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# Employment Tax Increment Financing –An Evaluation of Program Design and Analysis of Program Activity from 2010 through 2016, January 2019

Office of Program Evaluation & Government Accountability

Maine State Legislature

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## Employment Tax Increment Financing – An Evaluation of Program Design and Analysis of Program Activity from 2010 through 2016

Report No. TE-ETIF-16

### Recommendations include:

- ETIF’s objectives should be reconsidered based on Maine’s current economic development needs (pg. 38)
- ETIF’s requirements should be reviewed in light of current business realities and updated where necessary (pg. 39)
- Statute should be amended to clearly reflect all intended outcomes against which ETIF’s effectiveness will be measured (pg. 40)
- ETIF’s statute or rule should be amended to support effective implementation of the “but for” application requirement (pg. 41)
- ETIF’s economic consideration requirements should be made more explicit or eliminated (pg. 42)
- The Legislature should clarify whether the same qualifying jobs may be claimed for both ETIF and the MBHE Program (pg. 43)
- Statute should be amended to address businesses that change ownership (pg. 44)
- Confidentiality status of ETIF data should be clarified (pg. 45)
- DECD and MRS should address opportunities to improve fiscal impact forecasts and update rules (pg. 46)
- MRS should strengthen controls to prevent overpayments and ensure accurate ETIF records (pg. 47)
- DECD should address information technology and staffing challenges (pg. 47)

a report to the  
**Government Oversight Committee and Taxation Committee**  
from the  
**Office of Program Evaluation & Government Accountability**  
of the Maine State Legislature

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## OFFICE OF PROGRAM EVALUATION & GOVERNMENT ACCOUNTABILITY

Director: Danielle Fox

### Staff:

Matthew Kruk, Principal Analyst  
Scott Farwell, Senior Analyst  
Jennifer Henderson, Senior Analyst  
Amy Gagne, Analyst  
Kari Hojara, Analyst  
Joel Lee, Analyst  
Ariel Ricci, Analyst  
Etta Connors, Administrative Secretary

### Mailing Address:

82 State House Station  
Augusta, Maine 04333-0082  
Phone: (207) 287-1901  
Fax: (207) 287-1906  
Web: <http://legislature.maine.gov/opega>  
Email: [etta.connors@legislature.maine.gov](mailto:etta.connors@legislature.maine.gov)

## ABOUT OPEGA & THE GOVERNMENT OVERSIGHT COMMITTEE

The Office of Program Evaluation and Government Accountability (OPEGA) was created by statute in 2003 to assist the Legislature in its oversight role by providing independent reviews of the agencies and programs of State Government. The Office began operation in January 2005. Oversight is an essential function because legislators need to know if current laws and appropriations are achieving intended results.

OPEGA is an independent staff unit overseen by the bipartisan joint legislative Government Oversight Committee (GOC). OPEGA's reviews are performed at the direction of the GOC. Independence, sufficient resources and the authorities granted to OPEGA and the GOC by the enacting statute are critical to OPEGA's ability to fully evaluate the efficiency and effectiveness of Maine government.

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## Acronyms Used in This Report

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BETE – Business Equipment Tax Exemption  
 BETR – Business Equipment Tax Reimbursement  
 DAFS – Department of Administrative and Financial Services  
 DECD – Department of Economic and Community Development  
 ETIF – Employment Tax Increment Financing  
 FAME – Finance Authority of Maine  
 FOAA – Freedom of Access Act  
 GAO – Government Accountability Office  
 GOC – Government Oversight Committee  
 ICA – Investment Consulting Associates  
 LMA – Labor Market Area  
 MBHE – Major Business Headquarters Expansion  
 MDOL – Maine Department of Labor  
 MRS – Maine Revenue Services  
 MSTER – Maine State Tax Expenditure Report  
 NMTC – New Markets Capital Investment Credit  
 OIT – Office of Information Technology  
 OPEGA – Office of Program Evaluation and Government Accountability  
 PTDZ – Pine Tree Development Zones  
 TIF – Tax Increment Financing

## Terms Used in this Report

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**BDTI.** The Business Development Tax Incentive (BDTI) software is used by DECD to manage tax incentive program data.

**ERISA.** The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for pension and health plans in private industry.

**Gross State Product.** Gross State Product (GSP) is a measurement of a state's output and is the state counterpart of the Nation's gross domestic product (GDP). It is the sum of value added from all industries in the state.

**IMPLAN.** An input-output model used to estimate economic impacts.

**Job Year.** A job year of employment is defined as full-time employment for one person during one year. Job years count the duration of a job, such that one job that exists 10 years is counted as 10 job years.

**Labor Market Area.** A labor market area (LMA) is a geographic area within which individuals can reside and find employment within a reasonable distance or can readily change employment without having to move. LMAs are defined by the U.S. Department of Labor, Bureau of Labor Statistics based on commuting pattern data. There are currently 30 defined LMAs for Maine.

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# Employment Tax Increment Financing – An Evaluation of Program Design and Analysis of Program Activity from 2010 through 2016

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## Introduction

The Maine Legislature's Office of Program Evaluation and Government Accountability (OPEGA) conducts reviews of tax expenditures in accordance with Title 3 §§ 998 and 999. Tax expenditures are defined by Title 5 § 1666 as "state tax revenue losses attributable to provisions of Maine tax laws that allow a special exclusion, exemption or deduction or provide a special credit, a preferential rate of tax or a deferral of tax liability." Tax expenditure reviews fall into one of two categories, full evaluation and expedited review. The Government Oversight Committee, in consultation with the Joint Standing Committee of the Legislature having jurisdiction over taxation matters, assigns a category to tax expenditures and establishes a prioritized schedule for the reviews.

The tax expenditure review process was established as the result of Resolves, 2013, chapter 115, which directed OPEGA to develop a proposal to be considered by the Joint Standing Committee on Taxation during the 127th Legislative Session. On March 2, 2015, OPEGA submitted the report outlining the proposal for implementing ongoing reviews and included a chart of identified tax expenditures (<http://mainelegislature.org/doc/578>). The report states that the purposes of establishing a formal, ongoing legislative review process are to ensure that:

- Tax expenditures are reviewed regularly according to a strategic schedule organized so that tax expenditures with similar goals are reviewed at the same time;
- Reviews are rigorous in collecting and assessing relevant data, determining the benefits and costs, and drawing clear conclusions based on measurable goals; and
- Reviews inform policy choices and the policymaking process.

The proposal became LD 941 An Act to Improve Tax Expenditure Transparency and Accountability and was enacted as Public Law 2015, chapter 344. Part of this law, Title 3 § 999, provides that the Government Oversight Committee establish parameters for each full review based on the following:

- The purposes, intent or goals of the tax expenditure, as informed by original legislative intent as well as subsequent legislative and policy developments and changes in the state economy and fiscal condition;
- The intended beneficiaries of the tax expenditure;
- The evaluation objectives, which may include an assessment of:
  - The fiscal impact of the tax expenditure, including past and estimated future impacts;
  - The extent to which the design of the tax expenditure is effective in accomplishing the tax expenditure's purposes, intent or goals and consistent with best practices;

- The extent to which the tax expenditure is achieving its purposes, intent or goals, taking into consideration the economic context, market conditions and indirect benefits;
  - The extent to which those actually benefiting from the tax expenditure are the intended beneficiaries;
  - The extent to which it is likely that the desired behavior might have occurred without the tax expenditure, taking into consideration similar tax expenditures offered by other states;
  - The extent to which the State's administration of the tax expenditure, including enforcement efforts, is efficient and effective;
  - The extent to which there are other state or federal tax expenditures, direct expenditures or other programs that have similar purposes, intent or goals as the tax expenditure, and the extent to which such similar initiatives are coordinated, complementary or duplicative;
  - The extent to which the tax expenditure is a cost-effective use of resources compared to other options for using the same resources or addressing the same purposes, intent or goals; and
  - Any opportunities to improve the effectiveness of the tax expenditure in meeting its purposes, intent or goals; and
- The performance measures appropriate for analyzing the evaluation objectives. Performance measures must be clear and relevant to the specific tax expenditure and the approved evaluation objectives.

As directed by the 127th Legislature's Government Oversight Committee and in accordance with the parameters approved by the Committee, OPEGA has completed a review of the Employment Tax Increment Financing (ETIF) Program. The approved parameters can be found in Appendix C. Those parameters establish the goals, intended beneficiaries, and base performance measures assessed in this evaluation.

Maine's ETIF Program was established in 1996 and is governed by Title 36 Chapter 917. The program is administered jointly by the Department of Economic and Community Development (DECD) and Maine Revenue Services (MRS). ETIF benefits are available to any eligible Maine business that hires at least five net new, qualified employees<sup>1</sup> above its baseline employment level established at the time of application. These five new employees must be hired within two years of a business's ETIF certification, must be paid at a wage that exceeds the most recent annual per capita income in the county in which the employee is employed, and must have access to health and retirement plans. A participating business receives payment equal to a portion of withholding taxes submitted to the State on behalf of all ETIF qualified employees.

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The ETIF Program was established in 1996 and is jointly administered by DECD and MRS.

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<sup>1</sup> Throughout this report new employees will be referred to as new jobs.

The ETIF Program is closely tied to Maine’s Pine Tree Development Zone (PTDZ) Program. OPEGA released an evaluation of PTDZ in 2017 and notes that there is significant overlap between the issues identified in each evaluation due to the relationship between the two programs. The relationship also had implications for evaluating ETIF’s impacts and outcomes as noted throughout this report. PTDZ is subject to an automatic statutory repeal and consequently will stop certifying new participants after December 31, 2021. ETIF, however, has no similar provision.

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OPEGA’s review focused on the evaluation objectives detailed in Appendix A. OPEGA used data from DECD and MRS for program years 2010 through 2016, including some data classified as confidential taxpayer information.

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OPEGA performed extensive review of relevant statute and rules; reviewed program documents such as certification materials and annual ETIF requests filed by businesses; interviewed program managers at DECD and MRS; sought perspectives from stakeholders; and analyzed program data obtained from both DECD and MRS. The data OPEGA analyzed includes confidential taxpayer information obtained pursuant to Title 3 § 1001(1)(A). We are reporting our analysis of that data in accordance with Title 3 § 1001(1)(E-F) which limits the level of detail we are able to provide.

OPEGA’s analysis is limited to program years 2010 through 2016 as complete electronic program records were readily available for those years. Payments associated with program years 2010 through 2016 were made in fiscal years 2012 through 2018. Complete scope and methods for this evaluation are detailed in Appendix A.

## About the Employment Tax Increment Financing Program ---

### Program Description

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The ETIF Program makes payments to businesses equal to a percentage of the withholding taxes paid by net new qualifying employees. It was enacted in 1996.

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Maine’s ETIF Program was enacted in 1996. Although the ETIF Program is referred to as a reimbursement, the program does not actually reimburse businesses for any taxes paid on their own behalf. Instead, ETIF authorizes distribution of annual payments to certified businesses for up to 10 years. Payments to a business are based on a percentage of the withholding taxes paid by net new qualifying employees of that business. ETIF payments are funded by annual transfers of General Fund undedicated revenue to the state employment tax increment contingent account as provided in Title 36 § 6758(3). Upon the program’s enactment, total annual payments were capped at \$20 million to be adjusted for inflation. OPEGA estimates that the inflation adjustment results in a program cap of approximately \$32.1 million as of January 2018.

**Program Intent:** to encourage the creation of net new quality jobs in this State, improve and broaden the tax base, and improve the general economy of the State.

**Program Goal:** to encourage the creation of net new quality jobs.

**Primary Intended Beneficiaries:** for-profit businesses that create new quality jobs.

**Secondary Intended Beneficiaries:** job-seekers.



OPEGA estimates that ETIF's annual payments are capped at approximately \$32.1 million as of January 2018.

Only for-profit businesses can participate in ETIF, and retail businesses may only qualify under specific conditions<sup>2</sup>. Businesses in any non-retail sectors may participate in the ETIF Program. In order to maintain certification and be eligible for ETIF benefits, a business must hire at least five qualified new employees, above its baseline employment level, within two years of certification. The business must also submit Maine income tax withholdings to MRS for each qualified employee in order to claim ETIF payments.

Any employees hired above a business's employment baseline may be claimed as qualified if they are:

- full-time;
- hired in the State by a qualified business;
- offered access to an ERISA qualified retirement program;
- offered access to a group health insurance program; and
- provided with annualized compensation that is greater than the most recent annual per capita personal income in the county in which the qualified employee is employed.

These requirements apply to all ETIF employees statewide with the exception of employees at call centers in Washington or Aroostook counties who have adjusted minimum income requirements<sup>3</sup>. Employees that have been shifted to a qualified business from an affiliated business do not meet the requirement of being net new employees.

Under ETIF, a business may receive payments equal to 30%, 50%, or 75% of the State income tax withholdings paid for its qualified new employees. Elective, excess withholding is excluded from calculation of ETIF benefits. The ETIF rate each business may receive is determined based on the unemployment rate of the Labor Market Area (LMA) in which each business is physically located. However, a business jointly certified under ETIF and PTDZ may receive an expanded ETIF benefit equal to 80% of the withholdings regardless of the unemployment rate in that LMA.

<b>ETIF Benefit Rates</b>
<b>30%</b> for businesses in LMAs where unemployment ≤ State unemployment rate
<b>50%</b> for businesses in LMAs where unemployment rate > State unemployment rate and ≤ 150% of the State unemployment rate
<b>75%</b> for businesses in LMAs where unemployment rate > 150% of State unemployment rate
<b>80%</b> for PTDZ certified businesses

Businesses jointly certified under ETIF and PTDZ can receive 80% of the State income tax withholdings associated with their qualified new employees rather than the 30%, 50%, or 75% rates available to businesses certified for ETIF alone.

<sup>2</sup> Under Title 36 § 6753(11) retail businesses may qualify for ETIF if less than 50% of their total annual revenues from Maine-based operations are derived from taxable sales in the State or they can demonstrate to DECD that any "increased sales will not include sales tax revenues derived from shifting retail sales from other businesses in the State. Retail operations are defined as "sales of consumer goods for household use to consumers who personally visit the business location to purchase goods."

<sup>3</sup> For employees located at call centers in Aroostook or Washington counties, if the county unemployment rate is greater than the state average, income derived from employment needs to be at least 90% of the average wage for all Maine counties excluding Cumberland and York counties. If the unemployment rate of the county is equal to, or less than, the state average, income derived from employment needs to exceed 100% of the average wage for all Maine counties that don't include Cumberland and York counties.

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The PTDZ Program was extended by the 128<sup>th</sup> Legislature and will now certify new participants through 2021. Under current statute, after 2021, the 80% ETIF rate available to businesses also certified under PTDZ will no longer be available to new participants.

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The 80% rate available to PTDZ businesses represents a significant increase in the amount a business could receive under the ETIF Program alone, and stakeholders cite this joint benefit as highly valuable and desirable. OPEGA noted that since most of Maine is currently designated as a Pine Tree Zone, the 80% ETIF is available throughout most of Maine<sup>4</sup>, essentially rendering ETIF's differentiated benefit levels obsolete. OPEGA found that 89% of the projects associated with ETIF payments in FY17 were paid at this 80% rate rather than the 30%, 50% or 75% level that would otherwise have applied based on the unemployment rate in the local LMA.

The PTDZ Program was statutorily set to stop accepting applications after December 31, 2018. This would have closed the program to new entries after 2018 with payments ending in 2028 to participants certified in the final year. However, in the summer of 2018, the 128<sup>th</sup> Legislature extended the PTDZ Program to continue certifying new participants through the end of 2021. If certifications under PTDZ cease after 2021 without changes to either PTDZ or ETIF statutes, the 80% ETIF benefit rate would phase out as existing PTDZ certifications expired (after 10 years), and the differentiated benefit rates in ETIF statute would become effective again.

### ETIF's Classification as a Tax Expenditure

Although ETIF is considered a tax expenditure, it does not seem to clearly meet the definition of a tax expenditure program or have the characteristics of a typical one. Title 36 § 199-A(2) defines a tax expenditure as “any provision of state law that results in the reduction of tax revenue due to special exclusions, exemptions, deductions, credits, preferential rates or deferral of tax liability.” MRS includes ETIF in its biennial tax expenditure report on the basis of this definition. However, ETIF does not directly impact participants' tax rates or liabilities, and the program is not administered consistent with other tax expenditures.

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ETIF has some characteristics of a tax expenditure program but operates more like a grant program.

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OPEGA observed that the ambiguity about the nature of the ETIF Program, and the subsequent joint administration of the program by MRS and DECD, creates challenges for the State. Some of these challenges include:

- Administrative difficulties – ETIF benefits are claimed via the annual reporting process managed by DECD and processed manually by MRS, separate from the tax filing systems used to process claims for traditional tax expenditures. As a result, both agencies maintain ETIF records – DECD on the cumbersome BDTI database built in-house many years ago, and MRS on Excel spreadsheets.
- Data confidentiality conflicts – Since both MRS and DECD maintain ETIF records, it can be unclear which agency's statutes determine the level of confidentiality provided for which data elements. This creates uncertainty about which records may be publicly disclosed and about which measures the agencies holding the data are required to employ when the data is confidential.

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<sup>4</sup> Tier 2 PTDZ locations were only eligible to receive the 80% ETIF benefit for five, rather than ten years. Under Title 30-A §§ 5250-J(3-A) – 5250-J(3-B) beginning in 2010 Tier 2 locations included units of local government in York and Cumberland counties with municipal unemployment rates that did not qualify for Tier 1.

- Reduced transparency – ETIF’s funding is made by statutory transfer (Title 36 § 6758(3)) rather than by appropriation in the biennial budget process. This provides some benefits for businesses in terms of stability of future program funding. However, operating outside of the appropriations process means ETIF, like other tax expenditures, is not subject to the same rigorous public budgetary debate as other State priorities. The reduction in transparency echoes a finding by the federal Government Accountability Office (GAO) which stated in a 2012 report that “once enacted, tax expenditures and their relative contributions toward achieving federal missions and goals are often less visible than spending programs, which are subject to more systematic review.”<sup>5</sup>

### Confidentiality Status of ETIF Program Data

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There are a number of conflicting statutes that make it unclear which ETIF data is confidential and which ETIF data may be provided to the Legislature and released to the public to support transparency.

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Both DECD and MRS hold ETIF records containing data necessary for administering and evaluating the ETIF Program. Separate sections of law govern the confidentiality status of that data and those records. These sections of law do not work in concert and are subject to varying interpretations. The situation has implications for the level of protection required for particular records and data by the agencies that hold them, as well as for what ETIF data the agencies may disclose to support transparency and accountability for the program.

