Evaluation of the Job Creation Tax Credit

Draft

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Primary Staff for This Report

Robert Rehrmann
Matthew Bennett
Benjamin Blank
George Butler, Jr.
Mindy McConville
Maureen Merzlak
Heather Ruby
Theresa Tuszynski

Other Staff Who Contributed to This Report

Ryan Bishop

For further information concerning this document contact:

Library and Information Services
Office of Policy Analysis
Department of Legislative Services
90 State Circle
Annapolis, Maryland 21401

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TTY: 410-946-5401 ● 301-970-5401
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Email: libr@mlis.state.md.us
Home Page: http://mgaleg.maryland.gov

Department of Legislative Services
Office of Policy Analysis
Maryland General Assembly

Warren G. Deschenaux
Executive Director

November 17, 2016

The Honorable Richard S. Madaleno, Jr., Co-chair
The Honorable Jay Walker, Co-chair
Members of the Tax Credit Evaluation Committee

Ladies and Gentlemen:

As you know, the Tax Credit Evaluation Act of 2012 (Chapters 568 and 569) establishes a legislative process for evaluating certain tax credits. The legislative evaluation committee created by the Act is required to evaluate the job creation tax credit by July 1, 2017.

To assist the Tax Credit Evaluation Committee in its work, the Department of Legislative Services (DLS) is required to evaluate the credit on a number of factors, including (1) the purpose for which the tax credit was established; (2) whether the original intent of the tax credit is still appropriate; (3) whether the tax credit is meeting its objectives; (4) whether the goals of the tax credit could be more effectively carried out by other means; and (5) the cost of the tax credit to the State and local governments.

DLS has conducted its evaluation of the job creation tax credit and makes several findings and recommendations about the tax credit. The document is divided into 9 chapters.

Chapter 1 provides an overview of the Tax Credit Evaluation Act and the job creation tax credit.

Chapter 2 provides an overview of the intent and objectives of the tax credit.

Chapter 3 discusses the economic theory and evaluation of job creation tax credits.

Chapter 4 provides an overview of employment tax credits in Maryland and other states.

Chapter 5 compares the various employment tax credits in Maryland.

Chapter 6 discusses the State and local costs of the tax credit.

Chapter 7 discusses tax credit program activity.

Chapter 8 analyzes the economic impacts of the tax credit.

Legislative Services Building · 90 State Circle · Annapolis, Maryland 21401-1991
410-946-5510 · FAX 410-946-5529 · TDD 410-946-5401
301-970-5510 · FAX 301-970-5529 · TDD 301-970-5401
Other areas in Maryland 800-492-7122

Chapter 9 summarizes the findings of the report and discusses recommended changes to the tax credit.

The evaluation report is currently in draft form, pending additional work by the evaluation committee. The Act requires the evaluation committee to hold a public hearing on this report by December 31, 2016. By the twentieth day of the 2017 legislative session, the committee is required to submit a final report to the General Assembly that states whether or not the tax credit should be continued, with or without changes, or terminated.

We wish to acknowledge the cooperation and assistance provided by the Maryland Department of Commerce in the development of this report. DLS trusts that this report will be useful to members of the Tax Credit Evaluation Committee in its deliberations about the job creation tax credit.

Sincerely,

Warren G. Deschenaux
Executive Director

WGD/RJR/mlm

cc: Thomas V. Mike Miller, Jr., President of the Senate
Michael E. Busch, Speaker of the House of Delegates

Executive Summary

Since the mid-1990s, the number of State business tax credits has grown exponentially, as have related concerns about the actual benefits and costs of many of these credits. Although tax credits comprise a small percentage of total income tax revenues, the number and amount of credits claimed have significantly increased over time.

In response to concerns about the fiscal impact of tax credits on State finances, Chapters 568 and 569 of 2012, the Tax Credit Evaluation Act, established a legislative process for evaluating certain tax credits. The evaluation process is conducted by a legislative evaluation committee that is appointed jointly by the President of the Senate and the Speaker of the House of Delegates. The Act requires that the job creation tax credit be evaluated by the committee by July 1, 2017. To assist the committee in its work, the Department of Legislative Services (DLS) is required to evaluate the credit on a number of factors, including (1) the purpose for which the tax credit was established; (2) whether the original intent of the tax credit is still appropriate; (3) whether the tax credit is meeting its objectives; (4) whether the goals of the tax credit could be more effectively carried out by other means; and (5) the cost of the tax credit to the State and local governments.

Created by Chapter 84 of 1996, the job creation tax credit provides a tax credit to businesses that expand or establish a facility in Maryland that results in the creation of new jobs. During fiscal 2002 through 2016, the Department of Commerce (Commerce) issued 208 certifications to 101 businesses that reported creating 17,692 jobs. Tax credits totaled an estimated $21.8 million (in current 2016 dollars).

A majority of the research reviewed by DLS concludes that a well-designed employment tax credit can be at a minimum a modestly effective policy option. A common theme of this research, however, is that the efficacy of the credit is critically dependent on the program's design and implementation.

This report provides an overview of the job creation tax credit, including how the credit is claimed, the amount of credits claimed, the impacts of the credit on the State economy using a REMI analysis, and the geographic concentration of projects receiving the credit. An overview of employment credits in Maryland and surrounding states is also provided.

DLS makes several findings and recommendations related to the job creation tax credit as follows:

The Job Creation Tax Credit Provides a Modest Incentive to Large Businesses and Overlaps with Other State Employment Tax Credits

The job creation tax credit incentive is minor relative to the total cost of employing an individual. DLS estimates the credit comprises less than 0.4% of an employer's total costs after considering additional compensation costs and additional years of unsubsidized employment so the credit is unlikely to increase employment unless a business believes there is sufficient demand for their product. Additionally, minimum job creation and other program eligibility requirements limit the ability of new or smaller businesses to receive the credit, so participating businesses are much more likely to be large established companies. State employment growth, however, is the result of a number of factors and represents a diverse spectrum of companies. Most job creation tax credits have been claimed by businesses in the manufacturing, transportation and warehousing, and finance and insurance industries, so businesses in many industries have not benefited from the tax credit.

Furthermore, there is significant overlap between the job creation tax credit and other State employment tax credits including the enterprise zone, One Maryland, and businesses that create new jobs programs. While there are many similarities between the employment tax credit programs, the job creation tax credit is not as generous as other employment tax credits. The enterprise zone and One Maryland credits provide significantly greater incentives and total funding to promote economic growth within distressed areas of the State.

Recommendation: DLS recommends that the General Assembly consider eliminating the job creation tax credit or consolidating the credit with other employment tax credits. If considering the consolidation of the employment tax credits, DLS recommends that the General Assembly consider one program to increase economic growth within distressed areas and one program to promote broad-based job creation across the State, including provisions that target job creation for small and newly established businesses and businesses in high-growth industries.

While Credit Activity Has Occurred in Every Region of the State, No Credits Have Been Certified in a Quarter of All Counties

No businesses located within Calvert, Dorchester, Kent, Queen Anne's, St. Mary's, and Talbot counties have been certified for any credits through fiscal 2016. One factor explaining the lack of activity in some parts of the State is that it may be more difficult for businesses in rural areas to create the minimum number of required jobs.

Recommendation: DLS recommends that the General Assembly consider lowering the minimum threshold for the number of jobs created by businesses in rural counties. DLS also recommends that Commerce comment on any impacts such a change could have on the overall fiscal cost of the credit.

The Number of Businesses Claiming the Credit Has Declined Over Time

The job creation tax credit has a limited impact on overall job creation in the State. Moreover, its impact has decreased significantly over the last 15 years. Due to the Great Recession and long-term trends that predated the recession, the total number of jobs created in the State has slowed in the last several years. However, the number of job creations reported by businesses claiming the credit has decreased by a significantly greater amount. In fiscal 2002 through 2006, a business claimed a job creation tax credit for 1 out of every 189 jobs created in the State – this has subsequently decreased within the last five years to 1 out of every 380 job creations.

Recommendation: Commerce should comment on the reasons for the decrease in credit activity, including its efforts to conduct outreach and inform businesses about the credit.

Commerce Does Not Certify the Value of the Job Creation Tax Credit

Commerce is required by statute to certify that a business meets program requirements. While a business is required to provide Commerce with any information needed to verify that the business is eligible, Commerce is not required to certify the actual value of the credit. Consequently, Commerce certifies the number of qualified positions but not the value of the credit.

Recommendation: DLS recommends that the General Assembly require that Commerce certify the credit amount for each eligible business.

No Businesses That Qualified for the Credit Created at Least 30 New Jobs with Highly Paid Average Salaries

If not located within a priority funding area (PFA), an eligible business must create 60 new jobs within a two-year period to claim the tax credit. The minimum number of required jobs is lowered to 30 if the average salaries of the new jobs are highly paid as determined by a sliding scale relative to the average State salary. In fiscal 2002 through 2016, it does not appear that any business qualified for the credit by creating 30 highly paid jobs.

Recommendation: Since the credit does not appear to provide a strong incentive to hire highly paid workers, DLS recommends that the General Assembly eliminate the eligibility standard that a business can qualify for the credit by creating 30 new jobs if the average salaries of the new jobs are highly paid.

The Legislative Intent of the Credit Contained in Statute Differs from the Intent Stated in Regulation

The legislative intent of the credit as stated in statute is to increase the number of new jobs in the State by encouraging (1) the expansion of existing private-sector enterprises and (2) the establishment or attraction of new private-sector enterprises. Commerce has, through regulation, expanded the objectives of the tax credit to increase the number and quality of new jobs in the State by encouraging (1) significant expansions of existing private-sector enterprises; (2) establishment of new private-sector enterprises; (3) creation of family supporting jobs; and (4) revitalization of neighborhoods and commercial areas. Commerce indicated that it does not view the credit as a community revitalization program.

Recommendation: Since Commerce does not view the credit as a community revitalization program, DLS recommends that Commerce amends its regulations to remove the objective of revitalizing neighborhoods and commercial areas.

The Definition of a State Priority Funding Area for the Job Creation Tax Credit Is Different Than Under the Smart Growth Program

Under the Smart Growth program, the definition of a State PFA is generally the same for the job creation tax credit except that a county may designate any area as a

PFA and is not limited to one area only. According to Commerce, conforming the definition to the one used for the Smart Growth Program would reduce confusion and could increase program participation in rural areas.

Recommendation: DLS recommends that Commerce comment on how conforming the definition of a PFA would impact each county, particularly rural counties, and any impacts this change could have on the overall fiscal cost of the credit.

The Job Creation Tax Credit Must Be Claimed Over Two Tax Years

The calculation of the job creation tax credit and administration of the credit are relatively straightforward. However, unlike other credits a business claiming the credit must claim the credit over two tax years.

Recommendation: Commerce should comment on whether the advantages from eliminating the two-year requirement, including increased benefits to businesses and enhanced tax administration, are outweighed by tax compliance issues or other considerations.

The State Minimum Wage Should Be Used as a Criterion for Determining a Qualified Position

In order to qualify for the tax credit a qualifying position must meet several requirements, including the requirement that the position pay at least 150% of the federal minimum wage. State law currently requires that employers pay a minimum wage of $8.75 per hour (scheduled to increase to $10.10 on July 1, 2018) whereas federal law requires a minimum wage of $7.25 per hour.

