House Bill 3173 – Long-Term Rural Enterprise Zone Facility Tax Credit

Joint Committee on Tax Credits (JTAX), 76th Oregon Legislative Assembly

The Honorable Ginny Burdick, Co-Chair
The Honorable Jules Bailey, Co-Chair
The Honorable Vicki Berger, Co-Chair

April 28, 2011

business oregon
755 Summer Street NE, Suite 200
Salem OR 97301
503.986.2005
www.oregon4biz.com

MEASURE: HB 3173
EXHIBIT: 6
Joint Committee on Tax Credits 76th Session
DATE: 04-28-2011 PAGES: 10
SUBMITTED BY: Paul Grove

What is the public policy purpose of this credit?

- The Legislature established the Long-term Rural Enterprise Zone Facility Tax Credit to offer an inducement to create jobs aimed at major development opportunities in rural enterprise zones, where the county meets chronic economic criteria.
- It contributes to the creation of employment and economic activity in rural parts the state, many of which continue to lag behind metropolitan areas and face fewer opportunities for major, new private investment.
- It operates in conjunction with the long-term property tax exemption of 7 to15 years (distinct from the standard, commonly used 3–5-year exemption).
- The local zone sponsor in 42 out of 47 rurally designated zones, as shown in the attached map (▲), can currently offer these long-term enterprise zone incentives.
- This tax credit enhances the marketing of rural Oregon communities to private investors.

Is there an expected timeline for achieving this goal?

The timeline for achieving the above-mentioned policy goal remains ongoing.

Is economic development and job creation a primary goal of this credit? — Yes

a. Number of jobs associated with credit on an annual basis:

- At present, there are 360–400 jobs directly associated with the long-term rural enterprise zone program among five currently exempt facilities, with more than 100 jobs anticipated at future projects.
- These projects have arisen mostly over the past five years, so that lately, at least 50 such jobs are being created each year.

b. Break down between permanent and temporary jobs:

The jobs counted here are all full-time positions. They are by no means the only employment effects:

- Construction of these massive industrial facilities have and will temporarily employ hundreds of workers, as might be further estimated.
- Part-time, seasonal and other jobs would also exist at these facilities.
- Beyond standard estimation methods for indirect employment, some of these facilities may have especially high numbers of in-house contractor or vendor jobs.

c. Break down between traded sector and domestic sector jobs:

- They are exclusively traded-sector industries.

d. Estimates of average wage per job:

- Average wages are high due to required minimum average annual compensation (with fringe benefits) at 150 percent of the county average wage following the start of operations, to be maintained during the up to 15-year exemption period. (This requirement also eliminates this incentive for other, less well-paying opportunities)
- Excluding fringe benefits, the average wage is estimated to be currently at least $47,000 per year.

e. Estimate of tax revenue cost per job:

- There is no available data on tax revenue, such that cost per job may be zero.
- Nevertheless, using an assumed 80 directly attributable, full-time jobs and $200,000 of affected corporate excise taxes each year, the annual cost per job would be $2,500.
- Interactive consideration of the property tax abatement and other costs is appropriate, but in accounting for overall employment and economic return, there are also other benefits as noted above.

The above estimates are based on actual data from recent research with the cooperation of local government and company officials. It is proximate, derived from program operations for the property tax exemption, so that one must make conservative assumptions to isolate potential effects of the state income tax credit itself.

Who (groups of individuals, types of organizations or businesses) directly benefits from this credit? Does this credit target a specific group? – Yes

- The direct beneficiary is a business operating in rural Oregon that:
  1. Has received certification through the local sponsor of the enterprise zone, and
  2. Owns the facility receiving the 7–15-year exemption.
- To enjoy that exemption and to claim this credit, the facility must achieve minimum investment ($2–25 million), minimum new hiring (10, 35, 50 or 75 jobs), and minimum average annual employee compensation.
- The credit itself necessitates gubernatorial authorization, which also determines how long the taxpayer may claim it over 5 to 15 years on a Department of Revenue form.
- At 62.5 percent of the facility's gross payroll, it is limited to the tax liability relating to the facility, and then, only after an actual annual tax payment of as much as $1 million.
- Because of how these features are structured, this intricate tax credit has rather restricted potential for actually benefitting a typical taxpayer.
- Therefore, the credit very narrowly targets a locally approved business firm in rural Oregon that builds and operates a facility meeting particular criteria, which also benefits the persons and businesses that constructed, supply and work at the facility.

If so, is it effectively reaching this group?

- Data are unavailable for direct, corporate taxpayers' using this particular tax credit, and corporate tax savings cannot be assumed in view of its complex thresholds.

- Nevertheless, to the extent that such a corporate employer is paying sufficient taxes to the State of Oregon, that taxpayer can certainly claim the benefit provided by law.

What is expected to happen if this credit fully sunsets?

- Scheduled sunset would affect rural Oregon, by removing a targeted inducement, notwithstanding the small number of potential economic opportunities involved.
- This state income tax credit does enhance efforts to market parts of rural Oregon at little to no cost.

Could adequate results be achieved with a scaled down version of the credit? What would be the effect of reducing the credit by 50%?