DECD statute contains a general section (Title 5 § 13119-A) making certain records held by the Department confidential, such as proprietary information, tax or financial information, and credit assessments. Two subsequent sections (Title 5 §§ 13119-B and 13119-C) provide for situations where some information may be disclosed to the public upon request and, more narrowly, to certain entities for specific purposes.

Title 36 contains provisions requiring confidentiality for both tax records generally (§ 191) and ETIF records specifically (§ 6760). Section 191 makes it unlawful for any person who has been permitted to receive a copy of a tax return (in part or in whole), or other information provided pursuant to the Title, to divulge any information contained in those documents. This information is referred to as confidential taxpayer information.

From Title 36 § 191 -

“Except as otherwise provided by law, it is unlawful for any person who, pursuant to this Title, has been permitted to receive or view any portion of the original or a copy of any report, return or other information provided pursuant to this Title to divulge or make known in any manner any information set forth in any of those documents or obtained from examination or inspection under this Title of the premises or property of any taxpayer. This prohibition applies to both state tax information and federal tax information filed as part of a state tax return.”

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<sup>5</sup> GAO, *Tax Expenditures: Background and Evaluations Questions and Criteria*, GAO-13-167SP (Washington, D.C.: November 29, 2012)

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MRS and DECD currently apply differing levels of confidentiality for ETIF data even though most of the data they hold is the same.

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Under MRS standards, protection of confidential taxpayer information may require measures such as actual physical barriers to the information and additional security on laptop computers. These measures go beyond those typically required to protect confidential information that does not fall in the category of confidential tax information under § 191. Because § 191 applies to all of Title 36, which contains ETIF's enabling statute, MRS internally protects all ETIF records as though they fall within the category of confidential taxpayer information. However, once ETIF payments are entered into the State's accounting system (AdvantageME), that data is no longer protected with the enhanced security measures required for confidential taxpayer information. DECD has also not protected ETIF data with the enhanced security measures required for confidential taxpayer information historically, although the Department does currently protect most ETIF data from public disclosure.

#### **Three Levels of Confidentiality that May Apply to ETIF Data**

##### Confidential Taxpayer Information

This information may not be released to the public and must be protected by administering agencies with the most stringent measures.

##### Confidential and Protected from FOAA

This information may not be released to the public.

##### Not Confidential

This information may be released to the public.

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The names of ETIF participants, and amount of payments each received, are currently considered confidential data, but were published in publicly available reports in the past.

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The names of businesses who received ETIF benefits have been disclosed in the past, including as part of the report of the legislative Economic Development Incentive Commission in the year 2000. Statute appears to support this disclosure. Title 5 § 13119-B(1) states that DECD (or a municipality for applicable incentive programs) must release the names of recipients of or applicants for business assistance, including the business principles, if applicable. Under this provision, the information must be released upon request when the request is made after assistance has been provided to a business.

OPEGA recommends that the confidential status of ETIF records and data be amended to clarify what standards are required to ensure confidentiality and what information may be disclosed for the purpose of supporting accountability and transparency of the program. See Recommendation 8.

We also note that because the conflicting provisions make it unclear how ETIF data must be protected, OPEGA was required to protect the data to the highest level – as confidential taxpayer information – in order to obtain access to it. This made our evaluation process less efficient and limited what we are able to report.

### **History of Program Changes**

A few major changes have occurred to the ETIF Program since it was enacted in 1996. These changes impacted the level of benefits for ETIF participants, adjusted the requirements for program participation and introduced the flexibility to allow program participants to assign their ETIF benefits to the Finance Authority of Maine (FAME) in order to secure loans.

Since ETIF's enactment, changes have been made to the level of benefits available via the program and to minimum requirements for participants.

Upon initial enactment, ETIF provided only two benefit rates – 50% for businesses in LMAs with unemployment rates at or above the State rate and 30% for businesses in LMAs with unemployment below the State average. Two years into the program, a statutory amendment made a benefit rate of 75% available for businesses in LMAs where unemployment exceeded 150% of the State average. In 2003, the 80% rate was added to statute when ETIF was integrated with the PTDZ Program.

<b>Date</b>	<b>Description of Statutory Change to Program</b>
July 1998	<ul style="list-style-type: none"> <li>Added a payment rate of 75% for businesses in Labor Market Areas with unemployment rates greater than 150% of the State average unemployment rate (P.L. 1997 ch.766)</li> </ul>
September 2001	<ul style="list-style-type: none"> <li>Allowed a business to receive ETIF benefits after hiring 5 or more qualified employees rather than 15 qualified employees as originally required (P.L. 2001 ch.157)</li> </ul>
September 2003	<ul style="list-style-type: none"> <li>Added a payment rate of 80% for 10 years for qualified businesses that are also qualified for PTDZ benefits (P.L. 2003 ch.451)</li> </ul>
September 2009	<ul style="list-style-type: none"> <li>Adjusted definition of base level of employment for certain types of businesses under specific circumstances (P.L. 2009 ch.21 and ch. 461)</li> </ul>
October 2013	<ul style="list-style-type: none"> <li>Allowed a qualified business to assign their ETIF benefits to FAME to secure loans (P.L. 2013 ch.67)</li> </ul>
October 2015	<ul style="list-style-type: none"> <li>Adjusted the definition of qualified employees to include call center employees in Aroostook and Washington counties (P.L. 2015 ch.368)</li> </ul>

Source: OPEGA review of legislative and rule histories.

Other changes affected the minimum number of new jobs that a business is required to create before becoming eligible to claim ETIF benefits and how a business's base level of employment is calculated. The ETIF Program originally required creation of 15 jobs before benefits could be claimed, but in 2001 the minimum number of new jobs was reduced to five. The calculation of employment baselines was adjusted in 2009 in connection with two provisions introduced to the PTDZ Program allowing certain types of businesses in specific situations to be eligible for increased benefits via adjusted employment baselines.

In 2009, changes were made to allow two alternative calculations of employment baselines under two unique sets of circumstances – for working waterfront businesses that suffered catastrophes and for business with multiple locations that created 250 or more jobs at one location. In 2013, a statutory change made it possible for a business to assign its ETIF benefits to FAME to secure a loan. This change made it possible for a business to access larger amounts of capital up-front via loans that could be repaid by routing ETIF payments directly to FAME. ETIF's statute was also amended in 2015 to allow call centers located in Aroostook and

Washington counties to be qualified ETIF businesses with their own unique employee compensation requirements<sup>6</sup>.

OPEGA noted that DECD's state agency rules for the ETIF Program have not been updated to reflect the substantive statutory changes to the program made since 2009. See Recommendation 9.

## Administration of the ETIF Program

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ETIF is jointly administered by DECD and MRS. DECD certifies program participants and processes annual reports while MRS approves and makes annual payments to businesses.

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The ETIF Program is jointly administered by DECD and MRS. DECD is responsible for business outreach, certification and decertification of participants, and the collection and processing of annual reports. MRS is responsible for approving and making program payments, and for conducting audits of program participants as needed.

### Business Outreach and the ETIF Application Process

DECD outreach staff proactively contact businesses to make them aware of State programs and other resources that could support their business goals. According to DECD, about 75% of businesses find out about the ETIF Program through this kind of networking. During these contacts, businesses receive information about the benefits and requirements of the ETIF Program to help them determine whether they might want to participate. DECD also provides program information and application materials on its website.

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To apply for ETIF certification a business must submit a "but for" letter and a completed application. The "but for" letter is the business's attestation that the development project the ETIF application is based on would not go forward "but for" the program's benefits.

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The ETIF application process is detailed in DECD's State agency rules and is structured around the statutory requirements for certification in the program. The process requires an interested business to submit a "but for" letter and a completed application form to DECD.

In the "but for" letter, an applicant attests that the development project their ETIF application is based on would not go forward "but for" the program's benefits. DECD requires "but for" letters to contain very specific language in order to ensure applicants meet requirements for certification under Title 36 § 6756(1)<sup>7</sup>. Applicants are provided with a template for the letter which includes the required language and a few blanks for applicants to fill in. DECD reports that they strongly encourage businesses to use the template, and carefully scrutinize any deviation from the template language to make sure the statutory requirement is still met.

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<sup>6</sup> Compensation for qualifying ETIF employees is generally required to exceed the annual per capita personal income in the county. However, call centers in Aroostook and Washington counties in their first year of certification must provide qualifying employees with wages that exceed 70% of the average wage derived from all counties except Cumberland and York. Wages must exceed 80% of the same average in the second year of certification and must exceed 90% in the third year of certification.

<sup>7</sup> Businesses have typically applied for both the ETIF and PTZ Programs simultaneously and through one joint application, so DECD also seeks to ensure the "but for" letters they receive meet the PTZ "but for" requirement in Title 30-A § 5250-I(17)(A).

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DECD has used a joint application for the PTZDZ and ETIF programs until recently. Almost all businesses that apply for one program apply for both.

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One of the determinations DECD must make is that the proposed project will not result in substantial detriment to existing businesses in the State. OPEGA found this statutory mechanism to be ineffective.

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In 2016, the Commissioner of DECD and the State Economist both said they were unable to imagine a business expansion that would not contribute enough to the economy of the State to overcome any potential detriment to existing business.

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A business may submit an ETIF application at any time during the year, but only applications received prior to December 1<sup>st</sup> will be certified for that calendar year. For example, an application received after December 1, 2013 would be certified for 2014 rather than 2013. DECD’s tax incentive group provides assistance to any business that needs help completing or filing its application. After applications are filed, the tax incentive group is also responsible for reviewing them to ensure that they are complete and that the proposal meets ETIF’s statutory requirements. Applications that pass the tax incentive group’s review are forwarded to DECD’s Commissioner for final approval.

**ETIF Certification**

Under Title 36 § 6756, an ETIF applicant may only be certified if DECD’s Commissioner finds that:

- 1) the project described in the application would not go forward without ETIF certification; (This is often referred to as the “but for” requirement).<sup>8</sup>
- 2) the project described in the application will make a contribution to the economic well-being of the State; and
- 3) the project described in the application will not result in a substantial detriment to existing businesses in the State, or if it will, that this detriment is outweighed by the project’s contribution to the economic well-being of the State.

When interviewed in 2016, the former Commissioner of DECD reported that he was already familiar with projects by the time they came for his approval. In addition, he said that since the DECD staff had fully reviewed the applications and previously addressed any issues with them, he has never had to deny a certification. In the event that an application is denied, state agency rules<sup>9</sup> require unsuccessful applicants to receive written explanation of the reason for the denial and allow an applicant 10 days from receipt of the rejection letter to appeal the decision.

As part of ETIF certification, the Commissioner submits a form to the State Economist requesting input as to whether each proposed ETIF project would make an economic contribution to the State or might pose a substantial detriment

Some of the information businesses are required to provide on the joint PTZDZ/ETIF application includes:

- business name and location(s);
- sectors in which the business operates or plans to operate;
- a description of the planned qualified business activity;
- ownership information for pass-through entities;
- current employment statistics; and
- goals for future employment and investment in the project.

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<sup>8</sup> The PTZDZ Program also has a “but for” provision under Title 30-A § 5250-I(17) requiring businesses to demonstrate that their establishment or expansion of operations would not occur within the State absent the availability of the PTZDZ benefits. P.L. 2017, ch. 440, § 1, passed in the summer of 2018, added the requirement that PTZDZ applicants provide, “at a minimum, a signed and notarized statement” supporting their claim that their project would not move forward absent PTZDZ benefits. The slight variation between the ETIF and PTZDZ “but for” provisions is often overlooked since the two programs are so closely linked, often used in combination, and even had shared applications up until recently.

<sup>9</sup> State Agency Rules 19-100 Chapter 400 § 3.

to existing businesses. OPEGA interviewed the State Economist and DECD’s Commissioner in 2016 to understand how economic contributions or potential detriments to existing businesses were assessed. We found that there was no specific process or analysis used as the basis of this assessment because an economic contribution was a foregone conclusion in their view. They both stated they could not imagine a situation in which the economic contribution from a new business expansion would not be substantial enough to outweigh any potential detriment to existing businesses. As a result, OPEGA found that the statutory economic contribution requirement and substantial harm prohibition are not effective. See Recommendation 5 for further discussion.

Establishment of ETIF Payment Rates

During initial certification, DECD’s tax incentive group determines each business’s ETIF rate based on the LMA where the business is physically located. The payment rate for a business with multiple physical locations is set based on the LMA of the location where the qualified employment growth is expected. In rare cases, a business may expect employment growth in multiple LMAs as part of a single ETIF certificate and may have different payment rates associated with the employees in each LMA. The rate also varies depending on whether the business is an ETIF-only participant or also participates in PTDZ.

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Businesses may be eligible for an ETIF rate varying from 30% to 80% depending on whether they are also PTDZ certified and on unemployment rates in their LMAs at the time of application.

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The ETIF payment rate established at certification applies for the first five years of the 10-year certification period<sup>10</sup>. The exception to this rule is Tier 1 PTDZ certified businesses, which are eligible for the 80% ETIF rate for all 10 years of certification. For others, including PTDZ Tier 2 businesses and ETIF-only businesses, DECD reevaluates the ETIF rate in the sixth year of certification. This reevaluation is based on the average unemployment in the LMA for the 12 months prior. For example, an ETIF-only business in an LMA with unemployment lower than the State average at the time of certification would qualify for a 30% ETIF rate. However, if the LMA unemployment rate moved above the State average unemployment by the business’s sixth year of certification, then the business would qualify for a higher ETIF rate – either 50% or 75% – for its remaining years of certification.

Table 2. PTDZ Tiers as of November 2018	
TIER 1	TIER 2
<ul style="list-style-type: none"> <li>• All locations outside of York and Cumberland counties; and</li> <li>• Locations in York or Cumberland counties with municipal unemployment 15% higher than LMA unemployment; and</li> <li>• The Town of Berwick, and pilot projects in the Downeast Region, Washington County and the City of Sanford.</li> </ul> <p><b>Tier 1 certifications will become unavailable when PTDZ terminate at the end of 2021.</b></p>	<ul style="list-style-type: none"> <li>• Locations in York or Cumberland counties that do not qualify for Tier 1.</li> </ul> <p><b>Tier 2 certifications are no longer available after 2013 and benefits will expire at the end of 2018.</b></p>
Source: Title 30-A § 5250-J(3-A).	

<sup>10</sup> ETIF businesses that qualify for the 80% rate and that are located in Tier 2 PTDZ locations only receive the 80% rate for five years. For the remainder of their ETIF certifications they are eligible for a lower ETIF rate based on the unemployment rates of their LMAs.



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The ETIF employment baseline acts as the bar above which qualifying employees must be added.

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Establishment of Employment Baselines

The ETIF employment baseline acts as the bar above which five additional qualifying employees must be added in order for a certified business to be eligible for ETIF benefits. Calculation of the baseline is set in statute under Title 36 § 6753(4) and is generally based on the total employment of each ETIF applicant in the period leading up to the date of application.

**Baseline is whichever is greater:**

$$\left[ \frac{\text{sum of total employment at the end of each quarter of the } \mathbf{1} \text{ calendar year before application}}{4} \right] \text{ OR } \left[ \frac{\text{sum of total employment at the end of each quarter of the } \mathbf{3} \text{ calendar years before application}}{12} \right]$$

Statute does allow for two types of adjustments reducing the employment baseline for a business that is jointly PTDZ and ETIF certified. These adjustments may be used by a working waterfront business that experiences a catastrophe or by a multi-location business that creates at least 250 new jobs at one location.

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ETIF statute is silent on transfers in business ownership, so DECD has adopted internal protocols for these situations.

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OPEGA found that ETIF’s statute and rules are silent with regard to a transfer in the ownership of a certified business. As a result, it is unclear how employment baselines should be established when ownership is transferred. Absent statutory guidance, DECD has adopted internal protocols for these situations. When a certified ETIF business changes ownership, DECD does not automatically consider the new entity a new ETIF applicant with a baseline of zero. Instead, for most businesses that transfer ownership, DECD requires the new owner to adopt the prior owner’s existing ETIF certificate and associated baseline. In cases where there was no existing ETIF certificate, the Department says it typically calculates the employment baseline based on actual employment levels leading up to certification, including the period prior to the transfer of ownership, if applicable.

DECD’s internal protocol for assigning baselines to transferred businesses recognizes that although a new owner may be a new, legal entity in Maine, the jobs at the business existed prior to the change in ownership. However, in the past, DECD has occasionally allowed exceptions to its own internal protocol when it believed a transferred business was facing financial jeopardy and that jobs were at risk or had recently been cut but may be reinstated. Under these special circumstances, DECD has occasionally allowed the new owners of a pre-existing Maine business to have a new 10-year certificate with a base employment level of zero, regardless of whether the physical business was associated with an existing ETIF certificate.

OPEGA notes that the lack of guidance in rule and statute for establishment of employment baselines when businesses change ownership creates the risk of inconsistent treatment of ETIF businesses. DECD’s current internal protocol does set employment baselines for transferred businesses in a manner that ensures ETIF qualified jobs are “net new” to the State as required by statute. Codifying this protocol in rules or statute would ensure consistency over time and clarify expectations for potential applicants. See Recommendation 7 for more information.

## DECD's Processing of ETIF Annual Reports and Claims for Benefits

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Businesses participating in the ETIF Program are required to report to DECD annually to support their claim for benefits.

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Once a business is ETIF certified, it is required under Title 36 § 6758 to provide a report to DECD by April 15th of each year<sup>11</sup>. Reports describe activity that occurred in the prior calendar year. These reports allow DECD to monitor whether a business is meeting the requirement to hire at least five new employees within the first two years of certification. They also serve as the business's claim for program benefits for the year.

ETIF annual reports require general information about a business's physical location and total employment in addition to the following specific data for every in-state employee, including all of the business's employees that are not net new and do not meet ETIF requirements:

- position name;
- whether the position is full-time or part-time;
- employee name or ID number;
- employee hire date and separation date;
- employee gross earnings amount with and without benefits;
- whether the employee has access to health or retirement benefits that meet ETIF minimum requirements;
- whether the employee is being claimed as a qualified employee;
- employee withholdings; and
- amount of ETIF payment the business is requesting based on the individual employee's withholdings.

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ETIF's annual reporting process is labor intensive for DECD and for businesses participants.

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The ETIF reporting season is a busy time for DECD staff. They send multiple reminders to businesses about reporting requirements, distribute detailed reporting guidance, and provide personal reminders and support for businesses that encounter challenges in filing annual reports. DECD staff interviewed by OPEGA described these efforts as important customer service functions that facilitate a business's fulfillment of the reporting obligation and access to program benefits for which they are eligible.

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ETIF annual reports are processed via an old, cumbersome, database known as BDTI. The database performs some automated error checks on reported data, but DECD staff must still review each report manually.