Recommendation: DLS recommends that the General Assembly specify that a qualified position pay at least 150% of the greater of the federal or State minimum wage. DLS also recommends that other employment tax credits with this requirement be altered in the same fashion.

Commerce Should Provide Additional Information about the Job Creation Tax Credit

Commerce currently reports specified information about the job creation tax credit, including the companies claiming the credit and the number of certified jobs created, on an annual basis. In the final tax credit application Commerce collects additional information, including whether the company is a minority business enterprise or women-owned firm.

Recommendation: In order to better assess the credit's effectiveness in promoting job creation in different types of businesses, DLS recommends that Commerce collect and report the following information for each applicant: (1) whether the credit resulted from a business expansion, new business, or relocation; (2) whether the business had a presence in Maryland before claiming the credit; (3) the total employment of the establishment; and (4) the total number of years the company has been in business.

Recommendation: In addition, considering the General Assembly's interest in providing business opportunities for small, minority-, and women-owned businesses, DLS recommends that the General Assembly require Commerce to report on the

number of businesses that qualify as small, minority-, and women-owned businesses.

The Comptroller's Office Can Only Provide Partial Information on the Total Amount of Credits Claimed

The Comptroller's Office provided DLS with data on the total number of returns claiming the credit and the total credits claimed. However, the Comptroller's Office advises that the data reflects only credits claimed by a business in the first two tax years and does not include any amounts that may be carried forward to future tax years. In addition, the Comptroller's Office advises that current law does not currently provide for the treatment or priority of carry forwards if a business carries forward more than one tax credit from a previous year.

Recommendation: DLS recommends that the General Assembly specify the tax treatment or priority of carry forwards if the business is claiming multiple tax credits. In addition, the Comptroller's Office should adopt procedures to track tax credit carry forwards for all tax credits in order to more accurately report the amount of credits claimed in each year.

The Maryland Insurance Administration Did Not Provide Any Information on Insurance Premium Tax Credits Claimed in Recent Years

The Maryland Insurance Administration was unable to provide recent data on the amount of credits claimed or the number of businesses that claim the credit against the insurance premium tax.

Recommendation: DLS recommends that the General Assembly require the Maryland Insurance Administration to report annually for each credit that can be claimed against the insurance premium tax, the total amount of the credit claimed, and the number of businesses claiming the credit.

Requiring a Business to Have a Certified Public Accountant Verify the Credit Can Be Costly, Particularly for Small Businesses

An independent certified public accountant (CPA) selected by the business must provide Commerce and the appropriate taxing authority with a written statement certifying that the credit amount claimed by the business is correct. Thus, the business covers the cost of compliance instead of the State. According to Commerce, a CPA audit can be costly for businesses and can cost between $10,000 and $30,000 for more complicated audits.

Recommendation: DLS recommends that the General Assembly consider options to simplify the credit verification process.

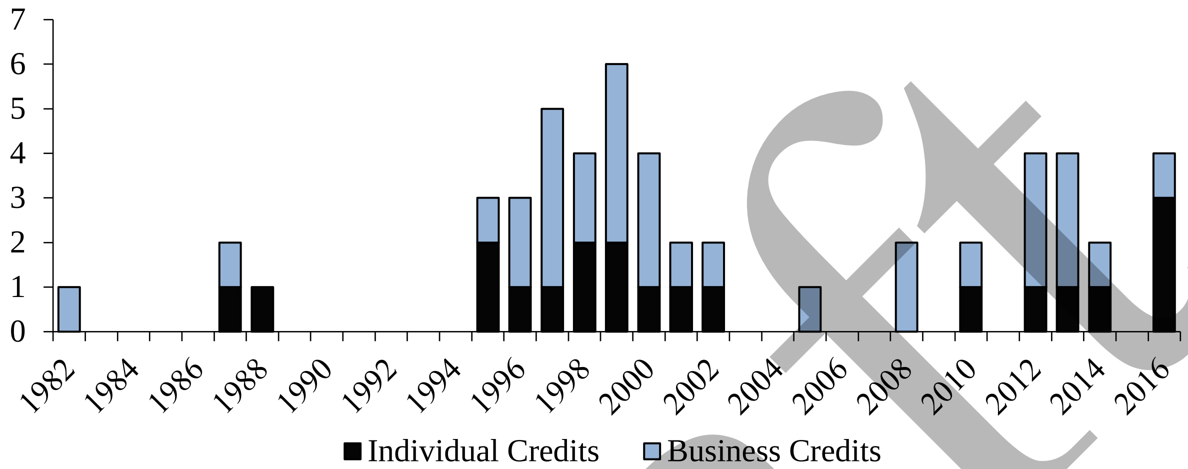
Chapter 1. Overview and Background of the Job Creation Tax Credit

Overview

Since the mid-1990s, the number of State business tax credits has grown significantly, as have related concerns about the actual benefits and costs of many of these credits. Although the reduction in State revenues from tax credits is generally incorporated in the State budget, most tax credits are not subject to an annual appropriation as required for other State programs. However, several of the larger credits that have been more recently established are subject to a budget appropriation, including the heritage structure rehabilitation tax credit and State reimbursement for one-half of the local property tax credit costs under the enterprise zone tax credit program. Reporting information for State tax credits varies. Under certain tax credit programs, agencies are required to publish specified information about the credit on an annual basis. The Department of Budget and Management (DBM) is required to prepare, every other year, a statement of the estimated amount by which exemptions from all types of State taxation reduces revenues.

Although tax credits comprise a small percentage of total income tax revenues, **Exhibit 1.1** shows that the number and amount of credits claimed has increased over time. Prior to 1995, there was one credit for individuals (earned income credit) and two primarily business tax credits (enterprise zone and Maryland-mined coal credits). Since 1995, 30 tax credits primarily for businesses and 18 tax credits primarily for individuals have been established. This includes temporary and expired tax credits. Twenty-nine of the credits were established between 1995 and 2002. More recently, 14 credits have been established since 2012, including 8 primarily for businesses. The total amount of credits has increased from a little less than $50 million in tax year 1994 to about $250 million in tax year 2008. Most of this increase has been due to an increase in tax credits for individuals, and in particular earned income credits, which have increased almost five-fold since 1994.

Exhibit 1.1
Number of Tax Credits Created Each Year
1982-2016



Source: Department of Legislative Services

Tax Credit Evaluation Act

Overview

In response to concerns about the impacts of certain tax credits, Chapters 568 and 569 of 2012 established the Tax Credit Evaluation Act, a legislative process for evaluating certain tax credits. The evaluation process is conducted by a legislative evaluation committee and must be done in consultation with the Comptroller's Office, DBM, the Department of Legislative Services (DLS), and the agency that administers each tax credit. The committee is appointed jointly by the President of the Senate and the Speaker of the House of Delegates and must include at least one member of the Senate Budget and Taxation Committee and one member of the House Ways and Means Committee.

Prior to July 1, 2016, the committee reviewed the following credits: enterprise zone, One Maryland, earned income, film production activity, and sustainable communities. Chapter 582 of 2016 altered the Tax Credit Evaluation Act so that the following credits are required to be reviewed by the date indicated:

- July 1, 2017: businesses that create new jobs and job creation;
- July 1, 2018: research and development and biotechnology investment incentive; and

- July 1, 2019: Regional Institution Strategic Enterprise Zones and cybersecurity investment incentive.

Chapter 582 made additional changes to the tax credit evaluation process. It required the agency that administers a tax credit subject to evaluation to provide information to and otherwise cooperate with DLS and the evaluation committee. The Act also altered the date by which DLS must publish an evaluation of the credit from October 31 to November 15 and the date by which the evaluation committee must hold a public hearing on the evaluation report from December 14 to December 31. Additionally, the Act eliminated the requirement that, in lieu of a specified evaluation date, a credit must be evaluated in the year preceding the termination date of the credit. Lastly, Chapter 582 increased the time period from five to seven years that a tax credit designated for evaluation under the Tax Credit Evaluation Act is subject to reevaluation.

Job Creation Tax Credit Program

Created by Chapter 84 of 1996, the job creation tax credit provides a tax credit to businesses that expand or establish a facility in Maryland that results in the creation of new jobs. The credit can be applied against the corporate or personal income tax, insurance premium tax, or public service company franchise tax. In any taxable year, however, the credit may only be applied against one tax. The credit can be recaptured during any of the three taxable years following the claiming of the credit if the business does not maintain a certain number of minimum jobs. The program is administered by the Department of Commerce (Commerce).

Job Creation Requirement

Businesses must be primarily engaged in a qualifying business activity. An eligible business must create 60 new jobs within a two-year period. The new jobs must be full-time, permanent, filled, located in Maryland, and pay at least 150% of the federal minimum wage. The job creation threshold is lowered to (1) 30 new jobs if the average salaries of the new jobs are highly paid as determined by a sliding scale relative to the average State salary or (2) 25 new jobs if the new jobs are created within a State priority funding area (PFA). A PFA includes (1) state enterprise zones; (2) federal empowerment zones; (3) Department of Housing and Community Development (DHCD) sustainable communities; (4) incorporated municipalities; (5) the area between the I-495 beltway and the District of Columbia or the I-695 beltway and Baltimore City; and (6) a growth area designated by each county for the purpose of this credit.

The jobs requirement is calculated on a rolling basis, so a business is eligible for the credit if it meets the job threshold in *any* two-year period. Thus, if a business creates 20 jobs in the first year, 40 jobs in the second year, and 20 jobs in the third year, the business meets the 60 job threshold in a two-year period by qualifying in the second and third years. Commerce issues a certification to the business for each instance in which the business meets the minimum job creation threshold. A business typically receives a certification for each year in which the requirement is met. About one-third of all businesses received multiple certifications.

Credit Value

The value of the credit depends on the number of jobs created, the wages of those jobs in the year the credit was claimed, and whether the jobs are located in a revitalization area.

- Standard Credit: The credit is equal to the lesser of $1,000 or 2.5% of the wages paid for the jobs in the year the credit was claimed.

- Enhanced Credit: If the jobs are created within a revitalization area, the credit is equal to the lesser of $1,500 or 5% of the wages.

A revitalization area includes: (1) state enterprise zones; (2) federal empowerment zones; and (3) sustainable communities as designated by DHCD.

A business is certified in the credit year in which it meets program requirements. The credit is earned at the end of the 12-month period during which the minimum number of qualified positions have been filled. The credit is ratable over two tax years – one-half can be claimed beginning with the credit year in which Commerce certified the business for meeting the program requirements with the remaining one-half claimed in the following tax year. Any unused portion of the credit can be carried forward for up to five tax years. The total credit claimed by a business cannot exceed $1 million in the credit year.

Application and Verification Process

A business must notify Commerce of its intent to seek certification before hiring the qualified employees and submit a preliminary application and employment affidavit. The preliminary application requires projected job and wage data. The employment affidavit establishes the number of jobs at the facility prior to creating new jobs for the credit. A final application is submitted to Commerce after the minimum number of jobs have been created and the jobs have been filled for at least 12 months. Commerce currently requires that a business submit verification of this information from an independent certified public accountant. The credit is claimed using Maryland Tax Form 500CR and a copy of the final certificate of eligibility is attached to the form.

Legislative Changes

No substantive changes have been made to the program since its original enactment in 1996. The General Assembly extended the termination date of the credit in 2008 and again in 2012, and the credit currently terminates on January 1, 2020.

