Long-term Rural Facilities Incentive

ORS 317.124 - 317.131	Year Enacted:	1997	Transferable:	No
	Length:	5 to 15 years	Means Tested:	No
	Refundable:	No	Carryforward:	5-year
TER 1.418	Kind of cap:	None	Inflation Adjusted:	No

Policy Purpose

Statute does not contain a specific policy purpose statement for this tax credit. While this policy was first implemented by the 1997 legislature (HB 2143), it was notably modified by the 1999 and 2001 Legislatures (SB 245 and HB 2103, respectively). None of the bill documentation for the three pieces of legislation specifically contains a purpose statement. Given the focus of the policy, however, it seems clear the intent is to alleviate chronic unemployment and low incomes in Oregon's rural areas. Also, this tax credit is designed to work in conjunction with a property tax exemption in the same rural enterprise zones. The implementing legislation for that exemption also lacks a specific policy purpose statement. However, it is reasonable to assume that these policies are an extension of the broader legislative policy pertaining to enterprise zones. In short, that policy is "... to stimulate and protect economic success in such areas of the state..."

Description and Revenue Impact

Eligible corporate taxpayers that make a large investment in a facility that is exempt from property taxes due to its location in a Long-Term Rural Enterprise Zone are eligible for a tax credit equal to 62.5 percent of the payroll costs during the tax year attributable to the exempt facility. Payroll costs include employee salaries, wages, benefits, and payroll taxes. The credit must be approved by the Governor. The duration of the tax credit can be at least five years but no more than 15 years. The credit may be only used to reduce tax above a threshold amount. In general, the threshold amount is $1 million of actual taxes paid; however, it may be lower under certain circumstances. The tax credit is nonrefundable but may be carried forward for five years.

Businesses operating in a qualifying county may be eligible for this credit if they meet minimum requirements for amount invested, new hires, and compensation. The amount of the incentive depends on the amount of investment, the average compensation of new hires, the number of new hires, the county population, and the distance of the business from I-5. The table below provides the schematic for the incentive.

	County Population and I-5 Corridor			
	< 10,000	10,000 to 40,000	> 40,000	
			Not I-5 Corridor	I-5 Corridor[1]
Investment[4]	$12.5M / 0.5% of RMV			$25M or 1% RMV
Hires[2]	10+	35+	50+	75+
Pay[3]	at least 150% of county wages			
Credit	$10,000 per hire	$12,500 per hire	$15,000 per hire	

[1] Within 10 miles of Interstate 5
[2] By the end of three to five years
[3] By the end of the fifth year
[4] If the investment is at least $200 million, standard compensation requirement, and at least 10 miles from I-5, then the hiring threshold is 10

To estimate the tax liability associated with the eligible facility, the corporation's state tax liability is multiplied by the income attributable to the facility as a share of the business' total Oregon income. If income information is not available, then the apportionment percentage is the average of the similarly calculated payroll and property factors. If the tax credit is granted, then 30 percent of corporate excise taxes collected by the state with respect to the exempt facility are rebated to the local taxing districts. As an example, the tax credit calculations for a hypothetical firm are shown in the following table.

Corporation (gross) tax:	$2,500,000
Payroll at the eligible facility:	$900,000
Net income of the facility:	$5,000,000
Net income in Oregon:	$25,000,000
Apportionment percentage:	20% = $5M/$25M
Potential tax credit:	62.5% * $900,000 = $562,500
Threshold:	$1,000,000
Tax available for offset:	($2.5M - $1M)*20% = $300,000
Credit to claim:	min($300,000 or $562,500) = $300,000
Carryforward:	$562,500 - $300,000 = $262,500

Due to the low number of potential claimants, the public nature of the related property tax exemption, and the requirement that the tax credit be granted by the Governor, the use and revenue impact are considered confidential information and may not be included in this report in accordance with taxpayer privacy disclosure laws.