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Businesses file ETIF annual reports via a spreadsheet template that DECD makes available online. Completed spreadsheets are submitted to DECD electronically and are received by DECD's BDTI database. When businesses attempt to upload spreadsheets to BDTI, the database performs automated error checks and prevents the upload if errors are found. These error checks include testing the annualized income derived from employment against the per capita county income, ensuring correct county codes, ensuring that employees counted as qualified have the appropriate codes indicating they meet the full-time employment, health insurance and retirement requirements. The database also ensures that the number of qualified employees in the file is less than, or equal to, the total number of employees minus the base level of employment.

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<sup>11</sup> Businesses may be granted reporting extensions on an individual basis at DECD's discretion.

Once any identified errors are corrected, each business can upload its information and DECD staff can begin their review. DECD's review focuses on verifying the accuracy and appropriateness of reports in order to ensure that only qualified employees above the baseline are included in the calculation of a business's ETIF payment. In review of the Department's written processes, and discussions with DECD staff, OPEGA learned that DECD's review includes:

- checking for duplicate positions;
- requesting more information about employees with zero withholding;<sup>12</sup>
- evaluating whether the reported annualized income derived from employment is reasonable given the reported earnings, hire dates and separation dates for each employee; and
- ensuring businesses with multiple certifications are not counting the same qualified employees or positions for more than one project.

The Department may also request further information from a business if a comparison of reported employees with prior year information shows an unusual shift between qualified and unqualified positions.

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After DECD has finished reviewing ETIF reports, Department staff provide copies of the reports to MRS.

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When suspected errors or inconsistencies are identified, DECD's staff works with a business to get additional information or to have corrected data uploaded to the BDTI database when necessary. After the reported data has been verified by DECD, the Department sends copies of the individual annual reports to MRS with a summary of the requested payments for the year. DECD has a goal of providing the verified reports to MRS by May of each year, although individual reports from businesses that struggled to meet the reporting deadline are occasionally sent later.

### **MRS' Approval and Payment of ETIF Benefits**

MRS's primary role in administering ETIF as prescribed by rule and statute is to authorize and provide ETIF payments to eligible businesses. This process begins when MRS receives the annual reports from DECD. MRS verifies that businesses have been remitting withholdings, and MRS staff perform a few additional checks to confirm that businesses are eligible for the amounts they have requested. If MRS determines that a business is eligible for less than was requested, a notice of adjustment or denial is sent to the business. MRS estimates this occurs in less than 1% of cases. The few businesses that do have their requested ETIF payments adjusted or denied may appeal the MRS decision.

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MRS reduces a business's ETIF payment if the business has outstanding debts to the State. ETIF payments may also be reduced to compensate for an overpayment in a previous year.

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Once MRS has reviewed the ETIF reports and made any necessary adjustments the ETIF payments are ready to be approved. After approving the payments, MRS also identifies any outstanding debts a business may owe to the State and reduces the ETIF payment to cover any such debts. An ETIF payment may also be reduced to compensate for an overpayment in a previous year. However, most ETIF certified businesses have no outstanding debt to the State or past overpayments and are able to receive their ETIF payments in full.

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<sup>12</sup> Employees with zero withholding are not qualified, and may not count toward the base level of employment if they are out of state employees or contract employees who receive a form 1099.

MRS staff record the final amounts approved for businesses, along with any offsetting amounts on a spreadsheet. This manual recordkeeping is necessary because neither the ETIF requests nor the ETIF payments are processed through MRS’ tax system. However, this type of highly manual record keeping increases the risk of errors in program records and payments. OPEGA did not perform a detailed review of all MRS ETIF records, but we did identify a small number of overpayments and erroneous records in the course of our data review. See Recommendation 10 for more information.

<b>Program Year</b> calendar year when qualified employees are employed	<b>Reporting Year</b> calendar year when report is submitted	<b>Fiscal Year</b> fiscal year when payment is made
2010	2011	2012
2011	2012	2013
2012	2013	2014
2013	2014	2015
2014	2015	2016
2015	2016	2017
2016	2017	2018

Once approved by MRS, payments are processed via the State’s AdvantageME vendor payment system. In order to receive payment businesses must have previously registered as vendors with the State. Under Title 36 § 6758(3) ETIF payments must be sent to businesses before July 31st of each year. As shown in Table 3 this means that a business report presented to DECD in April of 2012, for example, would describe activity that occurred during calendar year 2011 and would be the basis for a payment that would be made during fiscal year 2013.

MRS may conduct an audit of a qualified business under ETIF statute. If audit results show an overpayment, it is applied against future ETIF benefits unless MRS determines that the overpayment was the result of fraud. In such a case, MRS may disqualify the business from receiving any future ETIF benefits.

When there are no future benefits expected because the business is at the end of its eligibility or no longer meets the program’s requirements, the qualified business is liable for the amount of the overpayment. OPEGA notes that MRS has discovered some overpayments in the course of processing ETIF payments in the past. Those overpayments were recovered.

## Similar Programs Offered by Other States

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OPEGA researched programs in other states and found 10 programs that were similar to ETIF. The requirements and benefits for each of these programs is detailed in Table 4.

Other states’ benefits levels are difficult to compare directly due to the varied ways in which they are calculated. However, when they are compared based on the value of benefits as a percent of increased payroll costs, it appears that Maine’s ETIF is toward the middle of the other states identified.

ETIF’s minimum job creation threshold and wage criteria are comparable as well. Some states use percentage of federal minimum wage as the threshold for income and some increase benefit levels when certain job count and quality thresholds are exceeded. ETIF’s 10-year time span is also similar to the other states. In some states, the duration of benefits may be extended when certain conditions are met.

<b>Table 4. Active Programs Similar to ETIF in Other States</b>		
<b>State</b>	<b>Requirements</b>	<b>Benefits</b>
<b>Delaware</b> New Economy Jobs Program	Must create 50 new jobs with at least \$100K annual salary or create 200 new or retained jobs with at least \$70K annual salary.	Payment equal to 25% of total withholding for new employees plus 0.075% for each new employee in excess of 50 or plus 0.050% for each employee in excess of 200. Available for up to 10 years.
<b>Florida</b> Qualified Target Industry Tax Refund Program	Must create increase employment by 10% or create at least 10 new jobs. Wages must be 115% of the average private sector wage in the area. Local buy-in required*.	Tax credit of \$3,000 or \$6,000 per new job depending on business location. Benefits available annually until aggregate approved disbursement has been reached. Additional amounts available under special circumstances.
<b>Indiana</b> EDGE Program	Each project's required capital investment and employment are individually negotiated based on a cost-benefit analysis. Jobs must be full-time and permanent. Local buy-in required*.	Tax credit is a percentage (not to exceed 100%) of withholdings from new jobs created. Percentage is individually negotiated per project. Available for up to 10 years.
<b>Iowa</b> New Jobs Tax Credit	Businesses new to the state must create at least 1 job. Existing business must increase employment by at least 10%. Businesses must also be part of Iowa's 260E job training program.	Tax credit equal to 6% of gross wages for each new job in excess of the minimum requirement. Available for up to 10 years.
<b>Kansas</b> PEAK Program	Must create, or retain, at least 5 jobs in non-metro counties or 10 jobs in metro counties with wages above county thresholds or industry average and at least 50% of health insurance premiums paid by employer. All other jobs in the business must be more than the average industry wage in aggregate.	Payment equal to 95% of withholdings for qualified jobs created. Available for up to 10 years depending on how the average wage compares to the country threshold.
<b>Kentucky</b> Business Investment Program	Must create at least 10 new fulltime jobs with higher job creation requirements negotiated for some businesses. Wages must be at least 125% of federal minimum, or at least 150% of federal minimum for enhanced benefits. Must invest \$100K.	Tax credit equal to 4% of new employee gross wages or 5% for enhanced benefits, up to 100% of tax liability. Available for up to 10 years, typically, or 15 years for businesses in designated locations.
<b>Kentucky</b> Small Business Investment Credit	Must create at least 1 new job with wage of at least 150% of federal minimum. Must invest at least \$5,000 in qualifying equipment. Only available to businesses with fewer than 50 employees.	Tax credit of up to \$3,500 per new job created with a maximum of \$25K per business. This is a one-time tax credit provided one year after new jobs have been filled and investment has been made.
<b>Louisiana</b> Quality Jobs Program	Businesses with fewer than 50 employees must create 5 new, full-time jobs with annual payroll of at least \$225K. Businesses with more than 50 employees must create 15 new, full-time jobs with annual payroll of at least \$675K. Health plan must be provided and wages must be at least \$18/hour. Only certain business sectors are eligible.	Payments of up to 6% of gross payroll beginning in July 2018 (previously payments were based on 80% of gross payroll). Other sales tax benefits also available. Available for up to 10 years.
<b>Missouri</b> Missouri Works	Multi-tier program. Three program tiers require a minimum of either 2 or 10 new jobs depending on business location. Required wages also vary by location from at least 80% to at least 90% of county wage. Two additional program tiers require at least 100 new jobs with minimum wage requirements of 120% or 140% of county wage. All participating businesses must pay at least 50% of health insurance premiums.	Tax credits equal to 100% of the amount of new employee state tax withholding businesses in tiers requiring up to 10 new jobs. Credits equal to 6% to 7% of gross, new wages for businesses in the program tiers requiring more than 100 new jobs. Available for 5 years for businesses new to the state and 6 years for established businesses.

Table 4. Active Programs Similar to ETIF in Other States		
State	Requirements	Benefits
North Carolina Job Development Investment Grants	Approved projects must result in a net increase in a business’s employment in the state and a required number of jobs may be set at the discretion of the program’s administering agency. Businesses must pay wages meeting county average wage requirements and must pay at least 50% of health insurance premiums. Local buy-in required for some locations*.	Grant equal to a percentage of new employees’ withholdings. The percentage is set by the administering agency based on a number of factors. Businesses receive between 75% and 100% of the total grant amount, depending on their location. The remainder of the grant amounts is contributed to a state infrastructure account. Available for up to 12 years for most projects and up to 25 years for huge projects.
* “Local buy in required” indicates that in addition to other requirements for the incentive, projects must have some minimum level of investment from another group such as local government or private entity. Sources: Evaluation reports, state laws, and websites of economic development entities from other states.		

In researching other states, OPEGA noted that many seemed to have similar underlying goals, but use varied design elements to achieve them. A sampling of the varied approaches follows.

Targeting Geographic Areas with Less Development or Higher Unemployment

Programs similar to ETIF in other states often target geographic areas with less development or with higher unemployment by offering higher benefits to those businesses in those areas or by reducing program requirements for businesses in those areas.

ETIF’s benefit structure, prior to the PTDZ 80% benefit, provided a greater benefit to businesses that located or expanded in areas of higher unemployment. OPEGA found that other states also targeted specific geographic areas using a number of different approaches. Florida’s Qualified Target Industry Tax Refund Program, for example, is structured similarly to ETIF but offers double the benefit for businesses in areas where the state wants to encourage economic development. Other programs such as the Kansas PEAK Program and Missouri WORKS Program reduce the required number of jobs for businesses locating in less economically developed regions.

North Carolina’s Job Development Investment Grant Program takes a different approach that ensures less developed parts of the state benefit even if business participants locate in the more developed areas. The program does this by calculating the total benefits each participating business is eligible for, and then distributing a portion of that total amount to an infrastructure improvement fund earmarked for less developed areas.

Linking Benefits to Job Creation

The ETIF Program is designed to pay only for jobs that have already been created and to pay an amount that is proportional to the wages. This appears to be a standard practice in other state programs designed to encourage jobs. All similar programs reviewed provided benefits only after jobs had been reported. Most paid based upon withholding amounts or wage amounts with only Florida’s QTI and Kentucky’s Small Business Investment Credit providing lump sum amounts per job.

Targeting Benefits to Businesses that Would Not Otherwise Expand or Locate in the State


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OPEGA found that other states with programs like ETIF also try to limit program funding to projects that wouldn't occur without the incentive. However, few use attestation provisions like Maine's "but for" requirement.

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OPEGA found the desire to limit funding from economic development programs to projects that wouldn't occur without the incentives to be common among other states with similar programs. However, few of these states currently have similar attestation provisions in place. Evaluations of those that do have these requirements find them difficult to enforce or not meaningful. In lieu of "but for" requirements, some other states have tackled this challenge by limiting program benefits to a more specific subset of businesses. North Carolina takes a different approach. That state performs in-depth analysis of each business project up-front to assess how benefits from the state would impact the business's behavior and whether providing benefits would have a positive net impact on the state budget.

## Assessing the Likelihood That ETIF Affected Business Behavior —

The question of whether a payment that is intended as an economic incentive actually incents a behavior, or whether that behavior would have occurred anyway, is central to determining the effectiveness of any State economic development program. If job creation supported by State programs would have occurred even without the programs' benefits, then those State funds were not necessary to the job creation and could instead have been returned to taxpayers, spent on other government priorities, or spent on other economic development projects. The proportion of projects that would occur even without program benefits is difficult to determine.

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OPEGA finds that ETIF's "but for" provision is weak and is not adequate to support the assertion that if it were not for ETIF benefits, the jobs that have qualified under ETIF would not exist. However, determining the proportion of ETIF jobs that would exist even without the program's benefits is difficult.

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The existence of the "but for" provision in ETIF's statute creates the perception that none of the jobs associated with ETIF would have been created if the program didn't exist. If accurate, this would make analysis of the program's benefits substantially easier, but this perception is unlikely to be accurate for a few reasons. One reason is that the majority of the jobs were associated with one or more other economic development or tax incentive programs that could have been wholly, or partly, responsible for the job creation. Another reason, suggested by stakeholders, is that ETIF benefits are only one of the factors affecting business location decisions among other factors, such as access to infrastructure and labor availability and quality. As a result, OPEGA cannot conclude that the existence of the "but for" requirement proves that the availability of ETIF benefits caused businesses to expand in Maine and consequently create new jobs. See Recommendation 4.

Survey and Econometric Methods to Evaluate the Impact of Incentives on Business Decisions

OPEGA reviewed academic literature and other states' evaluations to identify accepted methods of estimating the likelihood that business decisions are affected by tax incentives. We found general agreement about the difficulty of estimating the proportion of projects that would not occur without an incentive, but we found no firm consensus on what the proportion might be. However, we did find that many state program evaluators and academic researchers used econometric techniques or surveys of program participants to estimate the effect of tax incentives on business behavior.

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Based on our review of academic literature and other states' evaluations of tax expenditure programs we estimate that up to 13.1% of ETIF job creation may have been due to the availability of ETIF benefits.

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In reviewing other states' evaluations we found that surveys of program beneficiaries can provide information about the impact of such programs on location and expansion decisions. However, all surveys are subject to possible bias because respondents may subconsciously answer with their own self-interests in mind or because the group of respondents may not represent the population we seek to understand. In addition, the surveys OPEGA found of tax incentive programs generally did not take into consideration the magnitude of programs' benefits in comparison to businesses' investment projects. This ignores the simple fact that a more substantial benefit has the potential for greater impact on the profitability of a project and is therefore more likely than a smaller financial benefit to influence a project decision.

The econometric method OPEGA used in this evaluation does consider the magnitude of financial benefits in estimating the degree to which business decisions are impacted by changes in tax policy. This work has been criticized by some, including Jennifer Weiner, of the Federal Reserve Bank of Boston, as overstating the effect of changes in tax policy on business behavior. However, critics have not offered alternate approaches. Recent academic papers on this method estimate that, on average, an incentive which lowers costs by 2% of wages would affect approximately 10% of businesses' location or expansion decisions<sup>13</sup>. ETIF's benefits provide an average 2.6% reduction in a business's cost of the wages of new, qualified employees. When we substitute this 2.6% cost reduction for the 2% cost reduction in the ratio above, the result indicates that ETIF's benefits could be expected to affect approximately 13.1% of participant businesses' location or expansion decisions.

## Estimating State Impacts Attributable to ETIF

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### Modeling Direct and Indirect Impacts

OPEGA estimated three performance measures using the Maine-specific IMPLAN economic modeling software to capture both the direct and indirect economic impacts attributable to the ETIF Program. These measures include net impact on the State budget, impact on the State tax base, and change in Gross State Product.

#### IMPLAN Model

Input-output models such as IMPLAN rely on detailed information about the economy to estimate how much activity in one industry is supported by the activities of other industries. Information about economic activity associated with the program, reported by recipient firms, such as jobs created or dollars spent on construction projects, is plugged into the model, and from this IMPLAN summarizes estimated impacts in the following categories:

- Employment – representing a mix of full and part-time jobs that varies by industry.

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OPEGA used economic impact modeling to derive some performance metrics. The Maine-specific IMPLAN model captured both direct and indirect economic impacts associated with the Maine ETIF Program.

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<sup>13</sup> A summary of the literature OPEGA reviewed is in Appendix B.



- Labor income – representing a combination of employee compensation i.e., wages and salaries and benefits provided to workers.
- Value added – more commonly known as gross domestic product or, in the case of this analysis, gross state product.
- Output – representing a firm’s gross sales or receipts, and consists of value added and the value of intermediate inputs.
- Associated Tax Revenue – from payroll taxes; taxes on firm production, imports, sales, and profits; and personal income tax and property tax, and other taxes.

### Model Inputs and Results

Estimating the total economic impact of the ETIF Program required determining program inputs for the Maine model to analyze. These inputs included the number of incremental jobs associated with program benefits.<sup>14</sup> OPEGA collected the inputs by analyzing ETIF records obtained from both MRS and DECD, including certification applications, annual reports submitted by businesses, and records of approved program payments. Each job reported by a business was counted as a whole job although some may have been filled for less than 12 months.

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Input data for the economic model was obtained from OPEGA’s analysis of DECD and MRS records.

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OPEGA did not include ETIF participants’ invested amounts as inputs to IMPLAN because sufficiently detailed investment data was not available. Consequently, our results may somewhat underreport the economic growth associated with ETIF projects. However, though invested amounts would typically be included in economic modeling of business projects, jobs are the primary driver of economic growth in the model and investments are not required to be made under ETIF.

OPEGA also did not adjust the model inputs to reflect the degree to which jobs supported by ETIF may also have been supported by other business incentive programs. ETIF participants potentially have access to benefits from other programs such as the Business Equipment Tax Reimbursement (BETR) and Business Equipment Tax Exemption (BETE) Programs, the High Technology Investment Tax Credit, the Maine New Market Capital Investment Credit (NMTC), and others. Ideally, OPEGA would have been able to assign a portion of the new jobs created in association with each program by some method like calculating the benefits derived from each program as a percent of the total benefits derived from all programs supporting the same business project. However, data about businesses’ participation in all of these programs was not readily available because there is currently no comprehensive State database with this information.