Chapter 2. Intent and Objectives of the Job Creation Tax Credit

Intent of the Job Creation Tax Credit

The job creation tax credit can be claimed by a business that expands or establishes a facility in Maryland that results in the creation of new jobs. Section 6-302 of the Economic Development Article states that:

> The General Assembly intends that the purpose of the job creation tax credit authorized under this subtitle is to increase the number of new jobs in the State by encouraging the:
>
> (1) expansion of existing private sector enterprises; and
>
> (2) establishment or attraction of new private sector enterprises.

The credit encourages the creation of jobs in certain fields or industries as eligibility is limited to businesses engaged in one of the business activities enumerated in § 6-303(b)(2) of the Economic Development Article, as seen in **Exhibit 2.1** below.

Exhibit 2.1
Job Creation Tax Credit
Eligible Business Categories

- Manufacturing or mining
- Agriculture, forestry, or fishing
- Biotechnology
- Central services for a business entity engaged in financial services, real estate services, or insurance services
- The operation of a company headquarters other than the headquarters of a professional sports organization
- Warehousing
- Transportation or communications
- Research, development, or testing
- Computer programming, information technology, or other computer-related services
- The operation of central administrative offices
- The operation of a public utility
- Business services, if the business facility established or expanded is located in a State priority funding area
- Entertainment, recreation, cultural, or tourism-related activities in a multi-use facility located within a revitalization area if the facility (1) generates a minimum of 1,000 new full-time equivalent positions in a 24-month period and (2) is not primarily used by a professional sports franchise or for gaming

The legislation enacting the job creation tax credit (Chapter 84 of 1996) stated that the General Assembly concluded that the widespread adoption of tax subsidies intended to move jobs from one state to another reduces the revenues in all participating states without increasing the total number and quality of jobs. Chapter 84 also instructed the Governor to work with the chief executive officers of Delaware, the District of Columbia, North Carolina, Pennsylvania, Virginia, and West Virginia to negotiate an agreement among all of these states by July 1, 1998, for the repeal of any law in each state that provides a tax subsidy, including any tax credit, deduction, exemption, or other modification, that is intended to create new jobs or entice new jobs to the state. There is no record of an agreement between Maryland, the District of Columbia, and the other states.

Regulations Specify Additional Objectives

The Department of Commerce (Commerce) adopted regulations (COMAR 24.05.20.01) to expand the objective of the tax credit program. Specifically, the regulations state that the objective of the program is to increase the number and quality of new jobs in the State by encouraging:

- significant expansions of existing private-sector enterprises;
- establishment of new private-sector enterprises;
- creation of family-supporting jobs; and
- revitalization of neighborhoods and commercial areas.

The Department of Legislative Services (DLS) contacted Commerce as to the reason why the objective stated in the regulation is expanded from statute, but Commerce could not offer guidance. DLS notes that certain components of the tax credit are consistent with the objectives stated in the regulations. For example, a qualifying job must pay at least 150% of the federal minimum wage and the threshold for minimum job creation outside priority funding areas is lowered to 30 jobs if the jobs pay a specified minimum salary. In addition, the percentage and maximum values of the credit are increased if the business facility is located within a revitalization area. It should be noted that DLS has evaluated the tax credit program based on the objective stated in statute.

Rationale for Government Intervention

The United States is a modern market economy as most goods and services are produced by the private market. Markets provide optimal benefits to society when economic activity and resources are efficiently allocated. This allocation depends on several conditions, including free competition and a clear assignment of prices and benefits. Although most goods and services in the United States are supplied by the private market, governments intervene in many markets by either supplying the good or service or causing different outcomes than that produced by the private market alone.

Market failures occur when the private market does not produce the most efficient outcome for society. For example, the private market may not incorporate all of the activity's costs and benefits to society. If the activity has additional benefits to society, such as health care or education, markets may under-produce the good compared to the socially optimal quantity. A recent U.S. Federal Reserve analysis noted that in the midst of the recent financial crisis and resulting recession, few people are left unconvinced of the possibility of market failures.

Governments can intervene in a variety of ways – through regulation, taxation, and/or subsidies. Subsidies are a form of government assistance provided by government to a subset of the public that lowers the cost of producing a good or the price that a consumer pays for a good. While tax credits are a form of subsidies provided through the tax code, subsidies can also be delivered via regulation and direct provision. Most analysts believe that although markets can fail, there should be an expectation that government intervention can improve outcomes before any action is taken. Poorly designed policies can result in society being worse off. For example, most economists believe that although there were market failures within the U.S. housing industry, poorly designed policies (including subsidies) contributed to the housing market implosion. Policy analysts typically identify two rationales for how subsidies can improve free-market outcomes:

- efficiency: subsidies can correct the failure of the market to produce the efficient amount of goods and services, thereby improving societal benefits; and

- outcomes: markets can operate efficiently but produce outcomes that are deemed inequitable – for example, private market activities can result in unacceptable levels of poverty and joblessness.

Outcome or Efficiency Goals of State Tax Credits

DLS reviewed the intent of numerous current and recently expired State business tax credits. For the vast majority of these credits, DLS could identify a valid efficiency or outcome goal specified in the legislation creating the tax credit that is supported by economic theory or that could be found in a similar federal program. For example, the research and development tax credit provides tax credits for a firm's qualified research expenses. Economists believe that firms may not produce the optimal amount of research as the benefits to society, through spillover effects, are greater than the private gain to the firm. In the absence of credits, firms will produce less than the efficient amount of research. The goal of four business tax credits – enterprise zone, community investment, employment opportunity, and One Maryland – is to change market outcomes, specifically those that the market produces in certain areas. In some cases, tax credits have both goals. Although the goals of these tax credits may be valid, DLS has questioned whether these programs efficiently achieve their goals, most recently in the evaluations of the enterprise zone, One Maryland, and film production activity tax credits.

Job Creation Tax Credit

The objective of the job creation tax credit is clearly defined in statute. The job creation tax credit is intended to address several outcome and efficiency market failures. The labor market is dynamic and involves a significant number of job creations and eliminations – this reallocation of jobs that are beneficial to the economy as a whole may be costly, even devastating, to the affected individuals. People who lose their jobs, even if only temporarily, can often suffer long-term negative outcomes. Unemployment and joblessness may then lead to social ills and long-term negative impacts to communities. To the extent the job creation tax credit increases employment, society could be better off as a result of the increased employment.

Chapter 3. Economic Theory and Evaluation of Job Creation Tax Credits

Economic Impacts of Job Creation Tax Credits

Tax credits reduce individual or business tax liabilities or provide refunds (money) in order to meet a stated policy objective or societal improvement. These credits lower the after-tax cost of the targeted activity, thereby creating an incentive for individuals or the marketplace to increase its output. However, poorly designed policies may not lead to any improvement in social welfare. A major impediment to effective tax credit design is their propensity to provide money to individuals who would have acted in the desired way in the absence of the credit. If this is the case, only a fraction of the subsidy actually increases the targeted activity.

Policies can promote employment by providing an employer subsidy that increases labor demand (*i.e.*, an employment tax credit) or an employee subsidy that increases labor supply (*i.e.*, child care and earned income tax credits). An employment tax credit such as the job creation tax credit subsidizes part of the cost for employers to hire workers. In theory, this decrease in cost to the employer will increase total employment as employers hire more workers than they would have without the credit. Additionally, an effective credit increases overall growth and is not merely accelerating when the growth occurs or shifting activity from a nearby location. An employment credit that creates sustained job growth is more effective than one whose effects disappear upon expiration of the incentive.

Unless businesses believe there will be sufficient demand for their products, however, they are unlikely to increase hiring despite the credit's availability. Faced with only a temporary subsidy of their labor compared to capital costs, firms may be unwilling to change production techniques and shift their input mix toward greater use of relatively less expensive workers. In addition to hiring additional employees, the U.S. Congressional Budget Office (CBO) outlined three additional responses by businesses. Businesses may also:

- reduce prices in order to sell more goods and services. Higher sales would in turn increase production, which could lead to increases in hours worked and hiring;
- pass the tax savings on to employees by increasing wages or compensation, which would in turn encourage more spending by those employees; or
- retain the tax savings as profits, which are passed on to the firm's shareholders or owners. Higher profits can increase household wealth and improve cash flow for businesses, enabling some firms to buy new equipment.

These additional responses can increase employment; however, the impact is indirect and less effective in promoting employment than a direct increase in employment.

Challenges of Evaluating Job Creation Tax Credits

The challenges to accurately measuring the impacts of a job creation tax credit include isolating its effects from other changes in the economy and determining what economic activity would have occurred in the absence of the credit. Comparing a business that claims a job creation tax credit to a control group can estimate how many additional jobs were created by the program relative to what would have happened in the absence of the program. Macroeconomic data can be analyzed to determine if employment has increased; however, it is difficult to assess whether job growth is attributable specifically to the program or to other policies. A business that qualifies for the job creation tax credit may also qualify for other tax credits, such as the enterprise zone and One Maryland tax credits. More detailed information on this overlap among credits and how it impacts the effectiveness of each program is discussed in Chapter 5.

Arguments For and Against Job Creation Tax Credits

Proponents conclude that well-designed job creation tax credit programs are cost-effective policies that can encourage significant job creation. Additionally, state programs may help attract businesses from other states or to retain existing businesses.

Opponents conclude that the vast majority of job creation tax credits are given to businesses that would have hired employees in the absence of the credit and are therefore not an effective policy. Opponents also conclude that job creation tax credits in theory may be a good idea but too often are overly complex and have low utilization rates. Finally, targeted population employment tax credits have additional shortcomings that further limit their effectiveness.

Despite the lack of agreement, a majority of the research reviewed by the Department of Legislative Services concludes that a well-designed employment tax credit can be at a minimum a modestly effective policy option. A common theme of this research, however, is that the efficacy of the credit is critically dependent on the program's design and implementation.

Credit Design and Implementation

A well-designed credit is one that is available to a wide spectrum of businesses that are aware of the credit before hiring decisions are made, is not complex or administratively burdensome, and provides a sufficient incentive that spurs additional hiring and generates the maximum benefit relative to its fiscal cost. Each of these key elements are described below:

- **Credit complexity/administrative burdens:** A more complex or administratively burdensome credit increases the cost of obtaining the credit. Greater complexity, especially if there are multiple components, reduces business awareness of the credit and dampens the incentive to increase employment.

- **Awareness of the credit:** A credit is more effective if businesses are aware of the program's incentives before hiring decisions are made, as this increased awareness influences more employment decisions throughout the economy. CBO notes that a shortcoming of the federal New Jobs Tax Credit of the 1970s was that many employers were unaware of the credit until they filed their tax returns, at which point the credit could no longer impact hiring decisions. CBO also states that although an outreach campaign requires additional resources it probably increases program effectiveness.

- **Restricting eligibility to certain businesses:** Restricting a credit to certain firms or industries typically requires more complex rules. In addition to the negative impact of requiring more complex rules, restricting eligibility to certain firms can reduce a credit's effectiveness if the employment characteristics of target firms differ from the average employer. For example, restricting a credit to small businesses or startups typically reduces effectiveness since employment at smaller businesses is often volatile. As a result, the average duration of employment subsidized by a tax credit is shorter than the average duration of jobs subsidized under a broad-based policy. Targeting a tax credit to certain firms or industries can also decrease effectiveness if the firms have lower rates of employment and by causing a misallocation of resources as some industries and firms are favored over others.

