Incentives to Spur Business Development – Programs:

Thank you Chair Lively, Vice-chairs Bonham and Fahey, and honorable members of the House Committee on Economic Development. We greatly appreciate the work of this and similar committees in addressing such important questions for these valuable parts of Oregon's so-called "toolbox" for economic development. I am happy to talk more fundamentally about the debate and role of incentives. For the moment, I will say only that the agency has always ascribed to the importance of good program design (just throwing benefits at businesses is no good), and secondly, incentives do not and should not make a weak project strong. Rather, at the margin, they help drive economic development, and cannot be isolated from other factors such logistics, useable land or available work force, as well as other state and local efforts.

Generally, Oregon has a limited toolbox when it comes to such incentives, compared to other states. For example, Oregon has hardly ever made much use of income tax incentives, and now, there is no state tax credit directly for economic development. As for tax incentives, Oregon instead relies all but exclusively on its other major revenue source – local property taxes.

The abatement of taxes on new property – despite our and other state agencies' duties – have a decidedly local character, so that local players are indispensable in this conversation. Property tax abatement can be very potent. This is all the more obvious the larger the capital investment. No single inducement or program can serve every situation, and there are various pros & cons in program design—for example, in being more or less programmatic versus discretionary, or in using tax preferences versus direct funds, like the first program presented below (BEP).

And tough administered by this agency, BEP is nevertheless governed by statutory requirements, and as for tax incentives, virtually everything we have to say is dictated by program laws or is a function of related tax law with prescribed local discretion.

We would also refer the committee to other sources of information, including:

- Biennial TAX EXPENDITURE REPORT (except for BEP, it is heavily drawn from here)
- State Transparency Website
- Business Oregon | Investments <http://www.oregon4biz.com/About-Us/Investments-Report>
- Committee staff's background briefs and Legislative Revenue Office (LRO) reports
- Others' and my presentation to the committee on February 6, 2019.

Finally, as noted in some cases below, we continue to look for ways to improve the completeness and thoroughness of the data available for purposes of accountability and public information, including working with local and state agencies. We are also pursuing efforts to update or undertake sophisticated, quantitative evaluation of these programs. Challenges in these endeavors include but are not limited to the decentralized nature of property tax programs and variable local capacities, as well as limited staffing and resources at the state level for data management and analysis.

Business Retention and Expansion Program (BEP) – cash award (forgivable loan) by Business Oregon

1. *What are the conditions for approval?* [By law]
   - The business needs to be an established employer with 150 or more employees.
   - It must engage in a traded sector industry and not be otherwise a retailer.
   - Business must present credible plans to hire at least 50 new Oregon employees at 150% or 130% of state or county average wage.
   - Money must be available in Strategic Reserve Fund (SRF) to cover incremental personal income tax revenue (IPITR) as estimated based on new employment over two years.
   - Standards and obligations in the agency performance agreement or contract with business.
   - Business needs to have entered into first-source hiring agreement with Employment Department, as the contact agency for local publicly funded job training providers, for purposes of client referrals for job openings at business.

2. *Is the program/incentive working or achieving its purpose?* **Yes**—in that the purpose is inducing singular opportunities with sizeable payroll through an incentive based on such payroll (in contrast to capital expense) that will help grow personal incomes and resulting tax revenue:
   - Over 8 years, BEP has been a critical further inducement for a handful of major, high-quality employment opportunities by Garmin, Daimler, Salesforce and others, distinct from the capital bias with property tax abatements and as an alternative to regular SRF awards.
   - Besides the return tp state income taxes, the agency scrutinizes the additional/but-for nature of this incentive in association with other available inducements.

3. *How do we know the program/incentive is working?*
   - State experiences first-hand the impact of the employment created and the longer-term return to general fund revenues.
   - The agency uses confidential payroll tax data to compute hiring and compensation in estimating actual IPITR based on the employees who meet wage criteria.
   - Greater use of this program could have prevented the loss other business development opportunities, but rather than available funds, the main restrictions are the high standards for business eligibility.