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<sup>14</sup> Because pilot projects are authorized only to a very limited degree, and operate under such a different set of requirements, we made the decision to exclude any certified pilot projects from our inputs. Title 30-A § 5250-J(3-A)(E), in PTDZ statute, authorizes pilot projects in specific circumstances, and in some cases, excludes those projects from the requirements of the qualified business definitions under § 5250-I(16)-(17) or from the qualified employee definitions under § 5250-I(18). Although these pilot projects are authorized under PTDZ statute, they also qualify for ETIF benefits because Title 36 § 6754(1)(D) provides ETIF benefits at an 80% rate for all PTDZ certified businesses.

For this analysis OPEGA included as inputs all jobs claimed under ETIF, even if they were also claimed under PTDZ or another State program. As a result, our results likely overstate the impact of ETIF alone.

Given the interconnected nature of ETIF and the PTDZ Program, it is particularly likely that many of the same jobs are supporting businesses' claims to benefits under both programs. In fact, the statutory design of the two programs seems to encourage businesses to use the programs together. We considered several approaches to allocating jobs created between the two programs. However, we were unable to allocate jobs with any accuracy because a reliable allocation requires knowledge of the full value of benefits under each program and the full value of PTDZ benefits per business is currently unknown<sup>15</sup>.

**Table 5. Economic Impact Modeling for ETIF Program, Key Inputs and Outputs 2010 – 2016**

	2010	2011	2012	2013	2014	2015	2016
<b>INPUTS</b>							
# of Direct Jobs Attributable to ETIF	775	819	930	1,072	1,144	1,257	1,194
<b>OUTPUTS</b>							
# of Estimated Indirect Jobs in Supply Chains Attributable to ETIF	894	939	928	992	973	1,033	976
Estimated Increase in Maine State Tax Revenue Attributable to ETIF (in millions)	\$12.94	\$12.18	\$12.84	\$12.40	\$14.29	\$15.60	\$16.14
Estimated Increase in State and Local Tax Revenue Attributable to ETIF (in millions)	\$23.22	\$21.55	\$22.67	\$21.44	\$25.34	\$27.63	\$28.93
Estimated Maine Gross State Product Generated Attributable to ETIF (in millions)	\$206.61	\$205.43	\$219.20	\$229.03	\$238.60	\$262.72	\$258.53

See Appendix A for more detail about the assumptions underlying OPEGA's economic modeling and the alternative assumptions we tested.

## Past Actual and Future Estimated Program Costs

### Direct Costs through Fiscal Year 2018 and Estimated Future Direct Costs

OPEGA estimated direct costs to the State as the value of the ETIF benefits paid by the State plus the administrative costs of the program. The value of benefits paid for each program year is based on the actual payment records maintained by MRS. Both MRS and DECD provided estimates of the annual administrative costs they each incur to manage the program.

The total value of ETIF payments to businesses has grown substantially since the program's early years. According to a 1999 DECD agency report to the Legislature, ETIF payments totaled just \$160,000 in that year and were distributed to just eight participants. By comparison, payments for 2016 totaled \$13.31 million and were distributed to 135 businesses<sup>16</sup>.

<sup>15</sup> The challenges with identifying the value of PTDZ benefits were discussed in OPEGA's 2017 report on the PTDZ Program. See Table 4 on page 22 of that report for details.

<sup>16</sup> Business counts may vary slightly from figures obtained from MRS and DECD due to differences in how businesses with more than one project or more than one tax identification number were counted.

**Table 6. ETIF Summary Statistics, Program Years 1998 and 2010 - 2016**

Year of Job Creation	1998	2010	2011	2012	2013	2014	2015	2016
Fiscal Year of Payments	FY99*	FY12	FY13	FY14	FY15	FY16	FY17	FY18
Total ETIF Payments (in millions)	\$0.16	\$8.03	\$9.64	\$11.56	\$12.98	\$13.68	\$14.82	\$13.31
Number of Businesses	8	89	85	107	120	132	142	135
Average Payment	\$20,048	\$90,228	\$113,432	\$108,076	\$108,206	\$103,641	\$104,358	\$98,575

\*In fiscal year 1999 ETIF payments were made in June of the fiscal year following the year of job creation. By fiscal year 2012 payments were pushed into July which meant they were paid two fiscal years after the jobs were created.  
 Source: For 2010-2016, OPEGA analysis of data obtained from MRS and DECD. For 1998, OPEGA analysis of data from the report of the 1999 Economic Development Incentive Commission.

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Combined annual administrative costs for DECD and MRS are less than 1% of the cost of ETIF benefits.

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Administrative costs were estimated by the agencies to be approximately \$98,151 annually. Of this total, \$9,790 is associated with MRS’ administration, and the remaining \$88,361 is associated with DECD’s efforts. OPEGA did not verify the administrative costs estimated by MRS or DECD, though we do note that the estimates seem reasonable in comparison to the administrative efforts of the agencies. Total administrative costs are less than 1% of the cost of ETIF benefits and do not add significantly to the total direct cost of the program. Neither MRS nor DECD receive separate appropriations to administer ETIF. As a result, administrative costs are covered within each agency’s existing resources.

Future ETIF costs could change significantly depending on the future of the PTDZ Program. If PTDZ stops certifying new participants after 2021, as currently required by statute, participants certified in the final year could potentially receive payments at the 80% ETIF rate through 2031. The number of businesses receiving benefits at the 80% rate would shrink as 2031 approached and businesses’ 10-year certifications expired. After 2031, the 80% rate would no longer be available to any ETIF participants. This could drive total ETIF payments lower, because even if a similar number of businesses participated in the program, they would be paid at the lower ETIF rates of 30%, 50% or 75%.

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Total ETIF payments could be lower in the future if PTDZ Program benefits – including the 80% ETIF rate – expire after 2031 as currently specified in PTDZ’s statute.

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As previously reported in OPEGA’s 2017 report on the PTDZ Program, approximately 89% of business projects connected with ETIF payments in FY17 received payments at the 80% rate that is available only to participants certified in both programs. OPEGA estimated that the total FY17 ETIF payments without the increased PTDZ payment rate would have been approximately \$8.62 million instead of the \$14.8 million that was actually paid. This estimated reduction in ETIF payments assumes that all participants would have continued in the program despite the change in payment rates. However, we heard from stakeholders that some businesses would not have used the program without the 80% payment rate because the lower rates would not have made it cost-effective to proceed with their projects in Maine.

While it is difficult to imagine a drop from the 80% rate to the 75% rate making a substantial difference to the cost-effectiveness of a business project, OPEGA found that 67% of ETIF businesses receiving payments in FY17 were located in lower unemployment areas of the State and would only qualify for a 30% ETIF if it were not for the PTDZ Program. When considered in the context of a large business project with hundreds of new, qualifying employees it becomes easier to imagine an impact from this reduction in rates.

**Estimated Net Impact on State Budget through Fiscal Year 2018**

OPEGA estimated ETIF’s net impact on the State budget for FY12 – FY18 could be up to \$11.7 million, or roughly \$1.7 million per year.

OPEGA estimated ETIF’s net impact on the State budget for FY12 through FY18 could be up to \$11.7 million. The net impact on State budget was calculated by subtracting the program’s direct costs from the State budget impacts estimated by OPEGA. We estimated State budget impacts using an economic model to capture the economic ripple effects of both direct and indirect jobs connected to ETIF projects. These ripple effects include additional income and sales taxes that might be expected from new employees in ETIF businesses as well as from other in-state businesses in the supply chains of ETIF businesses.

<p><b>Direct Jobs</b> ETIF qualifying jobs created in ETIF certified businesses</p> <p><b>Indirect Jobs</b> Additional jobs supported in the supply chains of ETIF certified businesses</p> <p><b>Induced Jobs</b> Additional jobs supported by the spending of employees that fill the direct and indirect jobs</p>
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Table 7 illustrates the significant variation from year to year in the estimated net impact on the State’s budget. This variation reflects shifts in the business sectors represented in ETIF participants. The economic model used by OPEGA recognizes that some sectors have more significant in-state supply chains, and it estimates bigger economic ripple effects from growth in those sectors as a result.

**Table 7. Estimated Net Impact on State Budget Attributed to ETIF, FY12 - FY18 (in millions)**

	FY12	FY13	FY14	FY15	FY16	FY17	FY18	TOTAL
Estimated Change in State Revenue Attributed to ETIF	\$12.9	\$12.2	\$12.8	\$12.4	\$14.3	\$15.6	\$16.1	\$96.4
Actual Total Direct Cost (including administration)	\$8.1	\$9.7	\$11.7	\$13.1	\$13.8	\$14.9	\$13.4	\$84.7
Estimated Net Impact on State Budget Attributed to ETIF	<b>\$4.8</b>	<b>\$2.4</b>	<b>\$1.2</b>	<b>(\$0.7)</b>	<b>\$0.5</b>	<b>\$0.7</b>	<b>\$2.7</b>	<b>\$11.7</b>

Source: OPEGA’s analysis of data obtained from MRS and DECD.

Note: Due to rounding, combining figures in this table does not produce exact totals.

OPEGA’s estimated economic impacts for ETIF may be overstated because our analysis did not reflect reductions in other government spending that might be necessary to fund ETIF.

OPEGA’s estimated net budget impact may be slightly overstated as it does not reflect budgetary impacts associated with any adjustments to other government spending that might be necessary to fund ETIF within a balanced budget. The impact may also be overstated because we attributed jobs to ETIF that may also have been supported by other programs. We did not have data about the value of benefits ETIF participants received from other programs for any of the same jobs associated with their ETIF benefits. As a result, our net impact figures reflect all of the benefits associated with ETIF jobs, but do not reflect the full cost of those jobs from all State tax programs. Given the degree of overlap between ETIF and PTDZ, we believe it is particularly likely that many of the same jobs claimed for one may also be claimed for the other. See the appendices for more information.

**Past Estimates of Fiscal Impact Published by MRS**

MRS reports estimated revenue loss for the ETIF Program in each biennial Maine State Tax Expenditure Report (MSTER). The estimates included when the MSTER is published are based on past actual ETIF payments and MRS assumptions about future economic conditions and observations about how the program is trending. MRS also reviews the accuracy of projected future ETIF revenue losses and makes adjustments in subsequent MSTER editions if they believe their estimates can be improved.

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MRS publishes estimates of future ETIF costs in its biennial Maine State Tax Expenditure Report.

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OPEGA finds MRS' method of estimating future ETIF costs to be reasonable. However, we also note that when the estimates are presented in the MSTER they are reported in one lump sum with estimates for two other unrelated programs. These two programs are the Loring Job Increment Financing Program under Title 5 §§ 13080-0 – 13080-U and the Brunswick Naval Air Station Job Increment Financing Program under Title 5 § 13083-S-1. Including those two programs adds between \$707,000 and \$1.4 million per year to the fiscal estimates reported in the MSTER for ETIF. OPEGA finds that presenting the estimates in such a manner makes the projected cost of each program less clear. See Recommendation 9.

## Assessing Impact on Intended Beneficiaries

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ETIF's statutory design ensures that only for-profit businesses that create new quality jobs can receive program benefits.

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The primary intended beneficiaries of the ETIF Program are for-profit businesses that create new, quality jobs. The secondary intended beneficiaries are job-seekers in the State. The degree to which OPEGA finds each intended beneficiary actually benefits from the program is discussed below.

### **Intended Beneficiary: For-profit Businesses that Create New Quality Jobs**

OPEGA found that some ETIF design elements work together to ensure that benefits flow only to qualifying businesses that create the required number of new, quality jobs. One element is ETIF's statutory definition of "qualified businesses" as for-profit businesses, excluding public utilities and most retail businesses<sup>17</sup>. ETIF benefits are paid only after hiring occurs and businesses remain eligible for program benefits only if they continue to meet program requirements. Additional design elements clearly define qualifying employees and ensure only quality jobs count toward businesses' hiring requirements.

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From fiscal years 2012 through 2018, 208 unique businesses received ETIF payments totaling \$84 million.

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Another critical element is the statutory requirement for certified businesses to report the number of qualified employees, the state income taxes withheld, and other information to DECD annually. This data allows DECD staff to verify that the reported employees qualify and that the amount of ETIF benefits requested are justified. OPEGA noted that while this detailed reporting (outlined beginning on page 13) helps assure that unqualified businesses do not receive benefits from the program, the level of effort required to comply could potentially discourage some eligible businesses from participating.

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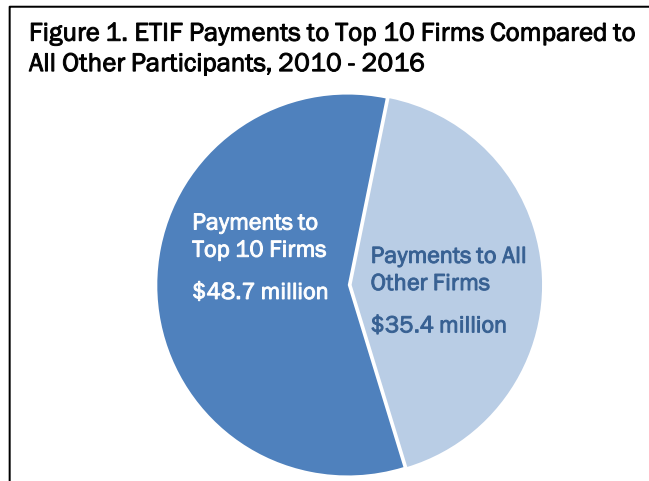
58% of all ETIF benefits between fiscal years 2012 and 2018 went to the ten ETIF businesses with the highest payments.

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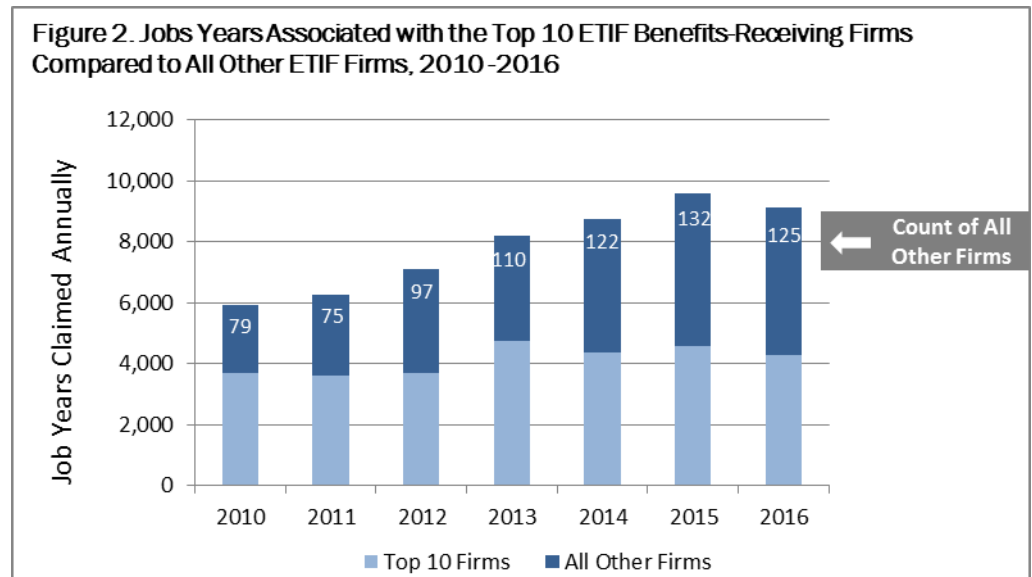
From fiscal years 2012 through 2018, a total of 208 unique businesses received ETIF payments totaling \$84 million. Annually across that period, the count of unique businesses receiving payments ranged from a low of 85 to a high of 142, and the average payment to businesses ranged from a low of \$90,228 to a high of \$113,431. As shown in Figure 1, approximately 58% of all ETIF benefits paid by the State between fiscal year 2012 and fiscal year 2018 went to the ten businesses receiving the highest payments.

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<sup>17</sup> Certain retail entities may qualify. See footnote 2 on page 4 for details.



Over that same period, the ten businesses with the highest payments claimed approximately 53% of all job years associated with ETIF payments made and represented just 9% of the total annual business participants on average.



OPEGA also observed that in very limited circumstances ETIF benefits have been provided to businesses that have not technically hired any net new employees. This has occurred only in rare circumstances when the availability of ETIF benefits appears to have played a role in allowing financially troubled businesses to continue under new ownership, thereby retaining at least some of the jobs pre-existing in the State that would have otherwise been lost. OPEGA found that \$23.6 million in ETIF payments were made to financially troubled businesses like these between FY12 and FY18. These payments account for 28% of all ETIF payments and 20% of job years claimed over that period.

**Job years** are frequently reported for the ETIF Program, rather than unique job counts. Job years measure the number of years that jobs qualify for the program. For example, five jobs that each qualify for 10 years are counted as 50 job years.

OPEGA observed that in a few rare circumstances where financially troubled businesses have had transfers in ownership, ETIF benefits have been provided to businesses that have not technically hired any net new employees.

From one standpoint, these jobs do not meet the definition of net new employees. However, DECD contends that these jobs should be considered net new because they are jobs that the Department is sure would have been lost if not for ETIF benefits helping to secure the sale of the financially troubled business to a new owner. The Department reasons that if – instead of being purchased – a financially troubled business had gone into bankruptcy, then all of its employees would have lost their jobs. If the same business was subsequently purchased by new owners, then all employees hired back would readily count as new, qualified ETIF employees. Therefore, DECD concludes that by allowing the jobs to be counted as new without actually requiring the bankruptcy to occur, the Department is simply approving the same jobs sooner rather than later, thereby avoiding the repercussions of bankruptcy for the business and temporary unemployment for the workers. The Department says that it has no other programs available to help businesses in trouble.

One could argue whether or not allowing jobs to be counted as net new under these unique circumstances is intended by statute. However, DECD's decision to allow them likely has positive economic impacts. Preventing a bankruptcy means avoiding negative economic effects on employees, customers and supply chains. In addition, even if the jobs are technically retained – meaning they were in place before ETIF certification – if they were actually in danger of being lost, and the ETIF Program played a significant role in keeping them, then the economic impact associated with those jobs is the same as it would be if they were brand new to the State.

### **Intended Beneficiary: Job-seekers in the State**

The desired outcome of encouraging creation of net new quality jobs in the State is well supported by a number of ETIF's design elements. The program's statute requires a business to add five or more qualified employees above their base level of employment within two calendar years in order to receive ETIF payments. Because a business does not receive payment until after the jobs have been created, and because the payments are based on the withholdings of employees who fill the new jobs, it is impossible for a business to legitimately claim ETIF benefits without creating the required new jobs.

