House Committee on Economic Development – Informational Meeting

Overview of Tax Incentives

February 6, 2019
Salem, Oregon

Incentives … a marketing thing

- **Neither 'subsidy' nor corporate welfare, and not meant to make a project feasible or profitable, where it would not otherwise be**

- **Not merely the supply-side effect of an equal amount of general tax reduction in the case of incentives based on taxes**

- **Rather direct inducements to motivate** (at a particular juncture)

    1. Improve cash-flow spreadsheet, price points and perceived risks

    2. Most often for existing firms to stay and grow (particularly asymmetrical options, such as relocate nearby in order to expand)

    3. Inter-state/national competitiveness, too, but rarely bidding war

    4. Bolsters sense of community support …, *putting skin in the game*

- **Differing influence on phases of decision-making from initial winnowing of sites/basic options … to deal-closing**

- **Other economic development factors and efforts still indispensable**

Other business development tools

- **Local, state and (others') national efforts also aimed more at the needs of industries, businesses and projects**
- **U.S. states & localities generally have:**
  - Favorable debt financing, capital access or more equity-like infusions
    - Lower interest rate or otherwise unavailable capital (small business)
    - Tax-exempt private activity bonds under federal tax code
    - New markets tax credits (NMTC to leverage off of federal program)
    - **Opportunity Zones**
  - Worker placement and training services (often quite cost-effective)
  - Federal tax credits for hiring of targeted groups (namely, WOTC)
  - Property tax increment financing (TIF – urban renewal in Oregon)
  - Public infrastructure funds (project-specific w/IOF and some SPWF)
  - Site/land – quality/readiness certification & documentation, as well as brownfield remediation or risk control
  - Access to research and other such public/private resources
  - Interagency regulatory coordination
  - Export assistance and advisory service for lean manufacturing, *etc*.

… many often classified as "incentives," too, and depending on details & delivery, they can certainly serve equivalent ends

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Oregon's incentives policy

- **Exemptions on new taxable property predominate—**statutorily defined with local discretion/negotiation in many cases,
  … effectively biased toward (physical) capital
  … *a blunt instrument* in terms of public policy …, but tax base payback, too?
- **In addition for economic–business development:**
  - Very limited income tax program (no credits to speak of)
  - Upfront discretionary awards (Governor's Strategic Reserve Fund–SRF and Oregon Business Expansion & Retention Program–BEP)
  - Various local & state resources and services (previous slide)
- **Major emphases historically –** green energy (ENERGY TRUST; 2016 solar grants ¢/kWh), as well as economic hardship and rural areas of state
- **Targeted (often implicitly) by industries, geography, *etc*. –** competitive for retention and some recruitment …, but neither high-impact, state-level offering like elsewhere, nor overarching policy or metrics
- **Typically fairly simple and certain for businesses and seemingly provide economical, solid public return**
- **Local–State collaboration critical in a number of ways**

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Business location factors
—cost & certainty

- **Fundamental to be viable for growing anywhere:***
  - **L**ogistics (regionally, hard to affect) – freeways, airport, rail lines
  - **L**and/site/space—price/rent, access, utilities, development time
  - **L**abor—quantity, skills, diversity and relative cost … aging demographics!
- **Other price points**, such as energy prices, construction costs, and regulatory/non-tax expenses, fees or charges
- **Taxes—broad climate effect? … variable, project-specific factors**
  - Property (largely local) assessment … literally everywhere in U.S.†
  - Sales & use on capital and current purchases by business†
  - Income of corporations & owners‡
  - Payroll—withholding taxes (employee income), FICA, unemployment insurance, transit districts, and worker's comp insurance/disability
  - Other types—gross receipts, capital worth, real estate transfer

* Simpler symmetry in recruiting outside businesses (who will also talk to locals)

† Exemptions are more or less common, especially manufacturing equipment

‡ Credits on corporate/owner liability have been common … but usability issues

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Summary of property tax relief
—exemptions on essentially new plant & equipment, **not** land or existing assets