4. *What happens if recipient doesn't fulfil the requirements? Are there claw back provisions?* **Yes**—essentially, the program is self-regulating as a forgivable loan, such that if final payroll data after two years indicate that the actual IPITR among sufficiently high-wage jobs is less than the amount awarded, then commensurately less of the loan is forgiven and must be paid back with interest under contractual obligations.

Standard Enterprise Zones – exemption on new qualified property of eligible business firms from local property taxes for three to five years

1. *What are the conditions for approval?* [By law]
   - Eligible business operations, full-time jobs and qualified property must be inside current boundary of designated enterprise zone (73 at present), sponsored by city, port or county government, and that satisfied local hardship and other statutory criteria at designation. (Same exemption allowed for certain cases in **rural renewable energy development zones**)

- Business needs to apply for authorization locally before beginning physical investment.
- Business and jobs must be engaged and property used for statutorily specified activities, that mainly serve to exclude retail or other locally competing business activities.
- The firm's employment in the zone is required (by law, of course) to grow by the greater of one job or 10% compared to pre-authorization annual average, as confirmed each year with exemption claim filing after qualified property is placed in service, unless waived at authorization by resolution(s) of local zone sponsor under specific alternative provisions.
- Business needs to have entered into first-source hiring agreement with Employment Department, as the contact agency for local publicly funded job training providers, for purposes of client referrals for job openings at business.

2. *Is the program/incentive working or achieving its purpose?* **Yes—**in that the purpose is the betterment of the state as a whole by directing particular assistance primarily through tax incentives, as desired by local government, to areas of need in order to stimulate employment, business, industry and commerce (based on ORS 285C.055):
    - Over many years—and subject to periodic legislative review, statutory changes, and extensions of sunset dates—enterprise zones continue to serve and complement local efforts in a variety of rural, suburban and urban settings that face economic hurdles in areas ranging from neighborhoods to the broader region.
    - Locally elected governments across nearly 200 jurisdictions review this tool and choose to deploy it, on a recurring basis, in order to support local businesses and induce additional investment that contributes to the property tax base after a relatively brief period, as well as new hiring, construction and commerce.
    - Across Oregon, the enterprise zone is often the only incentive available at the state and local level.
    - Hundreds of firms of all sizes with diverse business types and investments – and mostly operating already in the zone – are involved at one stage or another with the program, adding 1,000 to 2,000 full-time jobs each year (directly at the business in the zone, respective to 10% requirement which is typically exceeded) in communities throughout the state.
    - By and large, most of these businesses and their facilities appear to be going strong many years if not decades after the exemption period.

3. *How do we know the program/incentive is working?*
    - Local confidence in the program – among governments, who are often working productively together with the enterprise zone designation – based on direct involvement with community and businesses.
    - Local and state officials regularly witness its pivotal role—in retaining employers within a region, in competing for reinvestment capital within a larger corporation, in bolstering start-up companies, in attracting new operations to the community, and in inducing investments and hiring to go forward faster or bigger than anticipated.
    - Businesses fill-out rigorous Department of Revenue (DOR) tax forms before and after hiring and investment, and then annually, they file with locally based officials, who are engaged in the community, and for which there is every reason to believe that notwithstanding errors & omissions, these businesses want to avoid 20% penalty or the risks of falsification.
    - Authorizations are copied to state agencies, and pursuant to exemption claim filings, county assessors annually report property tax and jobs data to DOR.

- For nearly 20 years, the agency has provided templates and worked with DOR and assessors to improve the consistency and accuracy of the data, following up to assist with particular circumstances related to compliance and to otherwise clarify and resolve issues, including on a more regular bases of late for purposes of better data management, as well.
- Analytically, the agency is pursuing more sophisticated methods, especially for the following two paths for calculating the return to state and local revenues, for which even after trying to account in certain probabilities and factors, for which back-of-the-envelope estimates indicate robust payback of the property taxes foregone by way of:
    - Taxes on other property and on exempt property in the years following exemption.
    - Personal income taxes paid through net increases in employment.