Based on data businesses provided to DECD, OPEGA estimated that up to 1,295 new qualifying jobs attributable to ETIF were created by participating businesses between 2011 and 2016. This job count is far less than the sum of all jobs claimed in individual years between 2010 and 2016 – a total of 54,844. The primary reason for the difference is that most of the jobs reported annually by ETIF businesses are not new to the State in the year reported. The majority of them were originally created and filled in prior years. Those jobs continue to be reported by businesses annually because they continue to qualify the businesses for ETIF benefits for the durations of the businesses' certifications. However, those jobs are only truly new to the State in the year when they were first created. Adding them across years counts individual jobs more than once.

Beyond requiring the addition of at least five new jobs per business, ETIF's statutory provisions also ensure the new jobs created meet the definition of quality jobs as defined by the Legislature. Qualifying jobs must provide total compensation that is greater than the annual per capita personal income in the county where the

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OPEGA estimated that up to 1,295 new qualifying jobs created by participating businesses between 2010 and 2016 were attributable to ETIF.

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business is located and must provide access to health insurance and retirement benefits. OPEGA analyzed the jobs data reported to DECD by business participants and found that the majority of qualified jobs reported surpassed these requirements.

**Table 8. Comparison of Annual Compensation Reported in 2015 to Minimum Requirements**

	Amount by which Annual Compensation Exceeded Minimum Requirement		
	<10%	10% - 20%	>20%
% of Qualified Jobs	17.50%	9.30%	73.20%

Source: OPEGA analysis of DECD records.

OPEGA found that 54% of ETIF jobs in fiscal year 2018 were in areas of the State with below average unemployment.

OPEGA also analyzed the geographic distribution of ETIF qualifying jobs for FY18. This analysis shows that 54% of ETIF jobs in FY18 were in areas of Maine where unemployment levels were below the State average. Under ETIF’s statute alone, jobs created in these areas would only qualify businesses for a 30% ETIF payment. However, due to ETIF’s connection with the PTDZ Program, most of these jobs qualified for the same 80% payment rate as jobs in the highest unemployment areas of the state.

## Assessing Program Outcomes

OPEGA assessed whether ETIF’s design, as reflected in statute and rule, effectively supports achievement of each of the program’s intended outcomes or goals. We also assessed the extent to which each outcome was met during the period 2010 through 2016 using program data provided by MRS and DECD.

The program’s effect on the creation of net new jobs in Maine has already been addressed in the preceding discussion of programmatic effect on job-seekers. The extent to which it has achieved the goals of improving and broadening the tax base and of improving the general economy of the State are discussed in the sections that follow.

### Improving and Broadening the Tax Base and Improving the General Economy of the State

The ETIF Program has design elements that contribute to the goals of improving and broadening the tax base and improving the general economy of the State. The program requires the creation of new jobs at above-average wages. Job creation is a primary economic driver and should increase the base upon which individual income taxes are calculated by increasing the number of employed taxpayers, the amount of taxable earnings, or both. In addition, increased wages often drive increased consumption which increases sales tax revenue for the State.

Since ETIF benefits are only available to for-profit businesses, any improvements in a businesses’ profitability in connection with their ETIF certified projects will increase the tax base as well. Whether this would increase income tax revenue to the State depends largely upon whether the business is also eligible for offsetting

Although ETIF’s economic ripple effects should broaden Maine’s tax base in theory, it is unclear how much additional tax revenue will be captured and how much will be offset by credits or exemptions available via other tax incentive programs such as PTDZ.



income tax credits under the PTDZ Program or other State tax expenditure programs. OPEGA has previously stated, in our report on the PTDZ Program, that roughly 89% to 95% of business projects certified for ETIF between FY15 and FY17 were also part of the PTDZ Program. Since the PTDZ Program offers a 100% income tax credit for the first 5 years of certification and a 50% income tax credit for the remaining 5 years, it is likely that increased business income taxes would not be realized by the State for businesses certified under both programs until after PTDZ certification expired.

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Because ETIF businesses may also participate in other programs that reduce their tax liability, the impact on State and local tax revenue OPEGA estimated represents only potential increases in revenues and not increases in actual tax receipts.

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OPEGA used an economic model to estimate the impact on State and local tax revenue attributable to the ETIF Program. We found the total increase in potential State tax revenue attributable to ETIF could be as much as \$96.4 million for the period from FY12 through FY18, averaging as much as roughly \$13.8 million per year. Adding local taxes brings the total estimated increase in potential tax revenue to as much as \$170.8 million over the same period, an average of \$24.4 million annually. Because ETIF businesses may also participate in other programs that reduce their tax liability, these estimates represent only potential increases in revenues and not increases in actual tax receipts. Actual tax receipts would be lower if ETIF participants also received property tax exemptions via BETR or BETE or received sales tax exemptions or income tax credits via PTDZ or other programs.

OPEGA also modeled the estimated impact on Gross State Product (GSP) attributable to the ETIF Program. We found the total increase in GSP attributable to ETIF to be up to \$1.62 billion for program years 2010 through 2016. This represents average additional GSP per year of roughly 0.42%.

## Assessing Cost Effectiveness

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OPEGA found that ETIF has a low breakeven point. The program is likely to breakeven if just 11.52% of the jobs created by ETIF businesses were created due to the program's benefits.

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OPEGA analyzed ETIF's costs in comparison to the potential new State revenue that the IMPLAN model estimated could flow from ETIF qualified jobs between 2010 and 2016. We performed a breakeven analysis to identify the proportion of ETIF jobs that would need to have been created due to the program in order for the program to breakeven – or to be budget neutral. OPEGA's analysis showed ETIF's breakeven point to be just 11.52%. This means that if more than 11.52% of the jobs created by ETIF businesses were created due to the program's benefits, then the program would be expected to have a positive net impact on the State budget. Conversely, if less than 11.52% of the jobs created by ETIF businesses were created due to the program's benefits, then the program likely has a negative net State budget impact.

The low breakeven point for ETIF is a natural result of a few key elements of the program's design. The first is that benefits are "performance based," meaning that payments are only made if program requirements are met. In addition, the program requires the creation of jobs at above State average wages. Jobs – and high quality jobs in particular – are a significant driver of increased State revenue. As a result, a program that requires job creation is more likely to have a positive net State budget impact.

OPEGA analyzed cost-effectiveness for the ETIF Program based on the program’s impact on Maine’s GSP as well as the number of jobs created and the expected impact on the State and local tax base. Based on the outputs of the IMPLAN economic model, we calculated several measures on a per dollar of tax credit basis. Our analysis was based on businesses that received ETIF payments between FY12 and FY18 and reflects the total ETIF qualifying hiring activity of those businesses.

Cost-Effectiveness Measures Calculated by OPEGA
\$19.28 – Estimated GSP generated per dollar of ETIF payments
\$2.03 – Estimated impact on State and local tax base per dollar of ETIF payments
\$94,030 – Total estimated ETIF cost per direct job attributed to the program

- Gross State Product.** Using economic impact modeling, and applying the 13.1% attribution factor supported by our literature review,<sup>18</sup> OPEGA estimated that value added to Maine’s GSP attributable to ETIF for the period FY12 through FY18 could be as much as \$1.6 billion. This equates to an increase in GSP of approximately 0.42%. On a per dollar basis this represents roughly \$19 in GSP value added for every \$1 of program cost.
- Direct jobs created.** A common measure of cost-effectiveness for business incentive programs is the cost per job created. OPEGA divided total ETIF costs from FY12 through FY18 across all direct job years attributable to the program for the same period. The result was an estimated cost per job year of approximately \$11,754. This represents the program cost associated with a single year of a qualifying job attributed to ETIF. Assuming a job qualifies under ETIF for an average of eight years, this means the total one-time cost per job for qualifying jobs attributable to ETIF would be roughly \$94,000.
- State and local tax base.** Using an economic model, OPEGA estimated the impact to the State and local tax base attributable to the ETIF Program could be as much as roughly \$2 for every \$1 of program cost. Approximately 44% of this impact is due to expected increases in property taxes collected at the local level.

## Assessing Program Similarities and Coordination

OPEGA reviewed Maine’s other tax expenditures listed in MRS’ Maine State Tax Expenditure Report along with recently passed legislation to assess other State programs that are similar to, complementary to, or duplicative of the ETIF Program. While no program is completely duplicative, there are programs with goals and intended beneficiaries that are similar to ETIF’s. Programs that intend to benefit businesses that create quality jobs include the PTDZ Program, the Maine Shipbuilding Facility Investment Credit and the Major Business Headquarters Expansion Credit. The Jobs and Investment Tax Credit was also created for the purposes of increasing investment and employment in the State, but has since been repealed.

The ETIF and PTDZ programs complement each other by providing combined benefits that each program does not provide on its own.

As noted throughout this report, there is much overlap between ETIF and the PTDZ Program. The ETIF and PTDZ programs complement each other by providing combined benefits that each program does not provide on its own. There appears to have been a conscious effort to coordinate the two programs and some stakeholders have stated that this complementary design enhances the

<sup>18</sup> The basis for the 13.1% attribution rate OPEGA used in this analysis is documented on page 19 and supported by the literature review detailed in Appendix B.

effectiveness of both programs. However, this also increases the difficulty of attempting to discern the effects of each program on motivating the businesses' job creation the programs are trying to incent.

Other programs with similar goals to ETIF specifically preclude the simultaneous use of the programs by the same business. The Jobs and Investment Tax Credit, which was repealed in 2016, provided a credit equal in amount to the federal credit for non-retail businesses with a 5 million dollar investment which created a least 100 jobs. Prior to 2015, ETIF statute required participants to fully exhaust the allowable jobs and investment tax credit benefits prior to claiming ETIF benefits. Likewise, up until State capital improvement districts were repealed in 2003, ETIF statute disallowed any claims for benefits if otherwise qualified employees were employed within any State tax increment financing district approved under Title 30-A, Chapter 206. Similarly, the Maine Shipbuilding Facility Investment Credit disqualifies an applicant for the shipbuilding credit from both PTDZ and ETIF benefits. All of these exclusions appear to attempt to prevent the State from providing multiple incentives for the same jobs.

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The additional employment associated with the Major Business Headquarters Expansion Program could be used as net new qualified employees for a new ETIF project, and the company could receive payments from both programs for the same jobs.

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The recently enacted Major Business Headquarters Expansion Credit does not currently contain this exclusion of ETIF benefits for a company participating in the MBHE program. The creation of the headquarters and the employment of the significant number of individuals that are needed for the MBHE benefit could also qualify as a new ETIF project. The additional employment associated with the major business headquarters could be used as net new qualified employees for a new ETIF project and the company could receive payments from both programs for the same newly created jobs (see Recommendation 6). However, already certified ETIF projects associated with an MBHE recipient would not overlap with the major business headquarters project because those ETIF employees would be considered part of the baseline of employment for the headquarters project, not net new jobs.

## Conclusions

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The following questions, which this report responds to, are based on the process established for the evaluation of tax expenditures in accordance with Title 3 § 999.

### 1. To what extent are those benefitting from the tax expenditure the intended beneficiaries?

See pages 24 - 27 for more on this point

The ETIF Program's requirements are well defined and specific enough to ensure benefits are distributed to only the primary intended beneficiaries: for-profit businesses that create new, quality jobs. OPEGA found that, in FY17, 142 businesses received ETIF benefits totaling \$14.8 million. In FY18, 135 businesses received benefits totaling \$13.3 million. ETIF payments averaged 2.6% of businesses' increased employment costs for qualifying jobs in program year 2015.

In the period FY12 – FY18, the average ETIF payment for all businesses was approximately \$103,788 per year. That average payment is, however, distorted by the businesses receiving much higher than average payments. The 10 businesses with the highest ETIF benefits in FY18 received a total of \$7.1 million, which is 53% of the payments made to all businesses in that year. The average payment to these businesses was approximately \$710,600. Payments to the remaining 125 businesses in that year averaged just \$49,613 per business. The 10 businesses with the smallest payments had an average payment of \$5,112.

Job-seekers, the secondary intended beneficiaries, are targeted by program elements that require a business to create at least five new jobs, at or above a specified income level, to become eligible for benefits. Additionally, a business only receives benefits for jobs that are filled, and benefit amounts are linked to the number of jobs created and associated payroll. The degree to which job-seekers are benefitting from ETIF in terms of the number and quality of jobs created is detailed in the response to Question 5 on page 34.

### 2. To what extent is the design of the tax expenditure effective in accomplishing the tax expenditure's purposes, intent or goals?

See pages 27 - 28 for more on this point

OPEGA considers a program's design to be the definitions and requirements in statute and in the rules adopted by administering agencies. OPEGA assessed the degree to which the ETIF Program's design supports its goals of encouraging the creation of net new quality jobs in Maine, improving and broadening the tax base and improving the general economy of the State. We found that the program's design generally supports all of these goals.

ETIF's design effectively targets the creation of net new jobs by clearly establishing baseline employment for each applicant and by requiring the addition of at least five new jobs over the baseline before benefits may be claimed. Job quality is ensured by statutory requirements that qualifying jobs offer health insurance and retirement benefits and provide wages that are higher than established averages for the county.

The ETIF goals of improving the general economy of the State and improving and broadening the tax base are generally supported as by-products of these job-related design elements. Increasing the numbers of employed people and the total wages paid in the State generally contribute to economic growth. These increases can be presumed to drive increased individual income tax receipts and possibly increased sales tax receipts from additional personal spending. Similarly, ETIF businesses that experience increased profitability may pay additional business income and sales taxes if those increases are not counteracted by businesses' participation in other tax expenditure programs.

OPEGA noted that ETIF's design includes a tiered benefit structure that originally directed greater benefits to businesses creating jobs in labor market areas with higher unemployment. However, the PTDZ Program later introduced the expanded ETIF benefit rate of 80% for businesses jointly certified under both PTDZ and ETIF. The 80% rate was higher than any prior ETIF payment rates and was available essentially statewide, regardless of local unemployment levels. The broad availability of the 80% expanded ETIF rate substantially negates the ETIF Program's original targeting of higher unemployment areas. In program year 2016, 54% of qualifying ETIF jobs were in six counties where unemployment was below the State average.

ETIF Benefit Rates	
<b>30%</b>	for businesses in LMAs where unemployment $\leq$ State unemployment rate
<b>50%</b>	for businesses in LMAs where unemployment rate $>$ State unemployment rate and $\leq$ 150% of the State unemployment rate
<b>75%</b>	for businesses in LMAs where unemployment rate $>$ 150% of State unemployment rate
<b>80%</b>	for PTDZ certified businesses

3. What is the State budget impact of the tax expenditure, including past and estimated future impacts?

See pages 21 - 24 for more on this point

The ETIF Program's direct cost to the State is a combination of the value of program benefits paid by the State and the administrative costs borne by DECD and MRS. ETIF payments to businesses totaled \$84 million between FY12 and FY18 and grew from about \$8 million to \$13.3 million annually over that period. These figures include payments at the 80% expanded ETIF rate available only to PTDZ-certified businesses. Table 9 shows payments made in FY12 through FY18 for jobs reported by business participants in program years 2010 through 2016.

**Table 9. Total ETIF Payments Fiscal Years 2012 – 2018**

Program Year	2010	2011	2012	2013	2014	2015	2016
Fiscal Year of Payments	FY12	FY13	FY14	FY15	FY16	FY17	FY18
Total ETIF Payments (in millions)	\$8.03	\$9.64	\$11.56	\$12.98	\$13.68	\$14.82	\$13.31

Source: OPEGA analysis of ETIF payment records from MRS and ETIF annual reports filed with DECD by businesses.

Administrative costs for ETIF are estimated to be less than 1% of the total direct cost – just \$98,151 annually for MRS and DECD combined. Neither agency receives a specific appropriation to cover administrative costs.

Estimates of future ETIF costs are published in the biennial Maine State Tax Expenditure Report (MSTER) published by MRS. The next biennial MSTER is

expected in early 2019 and should include projected fiscal impacts for FY19 and FY20. OPEGA noted that MRS has typically reported ETIF's projected future costs in combination with two other, smaller programs. This has made it impossible to know the projected cost for ETIF alone. We suggest that MRS separate these estimates in future MSTRs to ensure projected ETIF costs are clear.

OPEGA used economic modeling to estimate the net impact on the State based on direct and indirect impacts to State revenues from qualifying jobs associated with ETIF payments in FY12 through FY18. This economic modeling is discussed beginning on page 19 with the net budget impact analysis beginning on page 21.

4. To what extent is it likely that the desired behavior might have occurred without the tax expenditure, taking into consideration similar tax expenditures offered by other states?

See pages 18 - 19 for more on this point

The most difficult question in any tax incentive evaluation is whether the program actually changed participants' behavior. It is also a key question for ensuring good fiscal stewardship and determining the activity and outcomes directly attributable to the program.

ETIF has a statutory provision that seems intended to ensure that the only businesses approved to participate in the program are those whose projects would not go forward without the program's benefits. However, OPEGA found this "but for" provision is not a meaningful filter on program entry. As a result, we cannot assume that absent ETIF benefits fewer jobs would have been created by participating businesses.

OPEGA researched other states to assess whether ETIF might be a factor affecting business decision-making when Maine was in competition with other states. We identified 10 other state programs similar to ETIF and found that Maine's 80% ETIF benefit level available to PTDZ-certified businesses falls roughly in the middle of the benefits offered by those states. Most of the comparable programs in other states had design elements that seemed intended to limit program benefits to businesses most likely to have their behavior impacted by program benefits. However, only four states implemented "but for" requirements with two of them using an attestation approach like Maine.

To gather perspectives for estimating the extent to which tax incentives like ETIF impact business activity, OPEGA reviewed academic literature and evaluations of programs similar to ETIF in other states. Applying our research results to the specific characteristics of the ETIF Program, we estimate that approximately 13.1% of qualifying jobs were potentially created due to the availability of ETIF benefits. OPEGA notes that this estimated attribution rate may slightly overstate the program's impacts for reasons discussed in the report's appendices. That said, we offer it as a starting point for discussing the program's potential outcomes and as an alternative to the unsupported assumptions that the program's benefits changed the behavior of all – or alternately, none – of the businesses participating in it.

Another factor impacting the likelihood that jobs associated with ETIF would have been created anyway is the degree to which the business projects associated with ETIF jobs are also supported by other State programs, such that the same jobs might be at least partially attributed to the other programs as well. With regard to

PTDZ, it seems likely that a substantial portion of the jobs OPEGA attributes to ETIF could be attributed to PTDZ as well, since participants of one program typically participate in the other. However, we were unable to quantify the degree of overlap between the programs in this evaluation. For other programs we either did not have all the data necessary to factor potential overlap with ETIF into our analyses or confidential restrictions on data prevented us from doing so.