- **Limiting the maximum value of the credit:** Limiting the maximum value of a credit reduces budgetary costs but limits the incentive to increase employment for firms that reach the maximum limit. A policy that has a low credit percentage and high maximum value is more effective than a high credit percentage and low maximum value.

- **Incentive value:** A credit must provide a sufficient incentive for businesses to increase employment. A credit that provides an insufficient incentive does not increase overall employment and will be claimed by companies who would have hired the employees in the absence of the credit. The credit will have little effect on wages and employment and will instead be passed on to the shareholders and business owners. On the other hand, a credit that is overly generous will lead to some employment increase but the excess value of the credit will not spur additional employment and will instead be retained by shareholders and business owners. The value of the incentive that generates the greatest benefits relative to its cost is a critical element yet often difficult to determine.

- **Targeted populations and geographies:** Broad-based credits are more effective than targeted (people or place-based) incentives as targeted incentives can lead to low utilization rates and place-based incentives may not increase overall employment but lead to a reallocation from other areas.

Federal Employment Tax Credit Studies

CBO Analysis

In the aftermath of the Great Recession, CBO reviewed a number of federal fiscal policy options that could promote economic growth and employment. These tax and spending policies included boosting household disposable income, providing support to businesses, and increasing aid to local governments and government spending on infrastructure. CBO concluded that lowering the cost of payroll taxes for businesses that increase employment was among the most effective policy options for increasing employment and output in the short term. In contrast, policies that primarily affected business income, such as reducing business income taxes or reducing tax rates on repatriated foreign earnings, had very little impact on output and employment.

CBO analyzed the impact of providing a one-year nonrefundable credit against payroll taxes for businesses that increased payrolls compared to the previous year. Specifically, CBO modeled the impact of providing a nonrefundable credit equal to 5% or 10% of the increased payroll. Compared to a tax reduction for all firms, CBO estimated that limiting the reduction to companies that increased their payroll would produce substantially larger employment impacts as it links tax benefits to payroll growth. In particular, fewer budget dollars would be used to reduce employer taxes for workers who would have been employed anyway. CBO estimated that gross domestic product (GDP) would increase by between $0.40 and $1.30 for each dollar of budgetary cost and that the cost of increasing full-time employment for one year was between $77,000 and $333,000. This estimated employment impact was between five and eight times greater than a general business income reduction and its impact on GDP was about four times greater.

It should be noted that the impacts of a state job creation tax credit and the proposal analyzed by the CBO could differ for several reasons. First, the proposed federal credit would have been economy wide and large in scope. Second, the proposal was a temporary employment credit designed to spur employment in the short term, whereas state job tax credits are typically designed to be permanent. Lastly, the federal proposal would have been enacted during a time of significant underemployment and other uncommon economic conditions.

Other Research Supporting a Broad-based Federal Employment Tax Credit

Neumark (2011) compared the employment impacts of the federal earned income tax credit (EITC) to a job creation tax credit. The study found that employment tax credits that target disadvantaged workers are generally ineffective as these targeted hiring credits stigmatize beneficiaries, there is low participation by businesses, and workers hired under the program displace employment by other individuals rather than increasing overall employment. Direct subsidies provided to workers, such as the EITC, are more effective in promoting employment and increasing incomes for low-income families. However, during or after a severe recession, Neumark concluded that a broad-based, well-designed employment credit may be effective at promoting job creation. Due to budgetary constraints during or after a severe recession, it may not be possible to enact a job creation tax credit. Neumark instead recommends a countercyclical employment tax credit that provides incentives to hire unemployed individuals and is funded in better economic times. An advantage of this credit compared to other automatic stabilizers such as the Supplemental Nutritional Assistance Program and Unemployment Insurance is the direct incentive to increase hiring whereas the other programs stimulate job creation indirectly.

Bartik and Bishop (2009) concluded that a well-designed, temporary federal job creation tax credit should be an integral part of the federal government's efforts to promote employment in the midst of the Great Recession. They estimated that a program that refunded 15% of additional payroll costs in 2010 and 10% in 2011 could create 5.1 million additional jobs. Basing the credit on payroll taxes directs more of the benefit to lower- and moderate-income workers and can encourage payroll expansions and not just new hires.

Maryland Job Creation Tax Credit Studies

The Center for Regional Economic Competitiveness (CREC) prepared for the Maryland Economic Development Corporation a January 2016 report examining 12 Maryland state incentive and financing programs in 6 categories, 1 of which was job creation and workforce development programs. CREC compared Maryland's programs to other states and recommended several changes to the program. CREC found that the value of the State's job creation tax credit is consistent with neighboring states but lower than in other states, particularly states in the Southeast that also have less stringent job creation requirements in rural, distressed, or other geographically targeted areas. CREC recommended that the Department of Commerce (Commerce) explore options to simplify the final verification process that requires businesses to submit verification from an independent certified public accountant. CREC suggested that Commerce should instead verify the final application by establishing a payroll record data-sharing agreement with the Department of Labor, Licensing, and Regulation. CREC also recommended lowering the job threshold for businesses located in rural areas and to implement a tiered credit value that directs additional credits to areas with greater need.

Sohn and Knaap (2005) examined whether Maryland's job creation tax credit increased employment within State priority funding areas (PFAs). The study concluded that the program modestly increased employment growth rates within the transportation, communication, and utilities and service industries but had little effect on the agriculture and mining, manufacturing, finance, insurance, and real estate industries. Overall, the study found that geographically targeted job creation tax credits can be effective, albeit with a modest overall impact and limited to certain industries. These findings contrast with other studies that do not find impacts from other geographically targeted employment tax credits such as enterprise zone tax credits. The study did not account for the impact of several other incentive programs, including other State business tax credits, that direct program funding to PFAs. Therefore, it likely overestimated the impact of the job creation tax credit.

Chirinko and Wilson (2016) examined Maryland's job creation tax credit as part of a study that evaluated 20 state job creation tax credits enacted between 1990 and 2007. This study concluded that job creation tax credits have a positive impact on employment, but that the impact was delayed by two to three years after enactment. The researchers found that job creation tax credits create an anticipatory dip in employment during the implementation period – the period between the enactment of the credit and the date a business qualifies – as employers anticipated increasing employment in order to earn tax credits. The average cost per job of a permanent job creation tax credit was $16,000, with an estimated 80% of all credits provided to businesses that would have created the jobs in the absence of the credit.

Studies by Other State Agencies

While the majority of states offer a job creation tax credit, only a few states have evaluated their credits. In 2015, the Iowa Department of Revenue evaluated the state's new jobs tax credit and found that two-thirds of eligible businesses did not claim the credit due to a lack of knowledge about the program or because the administrative costs outweighed the benefits. The report also found that the job creation reported by employers claiming the credit was not statistically different than businesses who were eligible to do so but did not.

Rubin and Boyd (2013) analyzed New York's business tax credits on behalf of the New York State Tax Reform and Fairness Commission. The analysis recommended eliminating all business tax credits as the benefits were insufficient relative to the negative impacts that result from the distortion of economic decisions and increased tax compliance and administrative costs for both businesses and governmental agencies.

The Wisconsin Legislature's Joint Audit Committee audited the Wisconsin Economic Development Corporation (WEDC) in May 2015. The committee found that WEDC did not verify the job and wage information submitted by businesses that claimed state tax credits. In response to the audit, WEDC performed a preliminary tax verification review on 18 tax credit awards from four different programs, including the state's jobs tax credit. WEDC determined that there were a total of $448,674 in erroneous overpayments or an average of $24,926 per tax credit.

Academic Studies of Other State Programs

Bartik and Erickcek (2012) estimated the impacts of the Michigan Economic Growth Authority (MEGA) tax credit program by using the REMI economic impact model. The study modeled financing the cost of the credit in two different ways – reducing government spending or increasing state business taxes – and presented various scenarios based on variable assumptions on how influential the credit was in hiring decisions. Under the assumptions the researchers thought were representative of the Michigan economy, the MEGA credit was found to be the decisive reason in about 8% of the jobs associated with the program, leading to an annual cost per job of $13,000. The researchers concluded that the program likely had a large effect on job creation relative to its fiscal costs and the MEGA credit provides superior job creation relative to a general reduction in state business taxes.

These conclusions contrast with those of Hicks and LaFaive (2011), who found that the MEGA credit does not impact county-level aggregate employment, unemployment rates, wages, or incomes. The study concluded that the only employment impact of the MEGA credit was a temporary increase in construction employment that occurred at a cost of $123,000 per job.

Faulk (2002) examined the employment impact of the Georgia jobs tax credit. Faulk estimates that about one-quarter of the change in employment in participating firms was attributable to the tax credit while the remaining three-quarters was not due to the incentive and would have occurred in the absence of the credit. The average cost per job was estimated to be between $2,280 and $2,678. The study found that the low cost per job of the broad-based tax credit made it an effective option compared to other incentives targeted to specific companies, many of which were large corporations.

Thompson and Garrett-Peltier (2010) conclude that state employer tax credits do not significantly increase the demand for labor as balanced budget requirements and limitations on the value of the credit negate most of the potential job creation. Credits often do not provide a sufficient incentive for employers to increase their employment. The authors suggest that states should instead increase spending within labor-intensive industries and on federally funded programs.

Contrasting this pessimistic view of employer tax credits, Lawrence, Briskin, and Qu (2013) reviewed state job creation tax incentive programs and identified several successful programs. These successful programs typically had a significant employment impact, were transparent with stringent audit standards, and aimed to revitalize communities.

Chapter 4. Employment Tax Credits in Maryland and Other States

Types of Employment Tax Credits

Tax credits designed to increase or retain employment have significant variation in their key elements but most can be classified into five different categories based on the credit's design and objectives:

- **Broad-based**: Tax credits might be restricted to certain businesses, such as those that increase employment, but in general are available to a significant portion of all businesses and directed at job creation for the general population.

- **Geographically targeted**: Geographically-targeted tax credits restrict eligibility or provide an enhanced credit to certain areas that have been targeted for revitalization due to economic distress and poverty. Geographically-targeted credits can also complement other policies such as land development strategies. Enterprise zones are a common example of geographically targeted programs.

- **Targeted populations**: Targeted tax credits are also available to most businesses but are designed to increase the employment of certain populations, typically focusing on individuals that may have barriers to employment (such as the long-term unemployed, ex-felons, or individuals with disabilities) or groups such as military veterans.

- **Targeted firms/industries**: These tax credits are often complex with a significant number of requirements that only a few firms meet. On a state level, these are often enacted when certain firms announce the possibility of locating or relocating a business enterprise.

- **Counter-cyclical**: Governments enact employment tax credits in the midst of a recession or periods of significant underemployment to boost an economic recovery and decrease joblessness.

Tax credits often combine several of these elements. For example, there is no employment tax credit that is available to all employers in Maryland – each available credit has restrictions on the eligible business activities and minimum job creation or investment requirements. Of the current State business tax credits that explicitly provide an incentive to create or retain jobs, the job creation tax credit is the only credit that can be classified as a broad-based employment tax credit. Two credits – enterprise zone and One Maryland – are geographically targeted credits whose goals are mostly to increase investment and jobs within economically distressed areas. The Regional Institution Strategic Enterprise (RISE) zone credit is also geographically targeted but does target revitalization of distressed areas. The two remaining credits, the businesses that create new jobs and aerospace, electronics, or defense contract (AEDC) tax credits, were designed to provide tax incentives to specific firms.