Policy Analysis and Other Issues

Because the policy objectives of the three enterprise zone tax credits included in this section are substantially similar, the policy analysis is provided once at the end of this section, following the Electronic Commerce tax credit.

Tribal Enterprise Zones

ORS 285C.309	Year Enacted:	2001	Transferable:	No
	Length:	1-year	Means Tested:	No
	Refundable:	No	Carryforward:	None
TER 1.419	Kind of cap:	None	Inflation Adjusted:	No

Policy Purpose

Statute contains legislative findings in ORS 285C.303 that state, in part, that the purpose of this tax credit is “...to remove the tax disincentives that currently inhibit private business and industry from locating and operating enterprises within the boundaries of the rural Indian reservations of this state.”

Description and Revenue Impact

Taxpayers operating a new business facility in a reservation enterprise zone or a reservation partnership zone are allowed to claim a tax credit equal to the amount of tribal property tax paid. If the business has not previously operated within the zone, the tax credit is equal to tribal taxes paid during the tax year. The credit is nonrefundable and may not be carried forward. Also, the credit is only allowed for taxes that are imposed on a uniform basis within the tribal territory.

The number of claimants has varied over the years. In some years, the data represent too few taxpayers to disclose. On average, between 2005 and 2014, roughly 15 taxpayers claim about $15,000 in tax credits each year and are able to reduce their Oregon tax liability by about half that amount.

Policy Analysis and Other Issues

Because the policy objectives of the three enterprise zone tax credits included in this section are substantially similar, the policy analysis is provided once at the end of this section, following the Electronic Commerce tax credit.

Electronic Commerce Enterprise Zone

ORS 315.507	Year Enacted:	2001	Transferable:	No
	Length:	1-year	Means Tested:	No
	Refundable:	No	Carryforward:	5-years
TER 1.420	Kind of cap:	Taxpayer	Inflation Adjusted:	No