- **Strategic Investment Program** (SIP) **for really massive projects – 15-year *partial* exemption anywhere in state***
- **Most rural enterprise zones can also offer 7–15-year 100% exemption on all new facility property†** (unlimited construction-period exemption)
- **Standard enterprise zone, qualified property 100% exempt*, †**
  - Three years, *as-of-right* for eligible (nonretail) firms adding jobs in zone (10%)
  - With zone sponsor agreement, 1–2 extra years, subject to excellent employee compensation and now wages too ‡

* Following an up to two-year construction-period exemption, like what is also generally available statewide for at least manufacturing facilities

† Inside designated zone boundary, of course

‡ Except urban zones inside Salem and Portland metropolitan areas

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The players with exemptions

- **The State**
  - Department of Revenue – crucial support, valuation, little discretion
  - Business Oregon
    - In-house expertise technical assistance
    - Oversight of zone designations and SIP through Commission
    - Other programs and resources with retention, expansion or recruitment
- **Fundamentally local**
  - City, port, county governments with land-use, permits, infrastructure, *etc.*, as well as economic development officials or organizations …
  - Local zone managers—diverse group, important mktg. & admin. roles
  - County assessor offices—also diversity with respect to rurality, staffing and county sponsorship—but always essential for
    - Customer service, big and small projects when there are complexities
    - Tax impact estimations for typically larger prospects
    - Compliance & enforcement, sometimes unavoidable … and special reports!
- **Property taxpayer – business firm/customer**

Oregon Investment Advantage

- **Ten-year state tax holiday: Reduces income subject to taxes (above line – not credit), by subtracting proportion based on facility's share of business in state, starting at least 24 months after operations begin**

- **Required of business firm at time of preliminary application:**
  - Operations new/unique to facility and to that firm in Oregon (statewide)
  - Not competing locally with existing businesses

- **Must then also:**
  - Hire five or more full-time, year-round employees at facility
  - Compensate (including benefits) at least those five at ≥ **130% (outside MSA) or** 150% of county per capita income (at time of prelim. appl.) or ≥ 100% … with sufficient medical coverage (≍ local municipal employees)
  - **Average wage of five ≥ most recent county average wage**

- **Administrative certification through Business Oregon**

- **County eligibility changes a little year-to-year, combination of per capita income and unemployment rankings**

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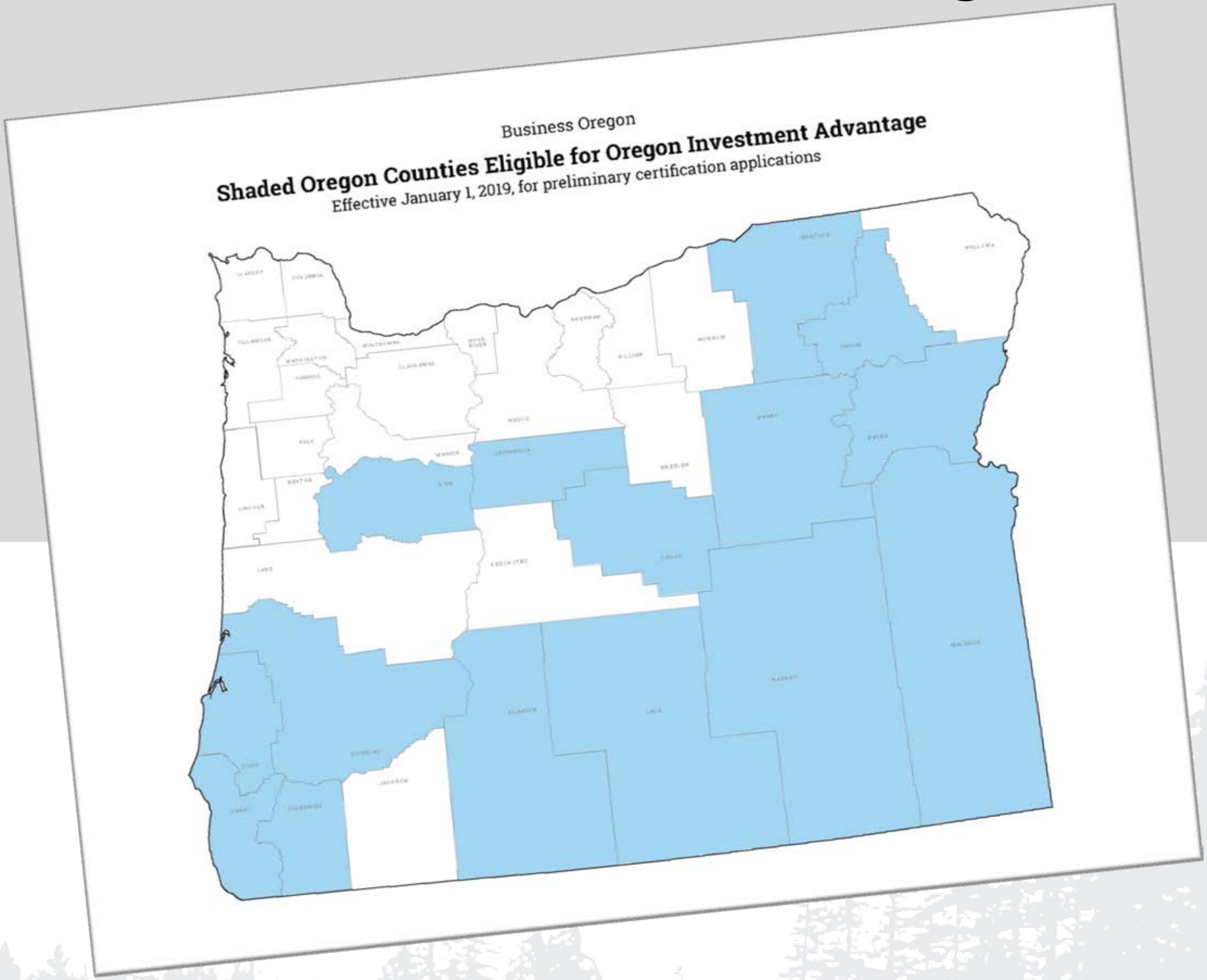
Eligible locations