Broad-based Job Creation Tax Credit

The job creation tax credit is designed as a broad-based tax credit that is available to a greater number of employers compared to other State employment tax credits. However, the tax credit has certain limitations that reduce the potential number of claimants. First, a business must be engaged in an eligible activity that excludes many industries. Second, a business must create a minimum number of jobs to claim the credit, which can be more difficult for smaller firms and firms located in rural areas. Although the job creation tax credit is potentially available to a larger number of businesses, only 101 businesses have claimed the credit statewide within the last fifteen years. More details on the scope and utilization of the job creation tax credit compared to other incentives offered is discussed in Chapter 5.

The credit also includes geographic aspects by providing an enhanced credit for jobs located within revitalization areas and having a lower minimum job creation threshold for businesses located within State priority funding areas (PFAs).

Geographically Targeted – Economic Distress

The enterprise zone tax credit program is intended to encourage economic growth within economically distressed areas of the State and to increase employment of the chronically unemployed. The Secretary of Commerce may only designate an area as an enterprise zone if it is in a PFA and satisfies at least one criterion related to economic distress. The most typical qualifying criterion is an elevated poverty rate of the population that resides in or near the zone.

The enterprise zone program has both a property tax credit for qualified investments in real property within the zone and an employment income tax credit. In addition, there is also an enhanced targeted population employment tax credit that provides a three year tax credit for the employment of a member of an economically disadvantaged household. In its evaluation of the program, the Department of Legislative Services (DLS) found that enterprise zone tax credits are not effective in creating employment opportunities for residents. In addition, the targeted tax credit for members of an economically disadvantaged household had significant administrative burdens that contributed to low utilization rates.

The One Maryland economic development tax credit was established to assist businesses with the costs of economic development projects undertaken in certain economically distressed counties and specifically to encourage capital investment and job creation in those counties. A business that establishes or expands a business facility in a PFA and is located in a qualified distressed county may be entitled to an income tax credit of up to $5.5 million. A business must expend at least $500,000 in eligible project costs and must also be engaged in an eligible activity. The project must create at least 25 additional jobs. In its evaluation of the program, DLS found that the One Maryland program is complex and difficult to administer. In addition, there was significant variation in the effectiveness of the tax credit in creating jobs.

Chapter 530 of 2014 established the RISE Zone Program, which is administered by the Department of Commerce (Commerce). RISE zones must be located in the immediate proximity of a private or public four-year institution or community college. A business may be eligible for a property tax credit for local real and personal property taxes imposed on qualified property and an income tax credit for the qualified employees hired by the business. Businesses located within a focus area qualify for enhanced credits. The employment tax credits, both the general employment tax credit and targeted credit for a member of an economically disadvantaged household, are identical to the enterprise zone employment tax credits.

Targeted Populations

In addition to the RISE and enterprise zone employment tax credits for members of an economically disadvantaged household, the State currently has one targeted population employment tax credit for employing individuals with disabilities. Two expired State tax credits – the employment opportunity and long-term employment of ex-felons tax credits – also provided incentives to employ certain populations. The work opportunity tax credit program, which expired in 2011, provided incentives to employ individuals who were receiving Aid to Families with Dependent Children (AFDC) or payments under the Family Investment Program. The long-term employment of ex-felons credit also expired in 2011.

Targeted Firms/Industries

Two business tax credits were established to provide tax credits and subsidies to specific firms. Both of these tax credits – the AEDC contract and businesses that create new jobs tax credits – are complex credits with numerous eligibility requirements.

The AEDC tax credit allows a credit against the State income tax for a business that is certified by Commerce as operating an AEDC tax credit project. Commerce may award a maximum of $7.5 million in tax credits in each year to a business that is certified as meeting the requirements of the program. Commerce may certify a project if the business that operates the project creates or retains at least 10,000 qualified positions and expends at least $25.0 million in qualifying expenditures during a credit year. Commerce may award a total of $37.5 million in credits in tax years 2016 through 2020. It is expected that Commerce will award at least a majority of the credits to one firm, Northrup Grumman.

The businesses that create new jobs tax credit program authorizes a county or municipal corporation to grant property tax credits against real and personal property taxes for a business located in Maryland that creates new positions and establishes or expands business facilities in the State. In order to qualify for the credit, the new or expanded premises must be located in a PFA and a business must create at least 25 new positions as part of the new or expanded business facility, which must be at least 5,000 square feet in size. Businesses located in less-populated counties (*i.e.*, those counties with a population of 30,000 or less) must create at least 10 new positions.

A business can qualify for an enhanced credit if it (1) obtains at least 250,000 square feet of new or expanded premises, continues to employ at least 2,500 individuals in existing full-time positions, and employs at least 500 individuals in new permanent full-time positions or (2) obtains 250,000 square feet of new or expanded premises and employs at least 1,250 individuals in new permanent full-time positions. In Montgomery County only, a business must spend at least $150 million to obtain at least 700,000 square feet of new or expanded business premises (through the purchase, construction, or lease of a new premises) and employ at least 1,100 individuals including at least 500 new, permanent full-time positions.

The local property tax credit is claimed over 6 years and is equal to, in each year, between 26% and 52% of the amount of property tax imposed on the assessed value of the new or expanded premises. In addition, the business also qualifies for a 6-year State income tax credit equal to between 14% and 28% of the eligible amount of property tax of the new or expanded premises. The enhanced credit is available for 24 years and is equal in each year to 58.5% (property) and 31.5% (income).

The businesses that create new jobs credit was originally enacted and later altered to provide incentives to 2 large businesses – Marriott International and Discovery Communications. The total number of qualifying businesses statewide is not known, but in Montgomery County a total of 16 businesses have received incentives**.**

In addition to these targeted tax credits, the State has established numerous tax credit programs that provide subsidies to or for a specific industry. These include the biotechnology investment incentive, research and development, wineries and vineyards, film production activity, cybersecurity investment incentive, Maryland-mined coal, and employer clearance cost tax credits.

Counter Cyclical

In the midst of the significant unemployment caused by the Great Recession, Chapter 1 of 2010 created a temporary employment tax credit designed to employ unemployed individuals who were receiving or had recently exhausted unemployment insurance (UI) benefits. The Job Creation and Recovery Tax Credit allowed a tax credit against the State income tax equal to $5,000 for each qualified individual hired between March 25, 2010, and December 31, 2010. The total value of the credit for a business was limited to $250,000. The Department of Labor, Licensing, and Regulation (DLLR) was authorized to award a total of $20 million in credits on a first-come, first-served basis. However, utilization of the credit was far less – the Comptroller reports that a total of $4.0 million has been claimed to date. According to the Office of Legislative Audits, as of May 30, 2011, DLLR certified 882 employers who hired 1,886 qualified individuals. This includes about $445,000 that DLLR granted erroneously on behalf of individuals that did not meet program requirements.

The State credit was similar to temporary federal employment credits established by the Hiring Incentives to Restore Employment Act of 2010. Employers could claim a credit against the employer payroll tax (generally equal to 6.2% of wages) of each unemployed person hired between February 3, 2010, and January 1, 2011. An additional credit of $1,000 could be claimed for each worker retained for at least 12 months**.** The U.S. Joint Committee on Taxation estimated that businesses would claim a total about $13.0 billion in credits.

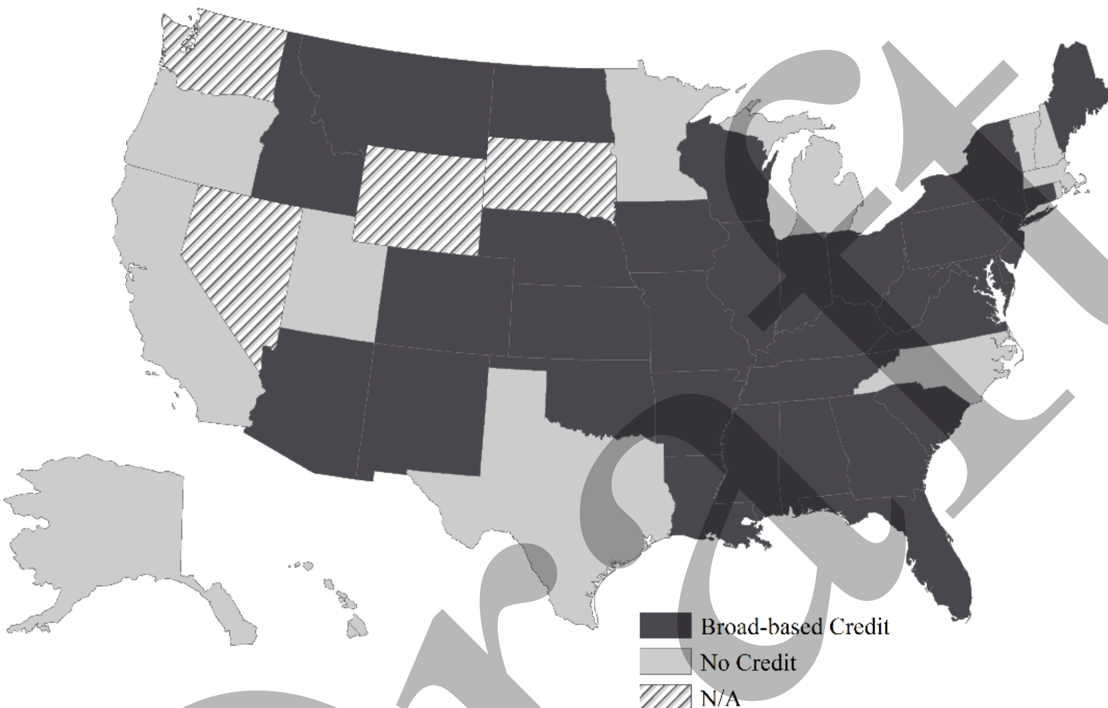
Due to their limited scope, both the job creation and job creation and recovery tax credit had very modest impacts on employment after the Great Recession. Another limiting factor is the requirement that the State must balance its budget each year, which requires that tax credit expenditures be offset by a corresponding reduction in spending or an increase in revenues. This is in contrast to the federal government's policy to stabilize the economy by increasing budget deficits.

Other state programs, although not aimed at increasing employment, had greater economic impacts due to a larger scale and a greater source of non-State funds. These programs include the Supplemental Nutrition Assistance Program (SNAP) and Unemployment Insurance (UI) benefits. The total UI benefits paid in the State increased from $383.5 million in calendar 2006 to $1.07 billion in calendar 2010. In addition to the larger scale, these funds had a greater economic impact per dollar as the majority was funded by the federal government or collected from employers in previous years during better economic conditions. The UI trust fund decreased from $1.07 billion during calendar 2007 and 2008 to $273.4 million in calendar 2011. As the economy recovered, employers were charged additional amounts and payouts decreased. Along with additional federal requirements the trust fund now is at a similar level to that of the beginning of the Great Recession ($996.2 million).

Employment Credits in Other States

The first federal employment tax credit, the New Jobs Tax Credit, was established in 1978. Nebraska established the first state job creation tax credit in 1987. Tax credits later became more common, with numerous states enacting credits during the 1990s and 2000s. As shown in **Exhibit 4.1**, 33 states have a broad-based job creation or retention credit as of July 2016. Credits are generally calculated based on either the number of jobs created or the eligible employee wages.

