years, the property tax rate has dropped from \$14 per \$1,000 of assessed value to \$11, Connelly said.

John Foster, a member of the Power Authority's governing board, questions the allocation of discounted hydropower to Verizon.

"There wasn't necessarily enough jobs or investment by Verizon to provide them the power requested," Foster said.

Verizon has committed to creating eight jobs per megawatt of power allocated. Yahoo is providing 8.3 jobs per megawatt.

That compares with 29 jobs per megawatt for about 60 other companies that have received power allocations since 2006, according to data maintained by The News.

Authority officials said other factors, including the high-tech nature of data centers and the high salaries they pay, were factors in awarding the allocations to Verizon and Yahoo.

Limited spin-off

Ultimately, economic development efforts are supposed to pay off in new jobs, but data centers are lean operations, requiring relatively small work forces.

What's more, the location and nature of their operations -- generally situated in outlying areas, requiring few locally provided goods and services -- means they have less of a ripple effect than many other businesses.

Models used by economic planners suggest twice as many jobs can be created with a call center like GEICO or a food-processing plant like Steuben Foods than with a data center. A chemical plant like Dupont can trigger three times the employment elsewhere in the community of a data center, according to the models.

Nevertheless, Orsi, of the state, and Kucharski, of BNE, see the potential for spin-off benefits.

To them, the first step is getting in the game by landing a few data centers. If, for example, Yahoo likes the region, perhaps it could be sold on locating some back-office operations here or purchasing locally produced computer components used in servers.

"We're trying to get the manufacturing here, also," Kucharski said.

Dave Kinyon, Lockport's economic development coordinator, said no firms have set up shop nearby because of the presence of Yahoo, although the facility just opened over the summer. He regards the construction of additional data centers in the region as a prerequisite for significant spin off.

That kind of concentration has yet to reap rewards in the Port of Quincy, however.

"One of our hopes was that a lot of high-tech would follow the data centers," said Connelly, the commissioner, "but we haven't had people knocking on our doors to build businesses here because they're here."

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