More detail about all of the factors and assumptions relevant to OPEGA’s estimation of impact ETIF had on business behavior begins on page 19.

5. To what extent is the tax expenditure achieving its purposes, intent or goals, taking into consideration the economic context, market conditions and indirect benefits?

See pages 27 - 28 for more on this point

ETIF’s most specific goal is encouraging the creation of net new quality jobs in Maine. OPEGA analyzed data from annual reports filed by ETIF businesses to assess the extent to which this goal had been achieved.

OPEGA found that total direct jobs supported by ETIF averaged 7,835 in any one year between program years 2010 and 2016. The qualifying jobs reported generally increased over the period with 9,588 jobs reported in 2015 and 9,104 jobs reported in 2016. These are the total jobs that qualified for ETIF payments in a year, but not all of these jobs were new in that year. Once created, new qualifying jobs may continue to be claimed by eligible businesses for up to 10 years. As a result, the majority of the jobs reported in any year were originally created in some prior year.

OPEGA estimated that 9,863 new qualifying jobs were added by ETIF-certified businesses between calendar years 2011 and 2016. Applying the attribution factor of 13.1% supported by our literature review suggests that up to 1,295 of the new jobs created between 2011 and 2016 could reasonably be attributable to ETIF. Table 10 shows the total qualifying jobs reported, the number of those we estimated were new in each program year and the number of those we estimated were attributable to ETIF.

**Table 10. ETIF Impact on Employment for Program Years 2010 – 2016**

	2010	2011	2012	2013	2014	2015	2016	Total
<b># Qualifying Jobs Reported</b>	5,908	6,245	7,093	8,178	8,728	9,588	9,104	<b>**</b>
<b># Unique New Qualifying Jobs</b> (subset of qualifying jobs reported)	*	1194	1592	1385	1797	2304	1591	<b>9,863</b>
<b>#Unique New Jobs Possibly Attributable to ETIF</b> (subset of new qualifying jobs)		157	209	182	236	302	209	<b>1,295</b>

\* OPEGA could only estimate new hires for 2011 – 2016 because the calculation was based on incremental jobs.

\*\*Qualifying jobs reported cannot be summed across years because the majority of jobs included in each yearly total are also included in one or more prior years as well.

Source: OPEGA analysis of ETIF data obtained from DECD and MRS.

We also assessed the degree to which the jobs supported by ETIF were high quality jobs, as defined by statute. To do this, we compared the annualized compensation for reported jobs in 2015 to the income requirements for qualifying jobs in that year. Qualifying jobs must offer income greater than the most recent annual per capita income in the county in which the job is located. The only exception to this rule is for jobs created at call centers in Washington or Aroostook counties. We

found that roughly 73% of jobs reported in 2015 had annualized compensation that exceeded the minimum threshold by more than 20%. This suggests that the majority of the jobs associated with ETIF payments significantly exceed the standard of quality established by the Legislature.

OPEGA used economic modeling to estimate the degree to which job creation attributable to ETIF has impacted Maine's tax base and contributed to the general economy of the State. Assumptions and limitations relevant to the economic modeling, and OPEGA's estimates for these outcome measures, are discussed beginning on page 28.

6. To what extent is the tax expenditure a cost-effective use of resources compared to other options for using the same resources or addressing the same purposes, intent or goals?

See pages 28 - 29 for more on this point

OPEGA found ETIF's breakeven point to be approximately 11.5%. This means that the program's impacts outweigh its direct costs if at least 11.5% of the business activity supported by the program would not have occurred if the program's support had not been available. ETIF's design lends itself to a low breakeven point both because benefits are only available to businesses that create jobs – a key driver of economic growth – and because the benefits paid by the program are relatively low – roughly 2.6% of increased employment costs associated with qualified jobs.

ETIF's relatively small payment amount can be seen as both a strength and a weakness for the program. On one hand, a smaller benefit means that the program presents a lower financial risk to the State. On the other hand, a smaller benefit is also less likely to be of a great enough magnitude to truly affect businesses' location or expansion plans in Maine.

Despite the relatively small magnitude of ETIF benefits, stakeholders suggest that the program may still affect business decisions by conveying the State's goodwill toward businesses. Others suggest the program may affect business decisions by compensating businesses, to some degree, for increased costs associated with barriers to growth in Maine – such as weaknesses in infrastructure or workforce skills. However, OPEGA notes that the program does not, nor is it designed to, directly address those barriers.

Best practices in evaluation of program impact and cost-effectiveness compare the estimated impacts of the program being evaluated to what could be expected from using the same amount of funds in a different way. The estimated impacts of ETIF could, for example, be compared to the impact of directing same amount of State funds to education spending, infrastructure investment, or across-the-board tax cuts. This type of comparative analysis was not performed in this evaluation because it would require more sophisticated fiscal modeling than OPEGA currently has access to.

Additional analysis of cost-effectiveness is discussed beginning on page 28.



7. To what extent are there other state or federal tax expenditures, direct expenditures or other programs that have similar purposes, intent or goals as the ETIF Program and to what degree are any similar initiatives coordinated, complementary or duplicative?

See pages 29 - 30 for more on this point

OPEGA did not find the ETIF Program to be exactly duplicative of any other State programs. However, it is only one of a number of programs in Maine with a goal of encouraging job creation. For example, both the PTDZ Program and the newly enacted Major Business Headquarters' Expansion (MBHE) Program target job creation as well. Both PTDZ and the MBHE Program allow certified businesses to receive benefits based on many of the same new jobs that qualify for ETIF payments. However, the MBHE Program has a narrower scope and under current statute allows for only two business projects to participate. In contrast, ETIF is more broadly available and can accommodate a large number of participants.

Two other state programs impacted ETIF participation but do not any longer. Prior to 2016, ETIF statute required that a business exhaust its benefits available under the Jobs and Investment Tax Credit (enacted in Title 36 § 5215) prior to claiming any ETIF benefits. As of 2016, the Jobs and Investment Tax Credit stopped accepting new claims and so no longer impacts ETIF eligibility. ETIF statute also formerly prohibited participants from claiming jobs for ETIF that were also being claimed in connection with a State Tax Increment Financing District. In 2017 this provision in ETIF's statute was repealed to reflect the fact that State Tax Increment Financing Districts<sup>19</sup> (under Title 30-A § 5242) had been repealed in 2003.

8. To what extent is the State's administration and implementation effective and efficient?

See pages 9 - 15 for more on this point

DECD and MRS jointly administer the ETIF Program. DECD is primarily responsible for certifying program participants, collecting and processing annual reports while MRS is responsible for authorizing and making payments. OPEGA found that both agencies are efficiently getting ETIF benefits to eligible businesses within existing resources. However, there are opportunities to improve administration and availability of program data by:

- addressing information technology and staffing challenges, which may require additional resources at DECD;
- maintaining accurate program records and ensuring appropriate payments; and
- updating State agency rules to reflect substantive statutory changes.

In addition, OPEGA found that conflicts in statute make it unclear which ETIF records may be publicly disclosed and which must be held confidential. This lack of clarity creates uncertainty for administering agencies about the level of protection required for data and about what can be disclosed publicly.

<sup>19</sup> This is not the same program as Municipal Tax Increment Financing districts administered under Title 30-A §§ 5221 - 5235.

## Performance Measures Calculated by OPEGA

Table 11 includes measures of ETIF's activity calculated by OPEGA based on the evaluation parameters for this review approved by the GOC. All measures were calculated by OPEGA using data obtained from DECD and MRS. Economic impact modeling was used to calculate these measures where appropriate and applicable. The inputs and assumptions underlying that modeling are detailed beginning on page 19.

<b>Table 11. Measures of ETIF's Activity</b>	
Total # of businesses receiving ETIF benefits	208 unique businesses for FY12 – FY18 142 businesses in FY17 and 135 in FY18
Total \$ value of ETIF benefits received by businesses	\$84 million total for FY12 – FY18 \$14.8 million in FY17 and \$13.3 million in FY18
Total direct program cost (ETIF benefits plus administrative costs)	\$14.9 million in FY17 and \$13.4 million in FY18 (admin costs are less than 1% of total cost)
Average ETIF payment per business	For FY12 – FY18: Average annual payment ranged from \$90,228 to \$113,431; Annual payment to the 10 highest paid businesses averaged \$695,182; Annual payments to the 10 lowest paid businesses averaged \$5,532
Impact on businesses' labor costs	Benefits averaged 2.6% of additional payroll costs associated with qualifying new employees
Total \$ value of direct payroll and benefits associated with new quality jobs attributable to ETIF	Annual value of payroll and benefits averages approximately \$68.5 million for FY15 – FY18 <sup>20</sup>
Comparison of actual wages and benefits for qualifying jobs to minimum requirements	73% of ETIF jobs in 2015 had annualized compensation that exceeded the minimum threshold by more than 20%
Net impact on State budget attributable to ETIF (using economic modeling to include indirect benefits)	Positive net impact of up to \$11.7 million across FY12 – FY18
Indicators of economic impact attributable to ETIF (using economic modeling to include indirect benefits)	Estimated average additional State and local tax revenue of up to \$24.4 million annually for FY12 – FY18; Additional GSP of up to 0.42% annually for FY12 – FY18
Total # of new qualifying jobs attributable to ETIF	Up to 1,295 new qualifying jobs added by ETIF certified businesses between 2011 and 2016 <sup>21</sup>
Cost per new qualifying job attributable to ETIF	Roughly \$94,000 in one-time total cost per direct job <sup>22</sup>
Value of additional payroll & benefits for qualifying employees attributable to ETIF per dollar of program payments	An average of \$4.96 realized in annual payroll and benefits per \$1 of State cost for FY15 – FY18
Gross State Product generated per dollar of total ETIF payments	Up to \$19.28 in GSP per \$1 of State cost across FY12 – FY18
Source: OPEGA analysis of data received from administering agencies.	

<sup>20</sup> Data limitations prevented OPEGA from calculating the value of payroll and benefits over the time span FY12 – FY18 as was done for most other measures.

<sup>21</sup> New jobs in 2010 could not be calculated because new jobs were estimated based on additions over prior year claims and 2010 was the first year for which OPEGA had jobs data.

<sup>22</sup> Based on the assumption that jobs qualify for ETIF for an average of eight years.

# Recommendations

## 1

### ETIF's Objectives Should Be Reconsidered Based on Maine's Current Economic Development Needs

In the 20 years since ETIF's enactment, the program has not had its goals or design reassessed to determine whether they adequately respond to current State economic conditions and needs. Stakeholders representing the business community interviewed by OPEGA universally stressed that ETIF, and the closely-connected PTDZ Program, are the key economic development programs Maine can use to attract and support business growth. The two programs are considered so key because they are the most broadly applicable programs with the most substantial benefits in the State. Without them, stakeholders say Maine would be at a significant disadvantage in comparison to other states.

At the same time, some stakeholders OPEGA interviewed felt that ETIF's focus on job creation may not address the State's most critical current barriers to economic growth, or the most critical areas of need, for some businesses in the State. OPEGA saw this theme reflected in other reports about Maine's economy or economic development programs and in the ways the program has been used that do not appear to be exactly what was intended.

- Barriers to economic growth – Though the ETIF Program may essentially compensate businesses for the difficulty of coping with barriers to growth, it does nothing to address these issues directly or to reduce their impact on businesses in the future. OPEGA reviewed Maine Development Foundation's 2017 *Measures of Growth* report, and noted the report indicated Maine has critical deficiencies in development of a skilled workforce and transportation infrastructure. Workforce challenges were also noted in the 2018 *Comprehensive Evaluation of Maine's Research & Development and Economic Development Incentive and Investment Programs* report prepared for DECD by Investing Consulting Associates (ICA).

"Companies and institutions continue to cite problems finding qualified workforce in the State or attracting workers to Maine."  
ICA's 2018 Report
- Prevention of major workforce reductions – Although there appears to be agreement that preventing losses of major employers in the State is important and worthwhile, Maine has no programs designed for these situations. OPEGA noted in reviewing ETIF data that the program has occasionally been used in the past to support the retention of jobs at financially distressed companies. This use of ETIF appears to be outside of the program's intent to create net new jobs, but may be filling a gap in the State's economic development toolbox.

- Supporting businesses at various stages of development – Stakeholders pointed out that ETIF is really for mature businesses and that the State has little to no support for businesses in other development stages that may not be ready to add many employees yet. While supporting mature businesses is valuable, some stakeholders felt that more, or better, programs were needed to help businesses that were not yet mature get access to the capital they need to grow.

### **Recommended Legislative Action:**

The Legislature may want to consider whether ETIF should be updated, or replaced, to better respond to Maine’s current economic conditions. Such an assessment would be most effective and meaningful in the context of a State economic development strategy like the one described in LD 367, considered during the second regular session of the 128<sup>th</sup> Legislature<sup>23</sup>. It may also be useful to consider the results of the DECD studies required as part of LD 1654, which was enacted during the 128<sup>th</sup> Legislature’s Second Special Session to extend the PTDZ Program.

If the Legislature decides to consider updating or replacing ETIF, the consideration should involve administering agency staff and business community stakeholders, and should be approached in a way that limits uncertainty for the business community and recognizes ETIF’s position as one of Maine’s most relied upon economic development programs. This could include ensuring that any changes to ETIF are phased in slowly and that if ETIF is to be replaced, its replacement is active before ETIF is phased out.

## **2 ETIF’s Requirements Should Be Reviewed in Light of Current Business Realities and Updated Where Necessary**

Many ETIF requirements have not been updated since the program was enacted in 1996. Stakeholders interviewed by OPEGA pointed out that some of the original design elements may no longer reflect the realities of the current business environment or may prevent some businesses from participating in the program. Some of the design elements that stakeholders raised to OPEGA include:

- Health insurance and retirement benefit requirements – Stakeholders noted significant changes in the health insurance market and in retirement benefits. For example, some employers are now providing reimbursement to employees for insurance purchased on the marketplace rather than providing traditional employer-based health insurance. Neither ETIF’s statute nor the program’s rules address whether this type of health insurance benefit would meet the health insurance requirement for an ETIF qualified employee. Statute and rules also do not acknowledge situations where employees decline the offered coverage because they have access to coverage they prefer through a spouse.

<sup>23</sup> LD 367 was carried over to Second Special Session of the 128<sup>th</sup> Legislature and died on the appropriations table when the Legislature adjourned.

- Wage requirements – Stakeholders agreed that a wage requirement was an important element for a quality jobs program like ETIF. However, they noted that the particular income requirement in ETIF can prove challenging for employers to meet because the threshold is per capita income which can be driven up by non-wage factors such as dividend income. Setting an income requirement as a certain percent above minimum wage was suggested as an alternative.
- Employment baseline lookback – ETIF’s employment baseline is calculated based on the greater of average employment levels in the past 12 or 36 months. Stakeholders noted that the business environment moves so rapidly today that a 36 month lookback can be problematic. An example of this would be a business that lost 25% of its workforce during the Great Recession of 2008, and considered an expansion to a new product line in 2010 in hopes of returning to profitability. A baseline calculated for this company in 2010 would include their employment prior to the 25% workforce reduction, rather than recognizing the business’s new reality.

**Recommended Management Action:**

DECD should review ETIF’s requirements, with input from stakeholders, to identify those in need of updating. The Department should then make a proposal to the Legislature describing the changes the Department would suggest.

### 3

#### **Statute Should Be Amended to Clearly Reflect All Intended Outcomes Against Which ETIF’s Effectiveness Will Be Measured**

The goals and measurable outcomes against which the ETIF Program should be assessed are not clearly articulated in statute. For the purposes of this review, OPEGA identified the program’s goals from Title 36 § 6752 which states that the program “is established to encourage the creation of net new quality jobs in this State, improve and broaden the tax base and improve the general economy of the State.” However, ETIF statutory definitions also include tiered benefit rates that suggest a possible intention to target more economically distressed areas of the state by directing higher benefits to businesses in LMAs with higher unemployment.

**Recommended Legislative Action:**

The Legislature should add a section to ETIF’s statute to clarify the program’s intended outcomes and how the program’s success should be measured in future evaluations. Model language can be found in similar provisions enacted by the 128<sup>th</sup> Legislature for the PTIDZ Program (Title 30-A § 5250-P(2)) and the MBHE Program (Title 36 § 5219-QQ(5)).

In considering the degree to which targeting economically distressed areas is a goal for ETIF, the Legislature should review the results of the DECD study of whether geographical limitations under the PTIDZ Program should be amended. This study is required as part of the bill which extended the PTIDZ Program, LD 1654, enacted during the Second Special Session of the 128<sup>th</sup> Legislature, and is to be reported out by January 15, 2019.

## 4 ETIF's Statute or Rule Should Be Amended to Support Effective Implementation of the "But For" Application Requirement

ETIF's statutory "but for" requirement appears intended to require that a business's ETIF application can only be approved if the business would not expand, and create jobs, without the program's benefits. However, as this requirement is currently implemented, it can be met by any business. This is possible because a business can attest truthfully that its project would not go forward without ETIF benefits for any number of reasons. For example, a business could set a particular profit expectation for the project that would not be met without ETIF benefits. OPEGA understands that some businesses may also feel justified in claiming they meet the "but for" requirement based on the logic that they know that the ETIF Program exists, and therefore, they would not be fulfilling their obligation to their shareholders if they did not secure ETIF benefits to improve the profitability of their development projects.

OPEGA observed that the current "but for" requirement's vague and subjective nature leaves program administrators at DECD caught between conflicting duties. One duty is to limit the program as required, which, by definition suggests filtering out some program applicants. Meanwhile another duty is to the Department's goal of maximizing economic growth in Maine. This goal is readily achieved by distributing ETIF benefits to as many businesses as possible, since every project has the potential to add something to the economy and the statutory cap on ETIF benefits far exceeds all benefits requested annually. Under these circumstances – and with no clear criteria in statute or rule – there is little support for DECD to deny an ETIF application, even if the Commissioner does not believe that the proposed project would not happen "but for" the availability of ETIF benefits.

OPEGA found the desire to limit funding from economic development programs to projects that wouldn't occur without the incentives to be common among other states with similar programs. However, few of these states currently have similar "but for" provisions in place. Those that do have these requirements find them similarly difficult to enforce and unlikely to be meaningful. Instead, other states have tackled this challenge by limiting program benefits to a more specific subset of businesses or by using caps on program benefits or participants. A few, such as North Carolina, perform an in-depth analysis of each business project up-front to ascertain the degree to which benefits from the state would impact the business's behavior and render a positive net impact on the state budget.

### **Recommended Legislative Action:**

The Legislature should direct DECD to bring forward a proposal for amendments to statute or rule to make the "but for" application requirement effective. At a minimum, the amendments should accomplish two objectives. The first objective is to define the criteria that must be met for ETIF's "but for" application requirement to be satisfied. The second objective is to establish the requirements for documentation to be submitted, and maintained, as evidence that a business meets the "but for" criteria.