Exhibit 4.1
States with a Broad-based Job Creation Credit
July 2016

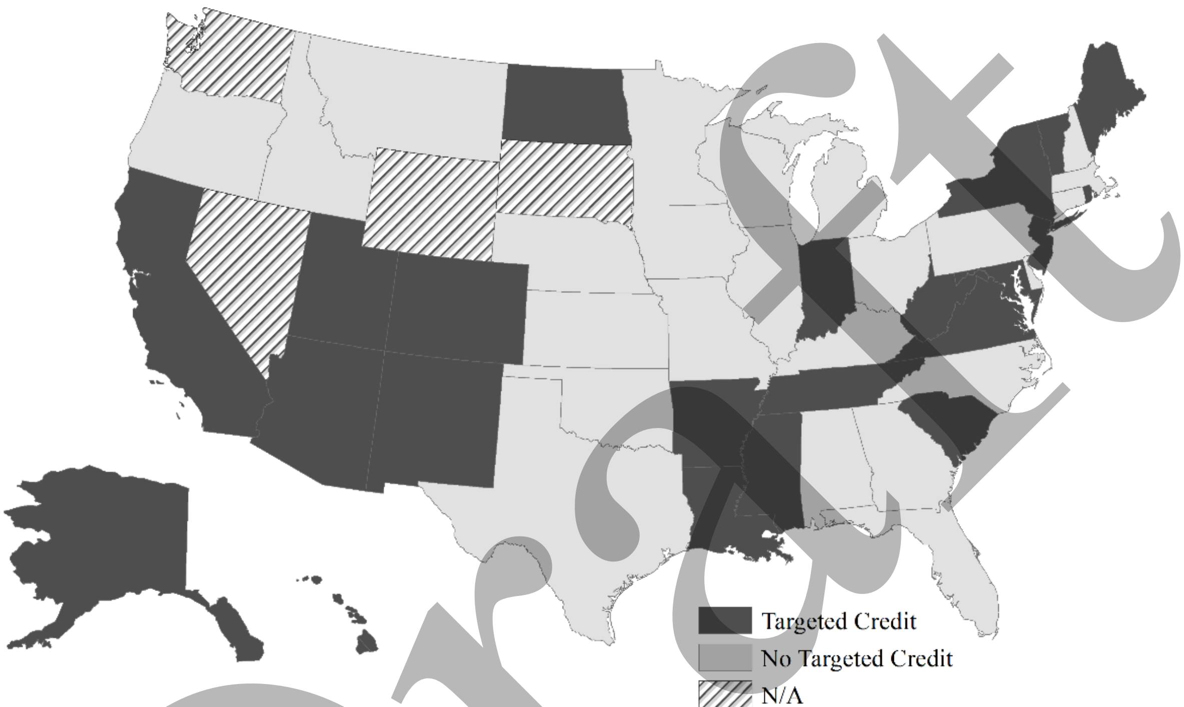


Note: N/A refers to a state that does not impose a tax on general business income.

Source: CCH Intelliconnect; Department of Legislative Services

Although broad-based employment tax credits are the most popular type of employment tax credit, 22 states have either a geographically or population targeted job creation tax credit, as shown by **Exhibit 4.2**.

Exhibit 4.2
States with a Targeted Job Creation Credit
July 2016



Note: N/A refers to a state that does not impose a tax on general business income.

Source: CCH Intelliconnect; Department of Legislative Services

Employment Credits in Nearby States

Delaware

Delaware offers incentives that encourage job creation and businesses to relocate to the state. The Delaware job creation tax credit allows an eligible business engaged in qualified activities to claim a tax credit if, during any consecutive 12-month period, the business hires at least 5 regular, full-time employees and invests a minimum of $200,000 at a qualified facility. At least one-quarter of the employees must be Delaware residents when the facility is placed in service. Eligible corporations receive a credit of $500 for each new qualified employee and an additional credit equal to $500 for every $100,000 invested, not to exceed 50% of the tax liability imposed in the year. These tax credits can be claimed annually over 10 years but may not exceed 50% of the company's pre-credit tax liability in each year.

The Business Finder's Fee Tax Credit is designed to incentivize existing Delaware businesses to help relocate out-of-state businesses to Delaware. Both the existing business and the relocating business are eligible for a tax credit equal to $500 times the number of full-time employees of the new business. Each business can claim the credit annually over three years.

In 2016, Delaware's Commitment to Innovation Act reestablished the New Economy Jobs Tax Credit that had terminated in 2014. According to the fiscal note prepared for the Act, the New Economy Jobs Tax Credit is designed to incentivize out-of-state firms to relocate to Delaware through a refundable tax credit ranging from 25% to 65% of the added employee withholdings attributable to new jobs created in Delaware. Prior to 2014, the credit was never used. The credit was reinstated as part of an effort to attract the headquarters facility that will result from the proposed Dow-DuPont merger.

District of Columbia

The District of Columbia does not provide a broad-based job creation tax credit.

North Carolina

North Carolina does not currently provide a broad-based job creation tax credit. North Carolina's tax credits for growing businesses program terminated January 1, 2014. Under the program, eligible taxpayers in certain industries could claim tax credits to offset up to 50% of the taxpayer's income, franchise or gross premium tax liability by engaging in job creation, investment in business property, and investment in real property.

Pennsylvania

The Job Creation Tax Credit allows eligible Pennsylvania businesses that, within 3 years, create at least 25 jobs or increase employment by 20% to claim a $1,000 credit for each new full-time job that meets certain minimum wage standards. The credit, which may be applied against a number of state business taxes, may be claimed only after the jobs are created. Pennsylvania allocates a minimum of 25% of all tax credits in each fiscal year to businesses that employ 100 or fewer employees. A taxpayer that does not maintain existing operations in Pennsylvania for at least five years from the start date must repay all of the credits received. A taxpayer who receives credits but fails to create the approved number of jobs within 3 years of the start date generally must also repay all credits received.

Virginia

The Major Business Facility Job Tax Credit allows qualified companies locating or expanding in Virginia to claim a $1,000 income tax credit for each new full-time job created over a threshold number of jobs (either 25 or 50 jobs depending on location) beginning in the first taxable year following the taxable year in which the major business facility commenced or expanded its operations. The threshold number of jobs must be created within a 12-month period. The credit is not available for the creation of seasonal or temporary jobs, positions in building and grounds maintenance, security, positions ancillary to the principal activities of the facility, or jobs created when a position is shifted from an existing location within the state to the new facility. The credit is available for taxable years before January 1, 2020. The credits are taken in equal installments over 2 years, and unused credits may be carried forward for up to 10 years.

West Virginia

Under the Economic Opportunity Tax Credit, qualified companies that create at least 20 new jobs within specified time limits as a result of new or expanded projects in West Virginia may be eligible for an offset of up to 80% of the corporate net income tax and personal income tax on pass-through income that is attributable to the qualified investment. If a qualified company pays its qualified employees an annual median wage higher than the statewide average nonfarm payroll wage, the qualified company may offset up to 100% of the corporate net income tax and personal income tax on pass-through income that is attributable to the qualified investment.

A qualified business creating less than 20 new jobs within specified time limits, or a qualified small business creating less than 10 new jobs, may claim a credit of $3,000 per new full-time job for five years, provided the new job pays at least a certain amount ($35,200 for tax year 2015) and offers health insurance benefits.

Chapter 5. Comparison of Employment Tax Credits in Maryland

State Employment Tax Credit Features Differ Significantly

The design and implementation of a tax credit program requires determining how a business qualifies, the size of the benefit, what eligible activities qualify, how this activity is measured, what portion of the eligible activity is subsidized, and how the benefit is provided to the business. The job creation tax credit requires a business to create a minimum number of jobs in an eligible activity and provides a one-time nonrefundable credit based on a portion of the qualified employees' wages.

Other employment tax credits share some similar features and objectives – the enterprise zone, One Maryland, and businesses that create new jobs programs require that a business must be located within a State priority funding area (PFA). While this is not a requirement for the job creation tax credit, about 90% of the credits have been awarded within PFAs. Most employment tax credits also require that a minimum number of jobs be created – the standard businesses that create new jobs credit and the One Maryland credit also have a similar minimum threshold as the job creation tax credit. However, the jobs threshold for the businesses that create new jobs credit is lowered for less populated counties. Two credits – the enhanced businesses that create new jobs and aerospace, electronics, or defense contract (AEDC) project tax credits – include requirements based on the number of retained jobs. There are no minimum requirements for the enterprise zone employment tax credit unless established by local standards. In 2014, these local enterprise zone standards required minimum job creation in about one-half of all zones, although these standards are generally less stringent than for the other programs.

Exhibit 5.1 shows for each tax credit the value and maximum limit, whether the credit is refundable, if the credit is awarded once or over multiple years, and the eligible activity the credit is based on (credit base). Unlike other programs the job creation tax credit does not provide a credit for investments or require a minimum level of investment. Credit components and eligibility requirements vary significantly across programs as there are five different credit bases and maximum credit values ranging from $250 to $10,000 per eligible job. Three of the credits are nonrefundable, one is refundable, and the One Maryland credit can be nonrefundable, partially refundable, or fully refundable. In general, credits with fewer eligibility requirements and lower minimum investment and job creation requirements are more likely to have a greater number of participating businesses. A more generous credit typically has a broader credit base, provides a higher percentage credit with low or no maximum limits, is refundable, and is awarded over several years.

Exhibit 5.1
State Employment Tax Credits
Credit Values, Limitations, and Required Investment and Jobs

Program	Credit %	Credit Base	Years Awarded	Max Credit Per Job	Maximum Credit	Refund	Investment	Jobs
Job Creation	2.5%-5.0%	Wages	1	$1,000-$1,500	$1,000,000	No	None	25-60
Businesses/New Jobs:								
Standard Credit	40%-80%	Local property tax assessed on business facility/ Personal Property[1]	6	None	None	No	5,000 ft[2]	10-25
Enhanced	90%		24	None	None	No	250,000 ft[2]	1,250 (new jobs) or retain 2,500+500 new
Montgomery County	90%		24	None	None	No	700,000ft[2] / $150,000,000	Employ 1,100 including 500 new
One Maryland	100%	Start-up & project costs	1	$10,000	$5,500,000	Certain projects[2]	$500,000	25
Enterprise Zone:							Local standards may establish minimum job creation and capital investment thresholds[3]	
Property	30%-80%	Local property tax assessed on capital improvements	10	*N/A*	None	*N/A*		
Employment	*N/A*	Per Employee	1	$1,000-$1,500	None	No		
Employment – Targeted	*N/A*	Per Employee	3	$1,000-$4,500	None	No		
AEDC project	*N/A*	Per Employee	5	$250	7,500,000[4]	Yes	$25,000,000	Retain 10,000

[1] 65% of the credit is applied against local property taxes and 35% against State business income taxes.
[2] If a project meets specified requirements the credit is partially or fully refundable.
[3] In 2014, 17 of 30 enterprise zones had minimum job creation and investment requirements.
[4] A business can earn up to three credits (maximum value $2.5 million) annually. It is estimated that one company will earn three maximum credits annually during the five years.
AEDC: aerospace, electronics, or defense contract
Source: Department of Legislative Services

Exhibit 5.2 compares the total funding, average credit value, and total number of job creation tax credit claimants to other State employment tax credits. The job creation tax credit has a greater number of claimants compared to the One Maryland, AEDC contract, and businesses that create new jobs tax credits. However, enterprise zone participation was about six times greater, despite that program's geographic limitations. The job creation tax credit's average benefit is substantially less than most credits, reflecting its lower credit percentage, narrower credit base, and one-time availability. Total job creation tax credits equal about one-tenth of the total One Maryland credits and about one-half of the combined State and local credits provided in Montgomery County for the businesses that create new jobs credit. Exhibit 5.2 generally reflects credits claimed during 2000 through 2016, except for the AEDC credit (tax year 2016 through 2020).

