THE PEW CHARITABLE TRUSTS

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February 23, 2021

RE: HB 1086, Maryland Tax Credit Evaluation Act – Alterations
Bill Position: Informational

Dear Chair Kaiser and members of the committee:

Thank you for your ongoing efforts to ensure Maryland's tax credit evaluation process produces detailed, high-quality evaluations and evidence-based policy decisions. Maryland consistently has been a leader in tax incentive evaluation since implementing its process in 2012 – a commendable accomplishment.

The Pew Charitable Trusts has supported states' efforts to evaluate their tax incentives since 2012. We provide technical assistance to states across the country with designing evaluation processes and, once those systems are in place, we help ensure evaluations draw clear, well-supported conclusions. Finally, we help policymakers understand and use these findings to inform policy decisions. We appreciate the opportunity to provide the Department of Legislative Services (DLS) with research and technical assistance and Delegate Luedtke's invitation to present at the November 6 House of Delegates' Revenues subcommittee briefing on tax credit evaluation.

While Pew remains neutral on HB 1086, our research provides useful context as lawmakers consider changes to the state's evaluation process. Below we discuss four aspects of the bill, how they relate to our research, and what we have observed in other states with evaluation processes.

First, the bill increases the scope of the evaluation process to include exemptions and preferences. Current law defines select credits that must be evaluated according to a specific schedule. Expanding the scope to include other types of expenditures can provide a more complete picture of costs, effectiveness, interactions between programs, and whether they contribute to the state's economic development goals.

Our research has found that, at a minimum, states should evaluate all major economic development tax incentives and ensure that newly created expenditures are also evaluated. This enables analysts and lawmakers to compare results across programs. Many states, like Indiana, Nebraska, and North Dakota, conduct evaluations on tax incentives that are "generally" available to businesses.

Second, the bill adjusts the evaluation schedule. Current statute requires DLS to follow the enumerated schedule and re-evaluate credits every seven years. The proposed legislation requires that DLS evaluate the cybersecurity investment incentive by July 2023 and, beginning in October 2022 and in conjunction with the Senate Budget and Taxation and House Ways and Means

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committees, establish a schedule to evaluate "each income tax credit primarily claimed by business entities" with an annual fiscal impact in excess of $5 million every ten years. Evaluations of other credits, exemptions, or preferences, or an aspect of a state tax credit, exemption, or preference must be requested.

Our research emphasizes the importance of conducting continuous and rigorous reviews of all major economic development tax incentives to ensure that lawmakers receive up-to-date information and analysis. The benefits of expanding the scope may be limited if some expenditures are not subject to regular reviews. This is particularly true for programs that offer multiple types of credits. For example, Maryland's enterprise zone program includes both a property tax credit and income tax credit. According to DLS' recent evaluation, the majority of the fiscal impact is from the local property tax credit which, as the legislation is currently framed, would not be subject to regular evaluation.

Indiana, for example, evaluates its enterprise zone program and related tax incentives together as part of the state's seven-year review cycle. Among other things, the report compares fluctuations in claims among the enterprise zone employment expense income tax credit, employee income tax deduction, and property tax investment deduction. Evaluating these in isolation would not provide a full picture of the program's size, cost, or effectiveness, nor would it reveal how individual components of the program interact or overlap.

Third, the bill allows for each previously evaluated income tax credit to undergo an "expedited" review, provided that it has not been substantially altered in the intervening years. This has been useful in other states that seek to balance the need for regular and thorough reviews with staff capacity and workload.

Maine's evaluation law implements this approach. "Full evaluations" include detailed analyses of empirical results. "Expedited reviews" are intended for expenditures that serve well-established tax policy principles (avoiding double taxation, for instance) and focus on their goals and whether they are still relevant. As a result, evaluation staff can focus their resources on the nuances of programs intended to incentivize specific behaviors or groups and analyze how effective they are in achieving their goals. Washington, which has one of the longest-standing and robust evaluation processes, also uses tiers to guide the level of review required for each tax preference as part of its ten-year cycle.

Fourth, the bill proposes to eliminate the public hearing requirement for the evaluation report. Our research shows that states with strong report review provisions, like dedicated hearings or interim studies, are more likely to yield substantive policy discussions and reforms.

Many states require committees to hold at least one hearing to discuss evaluation findings. Some, like Connecticut and Washington, holding hearings through their fiscal committees. Maine's

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government oversight committee oversees evaluations by the Office of Program Evaluation and Government Accountability and holds hearings on each of its reports. North Dakota and Oklahoma have found value in holding a series of hearings for each round of evaluations, allowing for in-depth discussions about each expenditure as well as evaluation results.

Maryland's current evaluation process has consistently yielded high-quality and thoughtful evaluations and the evaluations have translated into meaningful policy decisions. As the state looks at iterative revisions to its evaluation process, we at Pew are happy to further discuss this topic with you or provide technical assistance. Thank you.

Sincerely,

Khara Boender
The Pew Charitable Trusts