Given the already highly restricted nature of this tax credit, curtailment would likely detract from potential results. A 50% reduction is hard to conceptualize.

What background information on the effectiveness of this type of credit is available from other states?

- Many other states can offer property tax abatements of 10–15 years. In addition, various enterprise zone programs exist that typically rely on credits against state taxes.
- Both types of tools are evidently used to great effect in some of these states, subject to program design, implementation, opportunities and so forth, but diversity and differences defeat interstate comparison.
- In any event, Oregon's long-term rural enterprise zone program and this particular credit appear to be unique.
- In addition, such incentives have their greatest effect only within a context of other state and local programs and efforts, whether in Oregon or elsewhere.

Is use of a tax credit an effective and efficient way to achieve this policy goal?

- Yes, the availability and use of this credit has been a key feature for numerous inquiries by large companies considering major facilities in rural Oregon.
- So far, local zone sponsors have certified eight projects, with more than 500 direct, full-time employees.
- Approval by the Governor for this state tax credit has so far occurred four times with facilities involving large capital investments, for which local property tax abatement is the program's main driver.
- Nevertheless, this income tax credit appears to have been a significant motivator for two of the projects undertaken and for two tremendous opportunities that were lost for other reasons.
- Therefore, to that extent, it has had a significant effect in fulfilling its policy purpose.
- The efficiency of this tax credit is self-evident, in that even if the sunset is extended, the estimated, foregone revenues are modest relative to potential economic benefits with just the immediate, permanent jobs.

What are the administrative and compliance costs associated with this credit?

- Such costs exist to some extent across two state agencies and a number of local sponsoring governments, but they are diffused amongst related activities, including other aspects of Oregon's enterprise zone system.
- As such, there is not the data to estimate a figure.

Would a direct appropriation achieve the goal of this credit more efficiently?

- Not likely, in that there could be greater fiscal costs and complexities in managing direct funds.

- There would also be challenges designing program structures to ensure desired focus and efficiency with actual expenditures, as well as fine-tuning how much money to budget, year-to-year, not knowing when to predict the appearance of relevant opportunities.

What other [programs] (including state or local [funding or financing], federal tax expenditures or subsidies) are available that attempt to achieve a similar policy goal?

- This tax credit is unique in its nature and advances its goals for business development in combination with other state & local programs, which may include access to federal infrastructure financing and the like.
- Direct funding or other types of programs could be devised, of course, to achieve any equivalent incentive effect, with the potential of greater upfront impact and cash value for a prospective business project, but tax-based approaches can have their own advantages, like the aforementioned administrative points, as well as:
    - Proportionally greater discounted value for the taxpayer relative to the immediate impact on public revenues, in some cases.
    - Leaving economic decisions largely in private hands, thus minimizing distortions.
    - Having an incentive that from the outset, can be presented to applicable businesses with a high degree of certainty—which will often be indispensable for effectively marketing the state and certain locations to traded-sector businesses, whether they are new or existing in Oregon.

Could this credit be modified to make it more effective and/or efficient? If so, how?

- As noted, this credit has proven effective and efficient in helping promote economic development opportunities in parts of rural Oregon.
- Greater effectiveness may depend on relaxing restrictions, so that the tax benefit is more readily and reliably useable, and potentially more broadly applicable.
- Other options to consider or examine include having a comparable type of payroll-based incentive that operated independent of an enterprise zone program.

How would the return on the state's investment best be measured for this credit?

- The return to the state arises from greater economic opportunities for rural Oregonians through further development and increased employment.
- Within a reasonable amount of time, this return will improve the personal income tax base for the State of Oregon, both directly and indirectly.

Which of the following can be quantified as a "return" or "benefit" resulting from the use of this credit:

a. Jobs & overall economic activity? — Yes

b. Environmental goals such as energy conservation, air/water quality? — No

c. Social goals — No, other than increased employment

- In the above respects, the so-called 'but-for' question arises in terms of the degree, to which without the incentive, nothing would have happened any time soon. It may never be possible to provide absolute guarantees in such regards
- Nevertheless, with one of the four facilities so far approved by the Governor, this tax credit was crucial to winning that game-changing development in rural Oregon, based on close interaction with company tax managers.
- Public testimony on this bill has also told of two other examples of huge facilities by corporations with household names – and with otherwise minimal presence in Oregon – that failed to proceed for other reasons, but clearly, they would never have come so close but for this tax credit.

Using the three broad categories above, how do these credits rank in terms of their expected return on investment?

- Though difficult to quantify precisely, the overall return-on-investment for this tax credit seems a little less than that of the electronic commerce enterprise zone tax credit (1.418), which would be the only currently sun-setting tax credit that can be commonly categorized with respect to direct business development.
- Both credits, however, involve relatively little in the way of invested public revenues.
- In Oregon, few state income tax credits relate to economic development, but the effects and quantifiable returns of even those few are not directly comparable here.
- Finally, this tax credit is also aimed in particular at helping rural hardship areas of the state. To the extent that it does help to offset regional disadvantages, it may contribute not only to better economic equity but also to more efficient resource allocation within Oregon.

Oregon Enterprise Zones

July 2010