Exhibit 5.2

State Employment Tax Credits
Total Credits, Average Annual Claimants, and Credit Value

Program	Local	State	Total	Total Claimants	Average Credit
Job Creation	$0.0	$21.8	$21.8	117	$186,300
Business/New Jobs[1]					
Standard	$8.0	$4.3	$12.3	15	$817,600
Enhanced	17.2	9.3	26.5	1	43,098,600
Total	**$25.2**	**$13.6**	**$38.8**	**16**	**$3,460,100**
One Maryland	$0.0	$236.8	$236.8	45	$5,262,000
Enterprise Zone					
Property/Investment	$146.5	$146.5	$293.0	673	$436,000
Income/Employment	0.0	12.3	12.3	104	10.900
Total	**$146.5**	**$158.8**	**$305.3**	**776**	**$393,300**
AEDC	$0.0	$37.5	$37.5	1	$37,500,000
Total	**$171.7**	**$468.5**	**$640.2**	**955**	**$670,100**

AEDC: Aerospace, Electronics, or Defense Contract

[1] Data is for Montgomery County only.

Number of claimants is the estimated average number of unique claimants for each program. Average credit is the estimated total value of the credit including all of the years that a business can claim a multi-year credit. For the enhanced businesses that create new jobs credit, the estimated average value is projected through fiscal 2026 for the remaining eligible amounts.

Source: Comptroller's Office; Department of Commerce; State Department of Assessments and Taxation; Department of Legislative Services

Credits focused mainly on job retention provide significantly more money to a limited number of businesses. It is estimated that Discovery Communications will receive through fiscal 2026 a total of $43.1 million in enhanced businesses that create new jobs tax credits and Northrup Grumman will receive $37.5 million in AEDC project tax credits.

One Maryland and Enterprise Zone Tax Credits Provide More Valuable Incentives for Businesses in Distressed Areas

The job creation tax credit provides an enhanced credit within revitalization zones. This credit is in addition to the enterprise zone and One Maryland credits that aim to increase economic development within distressed areas of the State. The enhanced job creation tax credit within revitalization zones provided an additional $2.5 million in credits to these areas, far less than the other credits. In addition, the enterprise zone and One Maryland credits have much larger incentives for businesses to establish or expand a business within a distressed area, particularly if the business makes significant capital investments. For example, a business that hires 50 new employees and expends $2.0 million in capital improvements will receive an additional $75,000 job creation tax credit to locate within Baltimore City compared to a location that is not a revitalization zone. The same business would receive a $2.0 million One Maryland incentive and an enterprise zone incentive of $378,000.

Employment tax credits within distressed areas are not coordinated and differ depending on the tax credit claimed by the business. The job creation tax credit is generally up to 50% greater than the enterprise zone employment tax credit, thus the benefit to a business is dependent on awareness of the programs, if any, and if the business claims one or both of the credits.

Vast Majority of Maryland Businesses Do Not Benefit from Employment Tax Credits

Tax credit eligibility requirements, such as minimum job and investment requirements, limit the number of participating businesses relative to the scope of the Maryland economy. In each year, less than 10 businesses that create about 1,100 jobs are certified for the job creation tax credit. By comparison, within the last three years an average of 11,400 new establishments in the State created 92,500 jobs each year. About 40% of these jobs were created by new companies (start ups). Within these last three years, established businesses created an additional 200,000 jobs each year.

As a result, the job creation tax credit and other employment tax credits have a limited impact on total Maryland employment. Equity issues also arise as similar businesses may have different tax burdens due to credits providing significant benefits to a few companies, relative to a broad-based benefit such as a tax rate reduction. As discussed below, these issues are exacerbated as a limited number of businesses are awarded the majority of tax credits.

Businesses that Receive Employment Tax Credits Are Not Broadly Representative of Maryland's Economy

The limited number of businesses that benefit from the job creation tax credit and other employment tax credits are not generally representative of the Maryland economy. Minimum job creation and other program eligibility requirements limit the ability of new or smaller businesses to receive the credit, so participating businesses are much more likely to be large established companies. State employment growth, however, is the result of a number of factors and represents a diverse spectrum of companies. Each new business that created a job in Maryland during calendar 2014 created on average only seven jobs.

Most job creation tax credits have been claimed by businesses in the manufacturing, transportation and warehousing, and finance and insurance industries, so businesses in many industries have not benefited from the tax credit. Lastly, the job creation and other employment tax credit programs, including the enterprise zone program, have limited or no presence in certain rural areas of the State.

A business or business facility must be engaged in an eligible activity to claim the job creation, One Maryland, or enhanced businesses that create new jobs tax credits. The definition of an eligible activity is very similar, but not identical as some activities qualify in only one program. Restricting eligibility to certain industries can accomplish several goals. First, excluding industries that are mostly dependent on local demand – retail trade, restaurants, and other local services – can increase program effectiveness. Targeting tax credits to certain industries can also capture high-paying jobs in growth industries or create jobs for individuals with less skill and educational attainment.

Five out of the six largest industries by Maryland employment claim few job creation and One Maryland tax credits. These large industries – health care, retail trade, construction, accommodation and food services, and administrative support services – employ a little more than one out of every two private-sector workers in the State but have received only 10% of job creation tax credits and less than 5% of One Maryland tax credits. Most job creation and One Maryland tax credits have been awarded to the transportation and warehousing, manufacturing, and finance and insurance industries, as shown in **Exhibit 5.3.** Relative to the national average, these industries comprise a smaller share of Maryland employment, particularly for the manufacturing industry. In addition to a high utilization of the One Maryland and job creation tax credits, a significant number of enterprise zones specifically target the manufacturing, transportation, and warehousing industries.

Exhibit 5.3
Share of Total Credits by Industry
Job Creation and One Maryland Tax Credits

Industry	Share of Total Credits: Job Creation	Share of Total Credits: One Maryland	Share of Maryland Employment
Transportation and Warehousing	26.5%	15.8%	3.5%
Manufacturing	20.1%	35.8%	4.9%
Finance and Insurance	16.7%	25.7%	4.5%
Total	**63.3%**	**77.3%**	**12.9%**

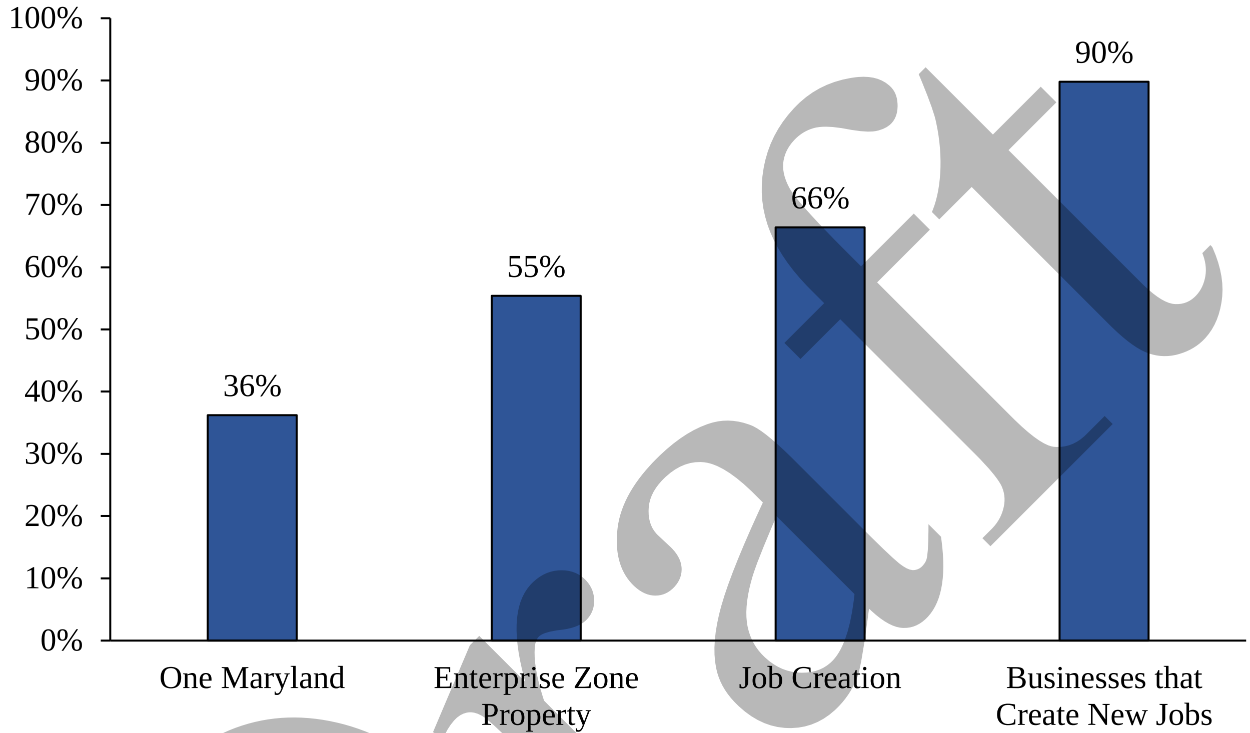
Source: Department of Commerce; U.S. Bureau of Labor Statistics; Department of Legislative Services

This mismatch between industry employment and program utilization will grow given current employment projections. Over the next 25 years, Maryland manufacturing employment is projected to decrease by one-fifth or 20,000 jobs and no growth is expected within the transportation and warehousing industry. In contrast, education and health services employment is projected to increase by one-quarter or 100,000 jobs.

Large Businesses Receive a Significant Concentration of Employment Tax Credits

A common outcome of State tax credit programs is a concentration of benefits to a few large corporations. Over one-half of the total credits ($640.2 million) shown in Exhibit 5.2 have or will be claimed by fewer than 50 companies through the One Maryland, AEDC project, and enhanced businesses that create new jobs programs. Of the 101 businesses eligible for a job creation tax credit, 10 businesses received a little more than one-half of all credits. Likewise, One Maryland credits are unevenly distributed as 10 certified businesses received 42% of all credits. Within Baltimore City for fiscal 2014, 4 companies out of the 288 companies claiming the enterprise zone property tax credit received one-third of the property tax credits. **Exhibit 5.4** compares by program the percentage of all credits claimed by the top 20% of businesses by credit size. Companies that are claiming a significant portion of the credits are typically large businesses, such as Fortune 500 companies and financial institutions. Additionally, many are claiming multiple State employment credits. For example, Morgan Stanley received the third largest job creation tax credit ($1.4 million) and also the third most One Maryland credits ($11.0 million).

Exhibit 5.4
Percent of Credits Claimed by Top 20% of Businesses by Credit Size



Source: Department of Commerce; State Department of Assessments and Taxation; Department of Legislative Services

Chapter 6. State and Local Costs of the Job Creation Tax Credit

State Costs

The job creation tax credit is an unbudgeted tax credit that is not subject to an aggregate limit on the amount of credits that can be awarded in each year. The annual revenue loss depends primarily on the certified number of qualifying jobs, the wages paid for those jobs, and the year in which the business claims the credit. As discussed previously, the value of the credit must be claimed over two years – this requirement is unique to the job creation tax credit. Any unused amount of credit can be carried forward to five tax years.