4. *What happens if recipient doesn't fulfil the requirements? Are there claw back provisions?* **Yes–** including local additional requirements as applicable, for which zone sponsor is responsible.
    - Many conditions or requirements are effectively tested at authorization (pre-project) or before the exemption is allowed to begin on the county assessment and tax rolls.
    - If employment or other conditions in the law are not maintained during the exemption period, then the law clearly provides for the payment of back taxes on disqualified property in the next tax roll.
    - Ultimately it is up to the county assessor (often the tax collector, too) to handle such enforcement, but in practice it is a team effort involving state agencies, as well as oftentimes local zone sponsors and managers, who interact with the qualified business firms and also receive statutory claim forms or even special local reports from them.
    - As such, a few disqualifications occur every year, and Business Oregon is often involved supporting local officials to recognize and act on noncompliance, which may or may not be really complex. In addition, one-year payments in lieu of disqualification are often allowed as a one-time, temporary option. Current systems are not able to capture the taxes or other moneys collected in these regards or arising from local additional requirements.

Long-term Rural Enterprise Zone Facility – exemption on new facility property from local property taxes for 7 to 15 years

1. *What are the conditions for approval?* [By law]
    - Business/facility needs local agreement with the zone sponsor and city & county resolutions approving the facility's receipt of the incentive as part of local certification.
    - Facility must be located inside the current boundary of designated rural enterprise zone in a county that satisfies certain economic or geographic criteria (39 of 73 zones, see above).
    - Business needs to apply for certification locally before beginning physical investment.
    - Facility investment costs must meet minimum that is usually $12.5 or $25 million, and new full-time hiring at the facility needs to be at least 10, 35, 50 or 75 new jobs; requirements decrease with county population and the greater the distance from Interstate–5
    - General facility employment must on average meet wage and compensation requirements respective to the annual county wage as fixed when the compensation requirement is first met within the first five years of the exemption.

2. *Is the program/incentive working or achieving its purpose?* **Yes**—in addition to that described above for the standard exemption, the purpose is to help drive major employment opportunities to rural parts of the state that face chronic economic conditions:
    - For 20 years—and subject to periodic legislative review, statutory changes, and extension of sunset date—this program has been a special tool for rather unique opportunities in some the more challenging parts of rural Oregon with respect to economic development.
    - As such, it is a special purpose tool with high standards not only for quality workforce by statute, but also for local discretion as a matter of practice, although most of the investments have not needed to cost nearly as much as they have.
    - Besides the choice to have the enterprise zone in the first place, locally elected governments carefully consider the opportunity that each facility offers and negotiate agreements, representing an important form of local control.

3. *How do we know the program/incentive is working?*
    - These facilities have tended to be very impactful or even transformative for the local economies affected, such that for many sponsors of eligible rural areas the issue would be how to find more such opportunities.
    - There have been 12 exemptions in only 4 counties by 8 companies so far, involving food processing, advanced lumber, data centers and other operations, with as many as 1,000 persons currently working in well-paying jobs of the business or for on-site contractors at these facilities. Several more facilities are certified including in 3 other counties.
    - To the matter of local discretion, zone sponsors have declined to offer this incentive in at least a few cases, and those that do, will have judged the likelihood of so much property otherwise being available for taxation.
    - Working with DOR, local zone managers and county assessors, the agency has created administrative tools and procedures to enhance local verification and data collection for evaluation on a systematic basis, for which further improvement continues.

      (These efforts are intended to compensate for a lack of statutory provisions and authority with respect to prescribed forms, processes and reporting after the start of facility operations and 7–15-year exemption period. As program use continues to grow, however moderately, ad hoc methods may not suffice going forward.)
    - This program will be incorporated into future analytical efforts noted above for the standard exemption, but the net benefit to the state may depend a great deal on the value of such facilities' locating where they do in affecting regional disparities and resource allocation.