The goal of establishing criteria is to provide a clear basis for DECD decisions about whether individual ETIF applications meet the “but for” requirement. A few examples of possible criteria include poor access to capital; infrastructure barriers that increase the cost of an expansion in Maine in comparison to other locations; or competitive economic incentives offered by other states or countries to a business that could easily relocate outside of Maine.

Specifying in statute, or rule, which conditions should justify approval of an otherwise eligible ETIF application – and conversely, whether any specific conditions should be excluded – would improve guidance for DECD and ensure a common understanding about the types of projects the program is intended to support. However, most imaginable “but for” criteria are still subjective in nature. This makes them difficult to prove conclusively and easy to render ineffective in implementation.

To support effective implementation of the new criteria, OPEGA also recommends statutory, or rule, changes to require increased “but for” documentation. Strong documentation standards would require applicants to submit detailed and specific evidence to validate that the “but for” criteria have been met. Also, DECD would need to keep similarly detailed documentation to support decisions to approve or deny ETIF applications. Review of the DECD’s documentation at future intervals could provide useful information to support future review – and, if needed, revision – of the “but for” criteria.

If changes are made to ETIF’s “but for” requirements, the Legislature should consider applying the same changes to the PTDZ Program in order to avoid confusion for businesses participating in both programs. The Legislature may also want to consider whether the same “but for” approach could be applied uniformly across all tax expenditure programs for which it is applicable. An across-the-board approach could simplify and clarify the application process for businesses.

## 5

### ETIF’s Economic Consideration Requirements Should Be Made More Explicit or Eliminated

OPEGA found the statutory requirements limiting ETIF certification to projects that will make an economic contribution to the State (Title 36 § 6756(2)) while not resulting in substantial harm to existing businesses (Title 36 § 6756(3)) are ineffective in meeting their presumed intent. Both DECD’s Commissioner and the State Economist reported to OPEGA that they could not remember a time when an ETIF application had been denied on the basis that it failed to meet these economic consideration requirements. There was a shared sentiment that an application would likely never be turned down on this basis because those involved have generally believed that all business projects involving job growth contribute to economic growth, and that the benefits of these projects in the State outweigh any potential detriment to existing businesses. OPEGA also observes that the vague language in these statutory requirements leaves DECD with nothing to support an appropriate decision to deny an ETIF application.

It is reasonable to assume that ETIF projects will make an economic contribution to the State since the projects must include creation of at least five new jobs. The creation of jobs is, in and of itself, an economic contribution. Thus, the requirement to make an economic contribution is redundant unless some contribution over and above job creation is expected. The prohibition of substantial harm to existing businesses, however, is not similarly guaranteed by the ETIF's design.

**Recommended Legislative Action:**

The Legislature should eliminate the economic contribution requirement under Title 36 § 6756(2) from statute, as this requirement and the program's job creation requirements are redundant. Alternately, if some economic contribution beyond job creation is expected of program participants, then the expected contribution should be made explicit in statute.

The Legislature should also either eliminate, or make more explicit, the requirement that ETIF certification is awarded only if a business project will not cause substantial harm to existing businesses. Quantifying harm to existing businesses is subjective in nature, much like the "but for" requirement discussed in Recommendation 4, and many of the same cautions apply to any attempt to strengthen this provision.

## 6 The Legislature Should Clarify Whether the Same Qualifying Jobs May Be Claimed for Both ETIF and the MBHE Program

Both ETIF and the recently enacted MBHE Program provide benefits based on creation of new jobs, and statute is silent as to whether the same new jobs may qualify a business for benefits under both programs. Another recently passed program – the Tax Credit for Maine Shipbuilding Facility Investment<sup>24</sup> passed in 2018 – also provides benefits based in part on creation of new jobs. This program specifically prohibits participation by a business participating in ETIF. This prohibition prevents a business from accessing both programs at once, regardless of whether the business is claiming the same qualifying jobs, or differing sets of qualifying jobs, for benefits under the two programs.

Similarly, up until State capital improvement districts were repealed in 2003, ETIF statute disallowed any claims for benefits if otherwise qualified employees were employed within any State tax increment financing district approved under Title 30-A, Chapter 206. This suggests that the Legislature has sought, in the past, to ensure jobs are not being claimed for ETIF that are also being claimed in connection with other State economic incentives.

If the same new jobs associated with the same business project are allowed to qualify under both MBHE and ETIF this could create administrative difficulties for DECD. Currently, there is the potential for a business to have one project under ETIF, and a separate project certified under MBHE. Tracking the potentially different employment baselines under each program would pose an administrative

<sup>24</sup> P.L. 2017, ch. 361.



challenge, as would monitoring which jobs meet the minimum qualifications for one but not the other, and which jobs qualify for both programs<sup>25</sup>.

**Recommended Legislative Action:**

The Legislature should clarify in statute whether participants in ETIF are allowed to also participate in the MBHE Program. In clarifying this point the Legislature should also consider the interaction between ETIF and the newly enacted Shipbuilding Program and should treat the programs consistently.

## 7

### Statute Should Be Amended to Address Businesses That Change Ownership

ETIF statute and rules are silent concerning businesses that change ownership. Absent statutory guidance, DECD has adopted internal protocols for handling transfers of ownership under two different sets of circumstances.

- When a business with an active ETIF certification changes ownership.  
Under these circumstances, DECD allows the active ETIF certificate to be transferred to the business's new owner. Consequently, the business's new owner has the same base level of employment that applied to the prior owner.
- When a business with no ETIF certification changes ownership, and the new owner subsequently applies for ETIF certification.  
Under these circumstances, DECD does not allow the new owner to be certified with a base employment level of zero, because this would ignore the fact that the business had employees in Maine before the change in ownership. Instead, the Department requires the business's base level of employment to be calculated based on employment levels for the one to three years preceding the ETIF application, regardless of whether the new or prior owner owned the business for that period of time. This protocol attempts to ensure that employees counted for ETIF – those over the base level of employment – are actually *net new to the State*.

OPEGA found that DECD has generally been consistent in applying these internal protocols. We also find that these protocols support ETIF's goal of net new job creation. However, unless these protocols are formalized, there is a risk of actual, or perceived, inconsistent treatment for businesses. There is also a risk that a business could challenge the basis for DECD's internal protocols. Such a challenge could be difficult to defend absent any formal guidelines to justify the decision.

**Recommended Management Action:**

DECD should bring a proposal to the Legislature for amendments to statute to address a change in ownership of a business.

<sup>25</sup> Qualifying jobs under ETIF must meet more requirements than those qualifying under MBHE. For example, ETIF jobs must meet minimum income thresholds that do not apply to MBHE jobs.

## 8

**Confidentiality Status of ETIF Data Should Be Clarified**

Conflicting statutory provisions have made it impossible to be sure which specific ETIF data elements held by DECD or MRS are designated confidential and which may be subject to public disclosure. In the summer of 2017, OPEGA requested an opinion from the Office of the Attorney General seeking clarification about the confidentiality status of the data. Unfortunately, the number and nature of statutory conflicts did not allow for the kind of clarification we requested, despite extensive review by the AG's Office. The result is a lack of clarity about which pieces of data are subject to public disclosure to support transparency for the program. It is also unclear which pieces of data are held confidential, either because they could expose businesses' plans to competitors, or because they include confidential taxpayer data.

The lack of clarity as to whether some or all ETIF data is considered confidential taxpayer data is particularly problematic because it creates uncertainty about how the data must be handled in order to ensure it is adequately protected. Under MRS standards, confidential taxpayer data must be protected with measures that go above and beyond what state agencies might typically use to protect other types of confidential data. These measures include everything from additional security on laptop computers to additional physical barriers to accessing the facility where the data is stored. DECD does not currently protect the ETIF data it holds to this degree, and because of the statutory conflicts it is unclear whether they need to do so.

The conflicts in statute have allowed agencies to exercise discretion – which may, or may not, have been intended – in deciding which pieces of information will be disclosed. OPEGA observes that considering ETIF data confidential tax records may afford businesses extra protections for program data they consider sensitive, but this comes at the cost of reduced transparency and can make it more difficult for legislators and the public to access pertinent program usage data.

**Recommended Legislative Action:**

The Legislature, with support from MRS and DECD, should determine which ETIF records or data elements should be accessible to public inspection and which should be considered confidential taxpayer records and thus protected from disclosure at the highest level.

Once the desired level of confidentiality has been determined, statute should be amended to reflect those determinations and to eliminate the existing statutory conflicts. If it is decided that any ETIF records will be considered confidential taxpayer records, then DECD's handling of that data should be updated to meet the protection standards for confidential taxpayer records practiced by MRS.

## 9

## DECD and MRS Should Address Opportunities to Improve Fiscal Impact Forecasts and Update Rules

OPEGA noted the following opportunities to improve specific aspects of ETIF's administration. We assert that the agencies responsible for administering ETIF have the authority necessary to make these improvements without legislation.

### Revenue Loss Estimated for ETIF in the Biennial MSTER Should Be Clarified

The MSTER is the sole source of ETIF fiscal impact forecasts for the Legislature. It has historically shown ETIF's estimated past, and forecasted future, General Fund revenue loss as a lump sum that includes estimated revenue losses associated with both the Loring Job Increment Financing Fund under Title 5 §§ 13083-O through 13083-T and the Brunswick Naval Air Station Job Increment Financing Fund authorized by Title 5 § 13083-S-1. For example, the 2018-2019 MSTER estimates FY18 revenue loss of \$15.8 million, and approximately \$800,000 of this amount is associated with the Loring and Brunswick programs. Reporting the amounts in combination does not provide the Legislature with a clear and accurate estimate of the past budgetary impact, or the future anticipated budgetary impact, of each program individually.

### ETIF Rules Should Be Updated to Reflect Significant Statutory Changes Since 2009

DECD is responsible for maintaining the ETIF Program rules, but the Department has not updated the rules since 2006. As a result, the rules currently in effect do not reflect substantive statutory changes made since that time. For example, as of 2018, rules did not include statute's allowance for PTDZ Tier 2 businesses to receive expanded ETIF benefits for up to five years or statute's redefinition of qualified employees with specific requirements for call centers in Washington and Aroostook counties. The recent extension of PTDZ will also necessitate updating ETIF rules to reflect the later sunset provision.

### **Recommended Management Action:**

MRS should ensure its estimations of future ETIF costs reflect only projected revenue loss associated with ETIF, rather than including revenue loss associated with the Brunswick and Loring Job Increment Financing Programs.

During this review, we discussed our recommendation with DECD that the Department's ETIF rules should be updated to reflect substantive changes to statute. As of December of 2018, the Department had prepared draft updates to ETIF rules. The Department is prepared to submit the rule updates as soon as it is clear whether any substantial changes to the ETIF Program will be considered during the 129<sup>th</sup> Legislature's First Regular Session which might impact the program's rules.

## 10 MRS Should Strengthen Controls to Prevent Overpayments and Ensure Accurate ETIF Records

OPEGA identified between \$125,000 and \$150,000<sup>26</sup> in overpayments made in FY15 and FY16. In the process of analyzing ETIF data, OPEGA noted a few payments that did not appear reasonable. When asked about these payments MRS reviewed their details and agreed that they had been overpaid due to erroneous reported withholdings amounts. MRS told OPEGA that the overpaid amounts have since been returned to the State.

OPEGA's data analysis also identified some inaccuracies in the records MRS maintains to support approved ETIF payments. Although these inaccuracies did not represent inappropriate payments, they are important because MRS has the only record of the number of jobs approved and value of benefits paid in connection with individual ETIF requests. Keeping this final record free from errors is necessary to ensure that any program utilization reports are accurate and will also make future evaluations more efficient.

ETIF claims are processed manually by MRS on spreadsheets, not on the agency's system for processing tax returns. This kind of record keeping is understandable given the fact that ETIF is a small piece of MRS's overall workload and given that ETIF is not claimed via tax filings. However, such record keeping comes with increased risk of error and requires additional controls to ensure data integrity.

### **Recommended Management Action:**

MRS should improve controls to ensure both the appropriateness of ETIF payments and the accuracy of ETIF records. OPEGA notes that MRS has been required to administer ETIF within existing resources and that improving controls can be challenging when resources are constrained. However, controls such as an added layer of verification or review for ETIF payment records do not need to be resource intensive.

## 11 DECD Should Address Information Technology and Staffing Challenges

The ETIF Program distributes approximately \$15 million per year, but has no ongoing appropriation to cover its administration. Administrative funding may have been unnecessary in the program's early years. However, the program has grown significantly and administrators are under increasing demand to monitor program outcomes and act as financial stewards. OPEGA finds that meeting these demands without any funding for administration<sup>27</sup> presents a significant challenge. This echoes what the ICA reported in 2018 – that they had heard from businesses that DECD's staff seemed under resourced.<sup>28</sup>

<sup>26</sup> In order to protect ETIF data to MRS standards OPEGA cannot report the exact amount of overpayments identified.

<sup>27</sup> The Legislature did appropriate a one-time amount of \$33,750 for updates to BDTI in FY19 when PTDZ was extended in P.L. 2017, ch. 440.

<sup>28</sup> ICA's Comprehensive Evaluation of Maine's Research & Development and Economic Development Incentive and Investment Programs, page 76.

DECD has a very small staff and no appropriation dedicated to administering ETIF or PTDZ, which together require a fair amount of administration and technical support for annual reporting. DECD finds the cost of OIT support often makes it inaccessible, and OPEGA found that OIT staff seemed to work with BDTI infrequently enough that when they are asked to do so they require extra time (at a cost to DECD) to become acclimated to the database again before accomplishing the requested support.

In addition, DECD has no business analysts or similar positions, so data analysis and technology skills are available in-house only when individuals hired for other positions happen to have them. This, in combination with the aging and complex nature of BDTI, has left the agency sometimes unable to readily produce basic program usage reports and unable to fully use the valuable data they collect annually from program participants. Current staff members have many ideas about how to make BDTI more user-friendly for business participants and how to streamline its use for themselves, but the cost of such improvements are prohibitive when ETIF must be administered within existing resources.

#### **Recommended Management Action:**

DECD should take the steps needed to address the technology challenges the Department faces and to ensure at least one individual on staff consistently has the data analysis and technology skills required to work with the tax incentive database. DECD should also consider the full cost of its administration of ETIF, including any increase in costs associated with addressing its technology challenges, and should propose to the Legislature a funding mechanism that will provide adequate resources to support robust stewardship of State assets and program management.

OPEGA found that some other states with programs similar to ETIF assess one-time certification fees or annual reporting fees to cover the costs of program administration. This is also similar to the model FAME uses to raise funds to administer Maine's New Markets Capital Investment Program. DECD is already authorized to assess fees for ETIF administration under Title 36 § 6759, but does not currently do so.

As of January 2019, the Department was in the process of issuing a Request for Information (RFI) to address their database needs.

## Acknowledgements

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OPEGA would like to thank the management and staff of both DECD and MRS for their cooperation throughout this review.

We would also like to thank the Attorney General's Office for their research and guidance regarding access to confidential taxpayer information.

## Agency Response

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In accordance with Title 3 § 997, OPEGA provided DECD and MRS an opportunity to submit comments after reviewing the report draft.

## Appendix A. Scope and Methods

The nine GOC-approved objectives for the evaluation of the ETIF Program are detailed in Appendix C. The scope of this review was limited to program years 2010 through 2016 because data from prior years had quality issues and was not available in a usable electronic format.

Information was gathered through:

- review of relevant statute and rules, including the history of changes made since the program's enactment;
- review of program documents from the Maine Department of Economic and Community Development and Maine Revenue Services, such as application and certification materials, tax bulletins, benefit claim forms, and internal procedural manuals;
- review of the evaluation reports prepared by ICA for DECD in 2016 and 2018;
- review of the Maine Development Foundation's 2017 *Measures of Growth* report;
- interviews with program administrators at MRS and DECD;
- interviews with stakeholders representing the business community;
- review of evaluations of programs similar to ETIF in other states;
- review of academic literature on methods for evaluating the economic impact of tax incentives; and
- review of available program data.

Data analyses in this evaluation were based on data sets provided by DECD and MRS. The following are adjustments OPEGA made to those data sets for the purposes of our analyses:

- Removed any authorized pilot projects from the data. ETIF pilot projects do not have the same requirements as other ETIF projects. For example, seasonal employees may qualify under certain pilot projects.
- Adjusted job counts and payments in rare cases where MRS had reduced one year's payment to compensate for an overpayment in prior years. Our adjustments aligned the payments with the year in which qualifying jobs were reported.
- Adjusted job counts and payments where MRS data and DECD data disagreed because MRS approved something other than the claimed amounts or because of errors in an agency's records.
- Adjusted payments to reflect the benefits businesses were eligible for each year regardless of whether the actual amounts paid were reduced to offset debts owed to the State or adjustments for overpayments in prior years.

The economic impact analyses in this report were based on the following key assumptions.

- We counted jobs as inputs to the economic impact model only in the years the jobs were claimed for ETIF, not for any additional years when the jobs may have continued to exist even if they were no longer ETIF qualified.
- We attributed all jobs claimed for ETIF solely to the ETIF Program, regardless of whether the jobs were also associated with other State tax incentive programs such as the PTDZ Program or the NMTC Program.
- We did not factor in possible ramifications of funding ETIF given Maine's balanced budget requirement. Instead we assumed the funding required to make ETIF payments has no impact on funding for other State priorities.

OPEGA also assessed the degree to which adjusting these assumptions would impact the results of our economic analyses. The alternate assumptions we tested, and the results of those tests, are detailed below.

OPEGA considered the possibility that businesses whose 11th program year occurs within our analysis window maintain jobs until the end of the analysis window at no additional cost to the State.

When a business project that has created jobs reaches its 11th year since certification, it is no longer paid by the State based on qualified jobs and also discontinues reporting their employment. In many cases these jobs may continue beyond the reporting period and continue to provide benefits to the economy. Assuming these businesses maintain the number of qualified jobs reported in their 10th year through the end of our analysis horizon increases the estimated change to State tax revenue by 9.2%. Making this assumption drops the breakeven rate for the analysis from 11.52% to only 10.55%.

OPEGA considered deleting qualified jobs from the ETIF analysis that could be rationally claimed to have been created by other State programs rather than by the relatively small ETIF payment.