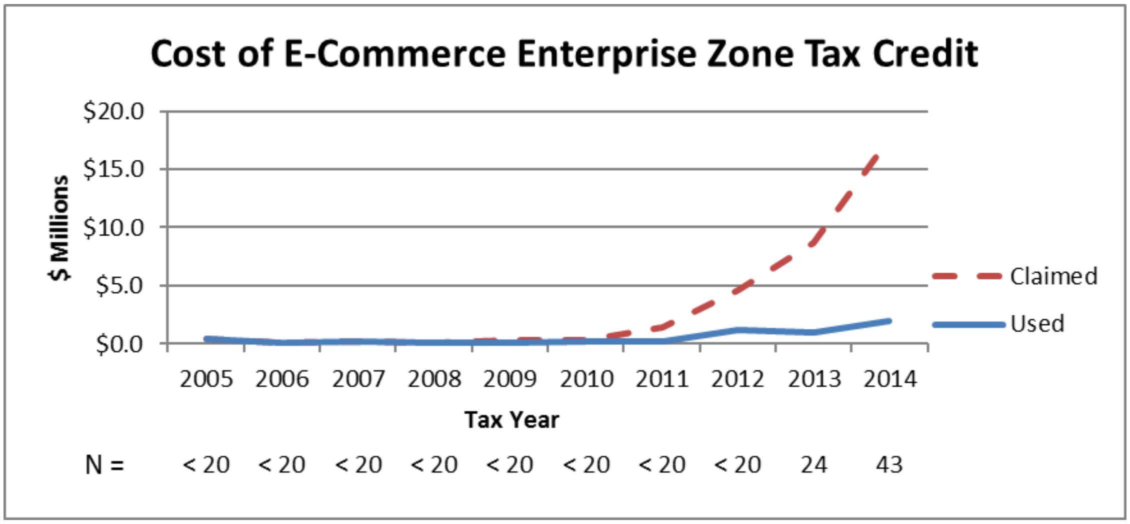
Policy Purpose

Statute does not contain a specific purpose statement for this tax credit. The documentation for the implementing legislation indicates that this policy was recommended by the Oregon Internet Commission in 2000. Their final report organized issues into four core areas: people, electronic government, business infrastructure, and legal infrastructure. The creation of Electronic Commerce Zones (ECZ) was part of the business infrastructure analysis. The key policy of the ECZ was the creation of a tax incentive to promote investments in electronic commerce activities. Because these zones were limited to existing enterprise zones, it seems reasonable to infer that the intent, at least in part, was to improve employment opportunities and increase incomes in areas of economic distress in Oregon. Given the source of the recommendation, the intent appears to include the goal of infrastructure improvement. As stated in the report, "[i]ncentives are needed to spur more e-commerce capital investments in Oregon than market forces would by themselves dictate, particularly (but not exclusively) in rural communities." It is, in effect, a capital investment policy with very specific targets, namely, internet-based businesses.

Description and Revenue Impact

Businesses that engage in electronic commerce within a designated "electronic commerce zone" are allowed an income tax credit equal to 25 percent of certain capital investments. To be eligible, the qualifying investments must be within an e-commerce zone and used in e-commerce operations related to e-commerce sales, customer service, order fulfillment, or broadband infrastructure. Also, the business must be exempt from property taxes through the state's broader Enterprise Zone program. The maximum amount that may be claimed each year is $2 million (plus any carryforward) per taxpayer.

The sponsor of an existing EZ is allowed to designate the zone for e-commerce, but the designation is not final until approved by the OBDD. The total number of e-commerce zones in the state is limited to 15 and the program is currently fully subscribed; eight of these are urban zones and seven are rural zones. The chart below shows the use of these tax credits between 2005 and 2014. Use of the tax credit was limited to about a dozen taxpayers each year until 2009. The number of claimants gradually doubled by 2013. In 2014 the number of claimants nearly doubled again. The amount claimed has significantly increased since 2011 while the amount used to actually reduce tax liability has leveled off at roughly $1 million per year. Much of the growth in the amount claimed appears to be a buildup of tax credit carryforwards.



Other Issues

For the most part, these tax credits are self-administered. To the extent there are administrative costs, they are largely born by the OBDD, mostly for the LTRI and E-Commerce zone tax credits. The DOR does incur some incremental costs, but they are generally associated with audit activity. The lack of administrative oversight may actually be a source of uncertainty for businesses. There may be some value in exploring a minimal amount of certification.

Many other states have enterprise zone programs. Highlights are include in the relevant table in Appendix B.

Key Characteristics of Tax Credits Offered by Other States

- Property tax exemption
- Investment tax credit
- New hires tax credit

Policy Analysis

Society is arguably better off if economic success is shared by all areas. In reality, however, it has been the case that economic growth has not been uniformly distributed. Consequently, long standing attempts by policy makers have targeted areas where growth has lagged. By offering tax incentives, the goal is that costs from barriers to entry may be offset. Often such barriers are not easily identified, but potential sources could be a lack of transportation infrastructure, limited access to capital or labor, high crime rates, environmental concerns, or other social issues. The tax policies addressed here most directly affect the costs of capital and labor. The thought process is that reduced costs for business inputs will lead to increased business investments, which will lead to increased employment, economic activity and incomes in the area.

While EZ programs are, by definition, a very local economic development tool, they are usually fairly broad in their eligibility requirements. Somewhat contrary to this general characterization, the three income tax credits available to EZ businesses in Oregon are further targeted. First, the LTRI is limited to businesses that make large capital investments with employment requirements. Second, the Reservation tax credit is designed to avoid a kind of double taxation. The third tax credit, for E-commerce, is targeted to a kind of industry. Effectively, it is a policy that targets an industry within targeted geographic areas. Proponents will focus on the potential efficiency gains from this approach. Critics may argue the approach may be a bit constrained. Relatively speaking, few tax credits are claimed for the three policies, so potential analysis is currently limited. This report includes some analysis of E-commerce businesses, but most of this analysis discusses the pros and cons of the EZ tool, what lessons might be learned from existing research, and how they may be applied here in Oregon.