Business location with preliminary application … also must be

- Industrially zoned land (inside or outside any city), *or*
- Within the UGB of small city (≤ 15,000 pop.), *or*
- Both.

Accountability–transparency

- **Maximize effectiveness & efficiency and fulfill public policy**
- **Good and Best Practices with businesses, examples:**
  - Program forms/steps before and after performance for criteria or data
  - Clear and upfront regarding performance & enforcement measures
  - With more discretionary situations—
    - Planning ahead about objectives for negotiations
    - Due diligence of business case, risks, *etc.* … benefit–cost analysis and relative but–for considerations, as applicable & warranted
    - Robust agreements (binding contract)
  - Consider overall deal and coordination among agencies and levels of "guberment" in terms of total offerings, services & so forth
- **Issues**
  - Beyond operational duties with respect to compliance, technical resources are lacking at state level and among diverse local settings
  - Applicability with what we do in Oregon? …, unlike many other states, our incentives tend to be decentralized, programmatic, …
  - Various helpful & hostile organizations nationally, academics, agendas, …

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Public information

- **Communication and openness are part of accountability …** nevertheless, data limitations, short attention spans aside from activists, and lack of systematic/automatic reporting methods from users
- **Transparency** **WEBSITE** (DAS–CIO) — economic development page
  - Useful with annual agency reports and composite assessor reports
  - Can be disjointed and messy, with no budget, rough data and laws based on broad-brush presumptions disconnected from program realities
- **Business Oregon efforts** **ONLINE** **and national organizations**
- **Governmental Accounting Standards Board** (GASB), Statement No. 77
- **Public records requests** for what government agencies possess
  - Proactive education and sharing with media & others is best, but …
  - ORS 192 exemptions as necessary and required confidentiality (NDAs?)
    - Personal finances, marketing info, *etc*., generally with economic development
    - Preliminary/pre-investment numbers, specially with Strategic Investment Program, and enterprise zone compensation figure and property schedules
    - Promises with certain voluntary submissions, “trade secrets,” … ?
    - Check with counsel and avoid appearing unnecessarily secretive