4. *What happens if recipient doesn't fulfil the requirements? Are there claw back provisions?* **Yes**–including local additional requirements as applicable, for which zone sponsor is responsible.
    - Investment, hiring, compensation and wage minimums must be met by certain points in time, and then maintained over the entire 7 to 15-year period, or all back taxes come due on the next tax roll, with limited provisions for extenuating circumstances.
    - As noted above, the agency is working with local partners to augment thin statutory provisions for monitoring business compliance, with which technical proposals in House Bill 2053 (2019) would also help.
    - In one rather complicated case, the agency assisted DOR and local partners to reverse the exemption on an additionally certified facility that expanded a previously exempt facility but that did not add enough new, additional jobs (75) at the facility site to qualify.

Strategic Investment Program (SIP) – 15-year abatement of taxes on property value above taxable portion (partial exemption) on very large eligible projects

1. *What are the conditions for approval?* [By law]
   - Business needs local agreement with county and city resolutions approving the eligible project, as executed after a county public hearing and before the county governing body votes to send the project to the Oregon Business Development Commission (OBDC).
   - Business must apply to the agency for OBDC determination of approval as an eligible project and definition of the project property to receive SIP tax treatment.
   - Statutes require that eligible project benefits a traded-sector industry and costs at least $25 million in rural areas or $100 million (in reality, costs need to be much greater for program use to make sense).
   - As contained in the agreement with possibly local additional requirements, business must annual pay a statutorily prescribed community service fee up to 25% of each year's tax savings, subject to certain maximums. (Another local agreement addresses distribution of fee moneys among the county, city and affected special service districts)
   - Business needs to have entered into first-source hiring agreement with Employment Department, as the contact agency for local publicly funded job training providers, for purposes of client referrals for job openings at business.
   - Business must annually report on project status, employment and payroll to the agency.

2. *Is the program/incentive working or achieving its purpose?* **Yes—**in that the purpose is to give localities a way to accommodate unusually outsized developments with extraordinary property tax implications, by being able to offer arguably more appropriate tax treatment and to work out potentially other arrangements. In 2003, ORS 285C.603 added as a significant purpose the improvement of employment in the region where an eligible project is to locate.
   - For 25 years this program has served as a special basis for local governments to negotiate with businesses that are proposing extremely large capital investments, of which almost all projects are in rural Oregon.
   - SIP has been indispensable in allowing Intel to remain competitive and grow its Oregon operations to nearly 12,000 exceptionally good jobs at SIP-affected campuses, and there are practically as many employees with associated contractors on-site, as well as other Intel locations in the Hillsboro area. (Intel's capital requirements are simply off-the-chart; and it is in any case far and away the largest taxpayer in Washington County)
   - Rural projects, though largely energy-related so far, have offered the means to work out mutually beneficial partnership between the county and developer; a notable example of this has been several massive wind farms, which are not only unsuitable for inclusion in an enterprise zone, but for which the assessment and tax effects of central assessment by the state have also been unpredictable at times, and unfavorable compared to other states.
   - Local governments are also intimately engaged in judging whether the project might happen anyway, the impact for local job market, and the value of agreement terms.
   - The regional proximity of employment might be at best assumed.

3. *How do we know the program/incentive is working?*
- Across northern Oregon in nine counties, so far, there have been 23 former or ongoing projects, and several more that are or will be constructed.
- Unusually large amounts of local revenue are collected early on, as a result of new taxable property and non-tax payments under SIP agreements (which may well exceed the taxes that might have otherwise been collected from a more common development), providing significant streams of income for local governments and predictable costs for the business.
- Annual reports by businesses to the agency provide a manageable and high-quality source of data for property tax effects, the additional fees or payments made by the business firms to local government, and the number of new and retained jobs and payroll directly connected to the projects to estimate state revenue from personal income taxes
- SIP will be incorporated into future analytical efforts noted above for the standard enterprise zone exemption.