Enterprise zones (EZs) are a common economic development tool that have been implemented in many states in one form or another since the early 1980s. The premise is fairly straight-forward, but the program specifics vary a great deal. The common theme is a policy that consists of a targeted, geographical approach to economic development. Proponents argue that areas of economic distress can be improved by reducing taxes in a targeted manner. Common indicators of economic distress include high or chronic unemployment rates, significant or sustained job or population losses, low incomes, high vacancy rates for business property, and low property values. In exchange for receiving the tax incentives, companies are often required to make certain capital investments or meet certain hiring targets. The jobs requirement may sometimes be further targeted to local residents, certain wage levels, or disadvantaged workers. For the most part, EZ policies provide property tax breaks, sales tax exemptions, low-interest loans, and, of course, tax credits.

Analysis on this subject ranges from academic research published in refereed journals to state-level analyses of individual programs. Collectively to date, the research results have not been overwhelmingly conclusive and tend to find little support for job creation. Some of the research focuses on property tax abatements, which are effectively an investment incentive. In some cases, the policy could actually work as an incentive to substitute capital for labor. This may explain some of the mixed results reflected in the literature.

It is important to note, that because these policies are locally crafted, caution should be used when applying research results from other states to Oregon's programs. It could be that there is too much variation across programs and that programs are so idiosyncratic that economic models have not been able to accurately capture their impacts. Also, the impacts may not outweigh the general "noise" of available data. The point of examining research on other programs is not to find a successful program and copy it, but rather to understand why certain programs succeed or fail in different was. Understanding program details and why they're effective is likely to provide valuable information as Oregon evaluates and works to improve programs here.

When evaluating development policies, it is valuable to be as clear as possible about what is meant by economic development. Often it is used as a euphemism for job growth. However, as Bartik (2012) states, it is more accurately described as a means to an end, "job growth is not a good in and of itself." Even in healthy economies, there is a certain amount of churning as business are born, grow, and then die. The larger policy intent is that job growth leads to other societal benefits. Support for such public policies are arguably based on the notion that the societal benefits exceed their costs. It's also worth noting that some economists have suggested that a lower rate of growth may be the new normal, so to speak. If that is, in fact, the case then policies should be crafted with that landscape in mind.

Given the long history of state EZs, there is extensive literature on the subject. Unfortunately, stakeholders and researchers have not yet come to a clear consensus on program impacts. While some studies conclude that there can be a net positive impact, most lean toward the opposite, finding little or no benefit. In fact, Greenbaum and Landers (2009) argue that there is little evidence that these policies have succeeded and they explore why states continue to implement such programs. The authors suggest the need for a stronger link between academic research and the state policymaking process.

An example of a study that showed little impact on employment was conducted by Kolko and Neumark (2009). They studied California EZs and found that, overall, they did not result in an employment increase. They posit that the lack of (an overall) employment increase could be due to a shift from labor to capital as a result of the investment incentives or that employment simply shifted to disadvantaged workers. They did, however, find variation in performance across the zones. They found that zones with a lower share of manufacturing, or zones where managers conducted more marketing and outreach experienced more favorable results.

Elvery (2009) studied the EZ programs of California and Florida that focused heavily on hiring tax credits. He found no measurable impact on employment of residents living within the EZs themselves. He actually found negative impacts when he did not control for EZ resident characteristics. The impact results did improve when controlling for such characteristics. The author posits that studies that do not consider such factors may show results that are biased downward to some degree. He also suggests that a possible explanation for the lack of a measurable impact could be that a longer time horizon is needed to realize employment gains.