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Program evaluation

- **More program-level metrics & analytics are certainly desirable**—in terms of quantified outcomes or estimated return on investment (ROI)? …, rather than the odd headline or who's receiving what
- **Currently found with:**
  - Tax expenditure report (TER/DOR) since 1997, great info but program benefits often addressed qualitatively; vast document … all sorts of stuff
  - Business Oregon budgetary reporting*
  - Legislative efforts – *ad hoc* at times and tax credit **sunset** cycle (LRO)
  - Secretary of State audit and HB 3377 – county reporting, long-term zone
- **Challenges:**
  - Thin staffing and no funds for independent, quality investigation
  - **Data** reality and resources (as with project-level transparency)
    - Systems based on paper or PDFs, not on-line data entry
    - Differing definitions of employment in law but not without good reasons
    - Confidentiality of tax return and UI-based labor market information (LMI)*
    - Expense and technical hurdles of accessing and protecting LMI data when allowed, as well as assembling and validating decentralized data sources*

* SRF & BEP receive business's state ID number (BIN) and job definitions align with LMI data

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Taxes Context

Oregon taxes

- **Generally good climate**, ranking among the lowest *average* rate (ETR) by Council of State Taxation (COST)/Ernst & Young for local and state *taxes* on business … especially favorable for capital
- ***No* sales & use tax (one of five states) on final purchase**
  - Equipment and all else totally exempt, saving 4–9%
  - Still, great majority of states exempt purchases of "manufacturing" equipment, but not necessarily other capital assets (for example, with traded-sector service centers)
  - Saliency of effective tax savings may be muted and diluted
- **Public Finance**—in addition to lottery, interest, *fees, charges, etc.*
  - **Property taxes only locally**
  - **Corporate** excise tax—greater of
    - Minimum — \$150 – \$100,000, based on Oregon sales (≈0.1%), cannot be reduced with credits, or
    - 6.6% on state income ≤ \$1 million, 7.6% of income above that
  - State personal income tax—major revenue source, indirect *influences?*

Minimum Tax due …	If Oregon Sales are less than
\$150	\$500,000
\$500	\$1,000,000
\$1,000	\$2,000,000
\$1,500	\$3,000,000
\$2,000	\$5,000,000
\$4,000	\$7,000,000
\$7,500	\$10,000,000
\$15,000	\$25,000,000
\$30,000	\$50,000,000
\$50,000	\$75,000,000
\$75,000	\$100,000,000
\$100,000	(maximum)

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Business property taxes in Oregon

- **Everything's taxable each year based on January-1 value at site according to tax code area, except inventory and registered vehicles**
- **Local rates vary by 2–4 times with code area's array of district levies, but except for school or capital bond levies, M5 limitations compress total rate them to 1.0% & 0.5% of real market value (RMV)**
- **Rate applied to taxable or assessed value (AV), which can trend lower than RMV due to M50's 3% cap on annual growth and changed property ratio (CPR) for new or modified property**
- **County assessor & State agency have various responsibilities, including determination of market value depending on account**
- **Unitary assessment of "utility" property:**
  - Valuation approach based holistically on economic entity
  - Centrally assessed but different from state-appraised property

Income taxes
—corporate | pass-through

U.S. Tax Return:*
revenues – costs | PIT adj. gross income (AGI)

Interstate factors – apportionment | residency

Additions and Subtractions
(*e.g.*, Oregon Investment Advantage)

State Taxable Income (STI) × tax rate
(6.6–7.6% | 5–9.9%†)

Income-based tax liability reducible with
credits [corporate minimum tax paid if greater]

* Federal law connection with exceptions—IC–DISCs, pass-through deduction
† Reduced for certain non-passive, pass-through business income

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Single sales factor
—interstate apportionment

- **Benefits *multi-state*, traded-sector C corporations, with major physical presence in state, compared to using all three factors**
- **Factor = "Oregon sales" ÷ all domestic sales**
- **Factor × consolidated federal income = income for state taxation**
- **Oregon sales (which also determine minimum tax) include sales that are thrown back, if made from Oregon to U.S. government or to customer where firm lacks *nexus* – *i.e.*, specific corporate entity not taxable there (*Joyce*) – often hard to ascertain in the abstract**
- **Intangible sales—traded-sector services and so forth now apportioned like sales of tangible goods with Senate Bill 28 (2017), but with throw-out rather than throwback**
- **Gubernatorial agreements with Nike and Intel in 2012 & 2013**

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