4. *What happens if recipient doesn't fulfil the requirements? Are there claw back provisions?*
- There is no statutory requirement in terms of employment or the like, and local requirements are governed by the county–business agreement.
- If, however, the county does not receive the annual community service fee or the agency does not receive the annual payroll report, then OBDC shall suspend the partial exemption.

Oregon Investment Advantage (OIA) – 10-year income tax subtraction of taxable income arising from new facility operations of certified business firm

1. *What are the conditions for approval?* [By law]
- Business must apply for preliminary certification with the agency before hiring or any work to construct or improve the facility.
- The proposed facility site must be in one of currently 15 eligible counties, which are recently among the worst counties in terms of both per capita income and unemployment.
- It must be also inside the urban growth boundary of a city of 15,000 or fewer residents or on industrially zoned land in a larger city or unincorporated area.
- The proposed facility needs to be intended to operate for at least 10 years.
- The proposed operations at the facility need to constitute new operations, unlike what the business does anywhere else in Oregon or what was done at the facility recently.
- These operations must not compete with existing employers in the city, port or county where the facility is located.
- The city, port or county does not officially object within 60 days.
- The business must hire five or more full-time, year-round employees at the facility.
- Those five employees (according to the statutes) need to each receive compensation at a certain level relative to the county per capita income from the time of the preliminary certification application, and their average wage must equal or exceed the current county average annual wage.
- Facility operations must begin within a reasonable time without undue delay after the preliminary certification was issued.
- Starting not less than 24 months after facility operations have begun, the business needs to apply annually to the agency for certification following each of the 10 allowed income tax years, for which it would claim subtraction.

2. *Is the program/incentive working or achieving its purpose?* **Yes—**in that the purpose is to provide further means to foster new business operations in Oregon's most economically lagging (rural) areas through an innovative type of tax incentive that relates directly to the taxable income arising from the new operations.
   - For 16 years, this program has helped augment efforts to expand and attract businesses to the poorest/highest unemployment counties in Oregon, serving as supplemental or alternative inducement apart from the capital bias attendant to property tax abatements.
   - The Cascades Tissue plant with 71 anticipated jobs in Scappoose is an excellent example of this program's ability to make a difference, from when Columbia County was still eligible.
   - OIA has been an important way to further economic development in the most rural parts of Oregon, where even the program's moderate requirements for well-paying jobs can be hard for likely business opportunities to satisfy.
   - General use is hampered by the rather involved set of conditions and criteria (see #1 above), the limited number of places where it applies, the business firm's needing a state tax liability to realize any benefit, and the difficulty of conceptualizing and communicating an income tax subtraction.

3. *How do we know the program/incentive is working?*
   - A little more than 20 rather diverse business facilities have used the program since 2006, at which there are still more than 1,000 good jobs in rural Oregon.
   - Although a number of preliminarily certified firms will be coming on in the next year or so (like Cascades Tissue), use has dwindled to only six businesses currently, with 232 jobs averaging well above local area wage levels.
   - Information comes from official forms and processes from the time the project is first proposed through to submissions each year before claiming the subtraction of income on state tax return in relation to a facility already in operations for 2 to 11 years.
   - Annual certification applications contain total employment and pay scales at the facilities, and the agency will explore ways to more formally analyze these data relative to tax effects, geographic objectives and so forth.
   - The program may also be having a rather unexpected revenue impact due to particular claimants of late, for which the agency has recommended capping the amount of income annually subject to subtraction for any particular taxpayer, but historically the program has performed efficiently relative to aggregate revenue impacts.

4. *What happens if recipient doesn't fulfil the requirements? Are there claw back provisions?*
   - Annual certifications provide for a check on continued eligible location and on adequate employment, compensation and wages, for which basic compliance can be reasonably assumed or ascertained as warranted.
   - If these requirements are not met then certification is denied and the business may no longer be certified prospectively. (Retroactive reversal of the subtractions' net tax effect might not be feasible for DOR to determine and collect as an administrative matter)