Ham, et. al. (2011) studied state enterprise zones (including Oregon's), federal empowerment zones, and federal enterprise communities. In contrast to other research, they found positive and statistically significant impacts on unemployment rates, poverty rates, share of income due to wage and salary, and employment. They noted that the impacts of the federal programs were much larger than those of state programs. Their research also showed some positive spillover effects in census tracts that neighbor the zones.

Other research has examined federal and/or state enterprise zone programs exploring impacts other than simple employment growth. Hanson and Rohlin (2011) examined federal empowerment zones and found that a wage credit attracted a net of just over 2 new establishments per 1,000 existing establishments. This growth is strongest in retail with some growth in the service sector. The growth was partially offset by declines or slower growth in other sectors. Reynolds and Rohlin (2014) also studied the federal empowerment zone program and found that the tax incentives enhanced the quality of the business environment for local firms and modestly improved the quality of life of residents.

Finally, Engberg and Greenbaum (1999) examined state enterprise zone programs in Florida, Pennsylvania, and Virginia. They explored the idea that increases in economic prosperity would be capitalized in higher housing prices. In two of the programs they found an increase in home ownership and occupancy rates attributable to the programs. In terms of a net effect, however, they found that housing prices did not change because corresponding reductions in employment offset those gains.

Several states have conducted evaluations of their EZ programs. Maryland, for example, concluded that tax credits were not effective at increasing employment for zone residents. They attributed the ineffectiveness primarily to labor mobility issues and a basic skills mismatch. The job skills and education levels demanded by businesses did not align with those possessed by the local labor supply. They suggested that the program could be improved by coordinating efforts with other services, such as job training programs. They also suggested that the program could be improved by specifying clear, desired outcomes along with quantifiable metrics. A key factor would need to be the collection of quality, uniform data.

New Jersey's analysis of their program concluded that it was "...bureaucratically cumbersome and costly to operate..." As a result, the state experienced inconsistent results regarding business expansion and job creation. The authors recommended significant program restructure. Their goal is to reduce administrative burdens, introduce a competitive process for the limited incentives, and increase accountability through the effective use of metrics.

In a review of their program, Louisiana identified opportunities for program improvement. The authors suggested clarifying the requirements for identifying additional, permanent jobs. They wanted to ensure that jobs credited to the EZ were not simply relocated from elsewhere in the state or from an acquired business. One key step they identified was the establishment of an employment baseline based on the recent history of the business. Such a baseline defines the context for a reasonable expectation of job gains and, potentially, jobs retained.

Florida found that their program produced a negative return-on-investment to the state because the program primarily shifted economic activity within the state. However, they did find positive property value gains that indicated positive results for local governments and their ability to provide services.

The full body of existing research is much too extensive to fully summarize, but the work described here provides a general flavor. The fundamental issue for Oregon revolves around what can be said about Oregon EZs. The Legislature commissioned a study in 2009, coordinated by the Legislative Revenue Office, that examined the property tax exemptions offered in EZs. That study found some evidence that suggested a positive impact on jobs. The focus here, however, is on the three income tax credits. First, for the LTRI, unfortunately, little can be shared publicly due to confidentiality concerns. What can be said is that nine businesses currently participate in the LTRI property tax program. The table below shows data taken from the Oregon transparency website. Roughly speaking, the participating companies have been exempted from paying about $30 million in property taxes for each of the last two tax years.

Property Tax Exemptions, $M

Company	2014-15	2015-16
Apple	$0.9	$4.5
Facebook	$15.7	$11.9
Murphy Company	$0.4	$0.4
Roseburg Forest Products Co	$0.4	$0.4
Columbia River Processing, Inc	$0.6	$0.5
Upper Columbia Mill, LLC	$0.3	$0.2
Conagra Foods Lamb Weston, Inc	$2.9	$3.9
Columbia River Technologies, LLC	$1.3	$1.3
Google	$6.8	$10.7
Total	**$29.3**	**$33.9**

According to the OBDD, fewer than five companies have received gubernatorial approval for the LTRI facility tax credit. The DOR publishes no data due to confidentiality concerns.