Businesses often avail themselves of more than one State program. As a result, determining the extent to which any single program caused the location or expansion of a business is problematic. Maine's economic development programs are administered by multiple entities, and there is no common database from which we can identify all the programs in which a business participates. OPEGA did, however, experiment with eliminating job years from the analysis which we know could rationally be thought to have been caused by other programs. This estimate only includes a small subset of these potential interactions and shifts ETIF's estimated breakeven point from 11.52% to 12.08%. Because a full accounting of program overlaps is not possible at this time, OPEGA did not pursue this option. Instead, OPEGA assumes that reported ETIF jobs are associated with only the ETIF Program and its maximum payment rate of 80% that is allowed by its interaction with the Pine Tree Development Zone Program.

OPEGA considered using an estimate of program attribution that does not hold government services constant.

The attribution rate used for this report assumes that government services are held constant. One could argue that an increase in businesses and employment, of which a portion would be from out of state, would increase the demand for government services. In OPEGA's analysis of the net effects on the State budget, government services were considered to be held constant for two reasons. First, government services for new businesses and new employees are primarily a municipal expense and so have only a diluted, indirect effect on the State budget. Secondly, approximately 28% of ETIF payments are for businesses that seemingly retained jobs rather than created new jobs. For these businesses demands for municipal services will be lower since retained jobs are less likely to prompt much out of state immigration and such businesses already receive municipal services. To quantify the effects of the assumption that the cost of government services remains constant, OPEGA re-estimated the attribution rate using data from Phillips and Goss (1995). They estimate that the elasticity of business behavior change is made less negative by 0.3 when public services are not assumed to be held constant. If OPEGA uses the resulting tax elasticity of -.2 instead of -.5, the attribution rate becomes 5.24% rather than 13.11%. Under this assumption, the ETIF Program would be expected to return only \$0.45 of State revenue for every dollar spent as compared to our estimate of returning \$1.14 of State revenue for each dollar spent.

## **Appendix B. Review of Literature Regarding Methods of Attributing Incentives as Causal Factors in Business Location and Expansion Decisions**

The question of whether a payment that is intended as an economic incentive actually incents a behavior, or whether that behavior would have occurred anyway, is central to determining the effectiveness of an economic development program. If projects that benefit from the program would have occurred even without program benefits, then a proportion of total program funds is being spent on projects that arguably do not need the benefits. This proportion of the program's funds could instead be returned to taxpayers or spent on other priorities. In either of these cases, the diversion of funds would not negatively affect the program outcomes. The difficulty is how to determine the proportion of projects that would occur even without the incentive. This effort to assess the likelihood that a program caused a change in business behavior is referred to as attribution, and it becomes even more problematic when projects are supported by benefits from multiple incentive programs, as is often the case in Maine.

State program evaluators and academic researchers generally agree that it is difficult to estimate the proportion of projects that would occur even without the incentive. Several literature reviews of the subject suggest there is no firm consensus of either attribution methods or results among researchers and practitioners (Office of Economic & Demographic Research, 2014), (Jin, 2015), (Bartik, 1991). Program evaluators in Maryland, however, found that with regard to attribution results “[m]ost research indicates that a majority of businesses receiving credits would have expanded or hired employees even if the business did not receive a tax benefit for doing so” (Maryland Department of Legislative Services, 2014, p. 32). Absent a generally accepted attribution method, evaluators and researchers have varied approaches.

One attribution approach calculates the economic benefits associated with an incentive program under various assumptions of the proportion of projects that would not have occurred absent the program's benefits. A 2014 evaluation of tax credits and abatements by the state of Connecticut reported impacts as if 0%, 20%, 50% and 100% of the project expenditures were due to the incentive (Connecticut Department of Economic and Community Development, 2014). That evaluation asserted that the extremes of 0% or 100% were unlikely, but made no claims about the likelihood of any percentages in between. This approach was also used in an evaluation commissioned by the Maine's own DECD (Investment Consulting Associates, 2016).

Other common attribution methods include surveys and econometric or statistical analyses. The survey approach tends to base conclusions upon the idea that there are many different reasons for a firm to locate or expand in a state. The survey attempts to ascertain these major factors and assess whether the government incentives might be among them for program participants. Econometric approaches tend to use more indirect, data driven methods to estimate the degree to which incentive program payments may cause changes in business behavior.

### **Survey Methods**

The decision to locate or expand a business in an area is based on factors such as available infrastructure, permitting issues, workforce quality, utilities, land availability, taxes, quality of life and economic incentives (Offices of the Florida Legislature, 2014). Conducting a survey of participating businesses regarding the importance of each of these factors is a method of estimating the degree to which an incentive impacted business behavior. One of the most detailed analyses involving surveys OPEGA identified was commissioned by the North Carolina General Assembly (Lane and Jolley, 2009). The study included companies that *do not* receive incentives along with companies that do. Lane and Jolley write:

The survey revealed several interesting findings about the perception of incentives among North Carolina businesses. Incentives ranked well below other factors such as skilled labor availability, highway access, tax rates, and regulatory climate. Incented businesses ranked incentives 12<sup>th</sup> and non-incented ranked incentives 13<sup>th</sup>, respectively. Surprisingly, 62% of surveyed NC executives were unaware that their company received an incentive. This lack of awareness by a majority of executives indicates that incentives in the form of tax credits have little impact on business decisions. (p.24)



Surveying businesses regarding the degree to which incentives change their investment and hiring behavior yields reasonably consistent results among those reviewed. This appears to be the case even when respondents are surveyed about different programs in different states. Table 12 includes a short list of results from different states' surveys.

State	Program Reference	Percent of firms that say they would proceed without changes to the project even without the incentive	Percent of firms that say they would proceed, but at a smaller scale even without the incentive	Percent of firms that say they would not proceed, but for the incentive
FL	Offices of the Florida Legislature, 2014	22%	42%	36%
MN	Economic Development Research Group, 2014	18%	34%	48%
MN	Office of the Legislative Auditor, 2008	19%	50%	31%
VA	Accordino & Fasulo 2014	15%	31%	54%
Average		19%	39%	42%

The above percentages reflect the average of responses from program participants, each of whom were subject to varying conditions and incentive levels. These results tend to support the assertion that most companies would invest or hire at some level regardless of the incentive. The results show that 19% would proceed with the project without any changes even if an incentive is not granted. Another 39% would proceed without the incentive, but at a smaller scale. The remaining 42% of participants would not proceed without the incentive.

Well-designed surveys can provide information about incentive participants' preferences and possibly the factors upon which they base their location and expansion decisions. However, all surveys are subject to possible biases which must be understood to validly interpret the results. This is well stated in a report on the Minnesota Angel Tax Credit (ATC) by the Economic Development Research Group (2014) which is quoted below:

Surveys were carefully designed to obtain meaningful results; overall response rates were quite high; and based on characteristics that could be identified for both groups, the survey respondents were very similar to the full population. Nevertheless, the use of surveys has several important limitations related to the presence of bias:

- **Response bias** could have occurred when asking (potential) beneficiaries of the ATC program to describe how it affected their behavior, particularly if they hope to benefit from the program in future years and know their responses may affect decisions to extend the life of the program. This form of cognitive bias is best addressed by carefully wording questions about behavior and supplementing findings with secondary, non-survey-based information.
- **Non-response bias** could have occurred if survey respondents differed from (or were not representative of) the full population of investors and businesses being studied. Even if survey respondents are similar in many ways, they may not be representative in their answers to key questions (i.e., those who responded may differ in significant ways from those who chose not to respond). Also, despite high response rates, in some cases results are greatly affected by a very small number of respondents because not all respondents answered all questions. Non-response bias is *not* a cognitive form of bias, and is therefore addressed by maximizing response rates and, in some cases, supplementing findings with secondary, non-survey-based information. (p.9)

## Econometric Methods

Econometric methods can also be used to estimate a threshold for behavior change. The idea that incentives act, in essence, as tax reductions makes studying the effects of broad tax policy changes on business decisions applicable to the attribution challenge. One of the econometric approaches to measuring the effect of tax policy on business decisions focuses on the elasticity of business response to the incentive. Simply put, elasticity is a measurement of the effect of one economic variable on others. In this context, it describes the responsiveness of business activity to changes in tax policy, including the award of economic development incentives. For example, if the elasticity of certain business activity to state and local business taxes is -0.2, then a 10% reduction in state and local business taxes will result in a 2% percent increase in employment or general business activity. (Office of Economic & Demographic Research, 2014, p. A1-5)

Bartik (1991) has argued that there is a small response in business activity as taxes decrease with elasticities ranging from -0.1 to -0.6 and averaging about -0.3. He later re-estimated the average elasticity at about -0.2 based on work by Wasylenko (Bartik 2018). Phillips and Goss (1995, p. 329), in their meta-analysis of the literature, note that their “results generally support the conclusions reached earlier by Bartik.” Bartik (2018, p. 10) further notes that Phillips and Goss “show that holding public services constant makes the business tax elasticity more negative by -0.3, which implies an overall elasticity, holding public services constant, of -0.5.” This implies that a 10% reduction in effective taxes will result in a 5% increase in business activity when government services are held constant. The 5% increase in business activity is greater than the 2% increase in business activity expected in response to the same reduction in taxes when government services are **not** held constant. The smaller business response to tax cuts when government services are **not** held constant reflects the observation that, if budgets must be balanced, then an increase in tax cuts (or incentives) reduces funds available for other government services – such as public infrastructure or education – and that reducing funding for these services can have a negative effect on business location and expansion decisions.

To apply the elasticities to employment focused incentives, Bartik (2018) states that reductions in business costs can be thought of in terms of the “value-added” associated with a new plant or facility expansion. He defines “value-added” as “the difference between sales and the firm’s purchase of goods and services other than capital and labor. For example, “value-added” for a steel company is the value of steel sold, subtracting the cost of inputs such as iron and coal and electricity.” (p. 9) Bartik then states that because state and local business taxes average 5% of a firm’s value-added, a 10% tax cut due to an incentive is equivalent to 0.5% of value added ( $5\% \times 10\% = 0.5\%$ ). With an elasticity of -0.5, if an incentive is offered that is 0.5% of value-added, then we would expect to increase business activity, or to increase the probability of location or expansion in an area, by 5%. In conclusion, he states that since “an incentive of 1 percent of value-added will be roughly 2 percent of wages”<sup>29</sup> then an incentive which lowers costs by 2% of wages would alter location decisions enough to boost employment by 10%.

Some researchers have expressed skepticism about the econometric research. Wasylenko (1997) evaluated tax elasticities in numerous studies in a meta-analysis. Although he believes there is small effect of tax levels on interregional location behavior, he establishes numerous cautions and caveats. He states that “[t]he median values of these elasticity estimates cluster between 0.0 and -0.26, indicating not much responsiveness of economic activity among regions to business taxes. (p. 45) He further notes that “the results for the interregional effects of taxes on economic activity are not stable. Elasticity estimates range between the implausibly high values of -15.7 in one or two studies to positive 0.54 in others.” (p. 45) Based on 34 studies which examined business tax elasticities, Wasylenko concludes that “[t]axes do not appear to have a substantial effect on economic activity among states.” (p. 47)

<sup>29</sup> This is based on statistics for export-based businesses (Bartik, personal communication). See Bartik (2017) Table 3.

Jennifer Weiner (2009), of the Federal Reserve Bank of Boston, isolates some of the reasons for skepticism which tend to reflect the belief that the econometric methods may even *overstate* the effects of taxation on behavior. She relates that the authors of these studies note that the studies suffer from serious measurement difficulties, potential endogeneity<sup>30</sup> problems and a lack of contextual information regarding how taxes affect different industries and local economies. She further states:

The finding that taxes have a statistically significant effect on economic activity has also proven fragile. Various attempts to replicate studies showing that taxes affect business activity have found the effects disappear when analysts use slightly different data. (p. 18)

Weiner (2009) notes another caveat that strongly affects more rural states like Maine. She says that both Bartik's and Wasylenko's reviews concluded that taxes have a bigger impact *within* metropolitan areas and that this is not surprising since other factors such as labor force quality and energy costs tend to be more similar within a metropolitan area. This would mean that "tax differences are likely to play a more influential role in business decisions" (p. 18) in metropolitan areas.

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<sup>30</sup> Broadly speaking, this is when the explanatory variable is correlated with the model's error term. This can occur for numerous reasons, and results in biased estimates. One reason relevant to these econometric studies is that participants self-select into the programs. This makes it difficult to determine if the program causes the increase in economic activity, or if businesses which enter into the program are those that are either planning expansions or are more likely to expand.

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## Appendix C. GOC Approved Evaluation Parameters

### Parameters for OPEGA's Full Evaluation of the Employment Tax Increment Financing (ETIF) Program as approved by the Government Oversight Committee 1-22-16

Established	Statute(s)	Type	Category	Est. Revenue Loss
1996	36 MRSA Chapter 917	Income Reimbursement	Business Incentive, Job Creation	FY16 \$13,289,000 * FY17 \$13,949,000 *

*Source for Estimated Revenue Loss: Maine State Tax Expenditure Report 2016 – 2017, adjusted by OPEGA to remove \$722,000 per year estimated attributable to the Brunswick Naval Air Station and Loring Job Increment Financing Fund programs.*

#### Program Description

Employment Tax Increment Financing (ETIF) is a program that reimburses approved, for-profit businesses 30-50% of the Maine state withholding taxes paid on behalf of qualified employees. The reimbursement rate goes up to 80% for Pine Tree Development Zone certified businesses. To qualify for ETIF a business must:

- have plans to hire 5 or more new, full-time employees over a two year period; and
- offer each new employee health and retirement benefits and an annual income higher than the most recent annual per capita personal income in the county where the employee works.

The portion of withholding taxes a business is eligible to be reimbursed for is based on the level of local unemployment. The withholding taxes refunded may only include the standard amount required to be withheld, not any excess withholding.

Only for-profit businesses may receive ETIF reimbursements, and retail businesses are eligible only under very limited circumstances. Businesses in Pine Tree Development Zones (PTDZ) are automatically approved for the ETIF Program as part of their PTDZ application, with a minimum of at least 5 new hires. Once approved, businesses may continue to claim the reimbursement for up to ten years.

The Department of Economic and Community Development (DECD) assists businesses with the ETIF application process and is authorized to approve qualified applicants. Under statute the State Economist is charged with reviewing ETIF applications and providing an advisory opinion to assist in DECD's approval decision. The State Tax Assessor is responsible for calculating the actual reimbursement due to approved businesses and authorizing payment. In addition, under 36 MRSA §6761 the Assessor may audit business recipients of ETIF. This program may not exceed \$20,000,000 annually (adjusted by the % change in CPI from 1996 to the date of calculation).

#### Evaluation Parameters Subject to Committee Approval

The following parameters are submitted for GOC approval as required by 3 MRSA §999 subsection 1, paragraph A.

##### (1) Purposes, Intent or Goals

Intent — To encourage the creation of net new quality jobs in this State, improve and broaden the tax base, and improve the general economy of the State.

Goal — To encourage the creation of net new quality jobs.

##### (2) Beneficiaries

Primary Intended Beneficiaries — For-profit businesses that create new quality jobs

Secondary Intended Beneficiaries — Job-seekers

**(3) Evaluation Objectives**

Below are the objectives the evaluation proposes to address. The objectives are coded to indicate which of the performance measures in section (4) below could potentially be applicable.

Each objective will be explored to the degree possible based on the level of resources required and the availability of necessary data. Any substantial statutory changes since the program's enactment will be considered in addressing objectives impacted by those changes.

<b>Objectives Allowed Under 3 MRSA §999 subsection 1 paragraph A</b>	<b>Applicable Measures</b>
(a) The fiscal impact of the tax expenditure, including past and estimated future impacts;	C, D, E Qualitative
(b) The extent to which the design of the tax expenditure is effective in accomplishing the tax expenditure's purposes, intent or goals and consistent with best practices;	Qualitative
(c) The extent to which the tax expenditure is achieving its purposes, intent or goals, taking into consideration the economic context, market conditions and indirect benefits;	A, F, I, J, L Qualitative
(d) The extent to which those actually benefiting from the tax expenditure are the intended beneficiaries;	A, B, L, J Qualitative
(e) The extent to which it is likely that the desired behavior might have occurred without the tax expenditure, taking into consideration similar tax expenditures offered by other states;	C, G, M Qualitative
(f) The extent to which the State's administration of the tax expenditure, including enforcement efforts, is efficient and effective;	Qualitative
(g) The extent to which there are other state or federal tax expenditures, direct expenditures or other programs that have similar purposes, intent or goals as the tax expenditure, and the extent to which such similar initiatives are coordinated, complementary or duplicative;	Qualitative
(h) The extent to which the tax expenditure is a cost-effective use resources compared to other options for using the same resources or addressing the same purposes, intent or goals; and	C, D, E, F, H, K, M Qualitative
(i) Any opportunities to improve the effectiveness of the tax expenditure in meeting its purposes, intent or goals.	Qualitative

OPEGA will perform additional work as necessary, and as possible within existing resources, to provide context for OPEGA's assessment of this program in Maine, including review of literature or reports concerning these programs nationally or in other states.

**(4) Performance Measures**

Performance measures are coded to indicate which of the above objectives they could potentially help address. Measures will be calculated to the degree possible based on the level of resources required and the availability of necessary data.

A	# Total businesses receiving ETIF reimbursement
B	Participation rate (% of Maine businesses certified for the program)
C	Total \$ value of reimbursements paid to businesses
D	Total direct program cost (direct tax revenue lost plus administrative costs)
E	Net impact on State budget (using economic modeling, as possible and appropriate, to include capture of indirect benefits and costs)
F	Total \$ value of payroll and benefits associated with new quality jobs created by businesses receiving ETIF reimbursement
G	Average tax reimbursement per business, including min & max
H	Leveraging Ratio, for example [ $\$$ of payroll & benefits associated with new jobs]/[Total direct program cost]

I	Indicators of economic impact in targeted business/industry or geographic area (i.e. jobs created, GDP – using economic modeling, as possible and appropriate, to include capture of indirect benefits and costs)
J	# New quality jobs created by recipients of ETIF reimbursement
K	Cost per new quality job created, for example $[\text{Total direct program cost}]/[\text{\# new quality jobs created by recipients of ETIF reimbursement}]$
L	Comparison of actual wages and benefits for qualifying jobs to minimum requirements
M	Return on Investment, for example $[\text{\$ amount reimbursed to businesses}]/[\text{\$ value of payroll and benefits associated with new quality jobs created by businesses receiving ETIF reimbursement}]$

Performance measures would typically be calculated by year to allow for analysis of percentage changes year over year, trends, etc. Further calculations and breakouts that would be considered, as appropriate, include:

- per beneficiary,
- comparison to industry or geographic trends,
- comparison to time period preceding program implementation or receipt of program benefits,
- by new vs. continuing beneficiary,
- by county,
- by firm size,
- by job type (FT, PT, temporary, permanent), or
- by industry.