The Reservation Zone credit has not shown a significant revenue impact to date, with upwards of maybe one or two dozen claimants; the dollar impact has been less than $10,000 each year. In some ways it is analogous to the income tax credit allowed for taxes paid to another state. By allowing an Oregon income tax credit for any property taxes paid to a Tribal Government, Oregon has aligned its tax policy such that it has chosen to forego some tax revenue equal to amounts imposed by another government.

Some data for the third credit, E-commerce, is available for analysis. The number of claimants is still rather small, which is a limiting factor. However, the number of claimants has increased by roughly 300 percent, growing from about a dozen to over 40 in a decade. The amount of tax credits claimed did rise dramatically from 2011 to 2014.

The OBDD has kept track of available information regarding the EZ program. Since 2011, they have attempted to collect data specific to E-Commerce zones. The responses from applicants has been sparse, but is improving over time. For example, for property tax year 2016-17 OBDD was able to obtain nearly complete investment and jobs data. The table below contains a summarized version of that information. Sixty percent (62) of the 104 EZ businesses with investments in FY17 operated within an E-Commerce Zone. One-third (21) of those were E-businesses.

	Businesses	Investment ($M)		New Jobs		Total Jobs	
		Total	Average	Total	Average	Total	Average
E-Commerce Zones							
E-businesses	21	$176	$8.4	853	41	1,872	89
Other businesses	41	$354	$8.6	1,370	33	3,673	90
Other Zones	42	$576	$13.7	1,094	26	3,842	91
Total	104	$1,106	$10.6	3,317	32	9,387	90

Began in 2016; does not include all active exemptions

There are some lessons that can be learned from the experience of other states. One conclusion from the Maryland study was the recognition of the need for clear, desired policy outcomes. To the extent possible, outcomes should be associated with quantifiable metrics for which quality data can be collected in a complete and uniform manner. New Jersey also noted the value of metrics. They also acknowledged the value of low administrative burdens and potentially introducing a competitive process for incentive awards. Louisiana suggested the possibility of establishing a baseline forecast as a way of creating reasonable expectations of outcomes and providing context for subsequent policy evaluations.

In Summary:

Long-Term Rural Incentives	
Advantages	• Focus on economically distressed areas • Magnitude of labor subsidy • Tied to jobs and investment
Disadvantages	• Complexity • Potential inability to use
Potential Modifications	• Adjust tax credit parameters • Explore ability to improve job targeting • Simplify the rebate process (to local governments)

Reservation Zone	
Advantages	• Ease of administration
Disadvantages	• Potentially uncertain cost
Potential Modifications	• Eliminate sunset date

E-Commerce Zone	
Advantages	• Focus on areas of economic distress • Focus on technology growth
Disadvantages	• Limited to certain geographic areas
Potential Modifications	• Expand to more areas of the state and more industries • Make refundable • Incorporate a labor incentive • Include data collection process

Appendix C: Policy Questions

When reviewing the tax credit sunset extension bills and proposed new credits, the Joint Committee on Tax Credits intends to address the follow questions:

- What is the public policy purpose of this credit? Is there an expected timeline for achieving this goal?

- Who (groups of individuals, types of organizations or businesses) directly benefits from this credit? Does this credit target a specific group? If so, is it effectively reaching this group?

- What is expected to happen if this credit fully sunsets? Could adequate results be achieved with a scaled down version of the credit? What would be the effect of reducing the credit by 50%?

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

- Is use of a tax credit an effective and efficient way to achieve this policy goal? What are the administrative and compliance costs associated with this credit? Would a direct appropriation achieve the goal of this credit more efficiently?

- What other incentives (including state or local subsides, federal tax expenditures or subsidies) are available that attempt to achieve a similar policy goal?

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