The Department of Commerce Does Not Certify the Value of the Credit

The Department of Commerce (Commerce) certifies a business for the total jobs that meet program requirements, as required by statute. However, Commerce does not certify or otherwise calculate the credit. Accordingly, the actual value of credits certified by Commerce is not known. Upon claiming the credit a business calculates the total credit available based on multiplying the total number of certified jobs in the credit year by the applicable credit percentage, subject to the maximum values of the credit.

Based on data provided by Commerce, the Department of Legislative Services (DLS) estimated the tax credit for which each business qualified through fiscal 2016. The credit value was calculated based on the number of qualifying jobs created, the wages paid for those jobs, and whether the business is located in a revitalization zone. During this time, Commerce issued 208 certifications to 101 businesses that reported creating 17,692 jobs. Tax credits totaled an estimated $21.8 million (in current 2016 dollars), as shown in **Exhibit 6.1**.

Exhibit 6.1
Total Jobs Certified and Eligible Credits
Fiscal 2002-2016

Fiscal Year	Certified Jobs	Eligible Credits	Average Credit	Average Wage
2002	3,877	$5,578,968	$1,439	$56,304
2003	1,256	1,679,343	1,337	45,953
2004	1,219	1,815,941	1,490	59,160
2005	483	584,861	1,211	54,021
2006	1,865	2,310,972	1,239	81,755
2007	855	664,558	777	39,879
2008	1,057	1,194,245	1,130	63,512
2009	262	306,787	1,171	69,417
2010	2,507	2,465,256	983	41,431
2011	548	681,351	1,243	66,656
2012	1,474	1,731,554	1,175	59,025
2013	384	508,296	1,324	77,549
2014	391	399,013	1,020	71,054
2015	637	837,571	1,315	75,067
2016	877	1,033,520	1,178	51,448
Total	**17,692**	**$21,792,236**	**$1,232**	**$57,879**

Note: Dollar amounts are expressed in constant 2016 dollars.

Source: Department of Commerce; Department of Legislative Services

Annual Credit Activity Varies Significantly

Commerce issued in each year an average of 14 certifications to 7 businesses (businesses are certified in each year in which the business meets the minimum job creation requirements). Commerce awarded on average $1.5 million in credits to businesses that reported a total of 1,179 qualifying positions, for an average of 85 employees per certification.

Although the credits awarded in each year are relatively modest compared to the State's most significant business tax credits, there is significant volatility from year to year and a lack of a consistent annual trend. On average, the annual percentage value of the credit changed (increase or decrease) by 72%. In one out of every five years Commerce awarded more than $2.0 million in credits, with a maximum of $5.6 million in fiscal 2002. Conversely, in about one out of every two years Commerce awarded less than $1.0 million in credits, with a low of $306,800 in fiscal 2009.

The year in which a business receives final certification is typically not the year in which the jobs are created. A business has 24 months to create the jobs and those jobs must be filled for at least 12 months. In addition, Commerce advises that some businesses apply for final credit certification a year or two later than the first eligible year and then file an amended tax return. Accordingly, most of the jobs reported in fiscal 2016 will reflect job creations in fiscal 2013, 2014, and 2015. Commerce advised that it is not certain as to the specific cause of the annual variation in tax credits. Given that few businesses claim the credit, a variation in the number of jobs created by businesses can cause significant changes in the total credits claimed. In fiscal 2002, 2006, and 2010, several of the businesses that claimed the credit reported creating a large number of jobs. For example, in fiscal 2002, three businesses – Southwest Airlines, T. Rowe Price, and Verizon Communications – each reported creating over 800 jobs in that year.

Data Limitations Make It Difficult to Determine the Amount of Credits Claimed

The total amount of credits awarded by Commerce to date does not reflect the actual cumulative fiscal cost to the State, which is dependent on the amount of credits claimed by businesses. The credit is not refundable, so if a business does not have sufficient tax liability in a taxable year the credit can be carried forward to future taxable years. Based on data provided by the Comptroller's Office, most credits have been claimed against the personal and corporate income tax. The Comptroller advises that it cannot provide a precise estimate of the amount claimed because it does not capture any amounts that are claimed as carry forwards. The Comptroller also advises that current law does not provide for the treatment or priority of carry forwards if a business carries forward more than one tax credit from a previous year.

The credit may also be claimed against the insurance premium tax or public service company franchise tax. DLS requested data from the Maryland Insurance Administration (MIA) on the total amount of job creation tax credits claimed in each tax year. MIA advised that for tax years 2013 and prior it did not have access to any automated records, and records for tax year 2014 and 2015 did not show any company filing for a job creation tax credit.

DLS has contacted MIA in previous years for information on the insurance premium tax, including information on all tax credits claimed. Although MIA typically could not respond to these requests, it did provide data several years ago showing that no job creation tax credits were claimed against the insurance premium tax in tax years 2002 through 2004 and that a total of \$2.9 million was claimed in tax years 2005 through 2008, for an average of \$719,300 in each year. No data was provided on the total number of companies that claimed the credit. The State Department of Assessments and Taxation does not have a record of any company claiming the credit against the public service company franchise tax in the last several tax years.

The Amount of Credits Awarded Each Year Has Declined Over the Long Term

The total amount of credits awarded by Commerce has decreased significantly over the long term. From fiscal 2002 to 2006, Commerce certified an average of 1,740 qualifying jobs. This decreased in the next five years (2007-2011) to an average of 1,046 jobs before decreasing further to 753 jobs in the last five years (2012-2016). As a result, the average amount of credits has also decreased – from $2.4 million in the first five years to about $900,000 within the last five years, a decrease of a little less than two-thirds. **Exhibit 6.2** details the credits awarded and business activity associated with the credit over each five-year period since fiscal 2002.

Exhibit 6.2
Job Creation Tax Credit
Total Jobs, Credits, Businesses, and Certifications
Fiscal 2002-2016

Fiscal Years	Jobs	Credits	Businesses	Certifications
2002-2006	8,700	$11,970,100	46	80
2007-2011	5,229	5,312,200	27	58
2012-2016	3,763	4,510,000	29	70
Total	**17,692**	**$21,792,300**	**102**	**208**

Note: Dollar amounts are expressed in constant 2016 dollars.

Source: Department of Commerce; Department of Legislative Services

A decrease in participating businesses was the largest factor causing the decrease in credits (explaining about 60% of the total). There was also a decrease in the number of jobs reported for each business claiming the credit – on average each business reported creating 59 fewer jobs within the last five fiscal years compared to the first five years. This decrease was responsible for a little less than one-third of the total decrease. From the first period to the last the average credit and credit percentage also decreased, from 2.3% to 1.9% and $1,376 to $1,198, respectively. However, this decrease explains only a minor (about 9%) amount of the overall decrease.

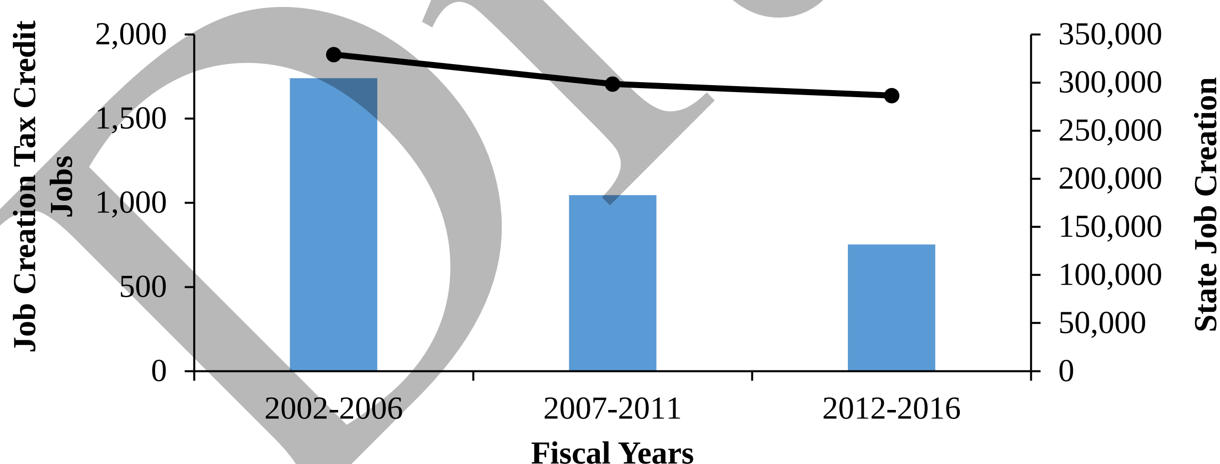
Declines in Job Creation Do Not Explain Long-term Decreases in Credit Activity

Given that the economic recovery from the Great Recession has created jobs at a slower rate than during previous recoveries, a decrease in job creation tax credit activity is not unexpected. However, the magnitude of the decrease in jobs and business activity associated with the credit is significantly larger than the decline in overall job creation.

The number of jobs associated with the tax credit has been very minor compared with the total number of private jobs created in the State, comprising about 0.4% of the 4.6 million private jobs created in the State since fiscal 2002. The diminishment of the credit over time means it has had even less influence in creating jobs in recent years. In fiscal 2002 through 2006, a business claimed a job creation tax credit for 1 out of every 189 jobs created in the State – this has subsequently decreased within the last five years to 1 out of every 380 job creations.

The Maryland economy created an average of 329,200 jobs annually (from fiscal 2002 through 2006). This reflects new jobs from both existing and new companies and does not equal the net change in employment, which would include job elimination at existing firms and businesses that cease operations. From fiscal 2007 through 2011 annual job creation decreased to 298,500 before decreasing further to 286,500 in fiscal 2012 through 2016. As a result, the Maryland economy has created 42,700 fewer new jobs annually within the last five years compared to fiscal 2002 through 2006, which is a decrease of 13%. However, over the same time period the average number of jobs associated with the job creation tax credit decreased from 1,740 to 753, a decrease of 57%, as shown in **Exhibit 6.3**.

Exhibit 6.3
Annual State Job Creation and
Job Creation Tax Credit Qualifying Jobs
Fiscal 2002-2016



Note: State job creation is the total number of new jobs created by existing and new businesses in the State and does not reflect the net change in employment in the State.

Source: Department of Commerce; U.S. Bureau of Labor Statistics – Business Employment Dynamics; Department of Legislative Services

Program Administrative Costs

Currently, two staff and a program manager at Commerce devote a portion of their time to administering the credit. In fiscal 2016, Commerce processed a total of 79 intent letters, issued 28 preliminary and 16 final certificates, and conducted additional compliance activity on about 40 companies.

One factor mitigating program administrative costs is the requirement that an independent certified public accountant (CPA) selected by the business must provide Commerce and the appropriate taxing authority with a written statement certifying that the credit amount claimed by the business is correct. Thus, businesses claiming the credit bear these compliance costs instead of the State. According to Commerce, CPA audit costs range from $10,000 to as much as $30,000 for more complicated certifications. Commerce advises that it currently does not have the staff needed to audit businesses in lieu of the current requirement.

Local Fiscal Impact

Local governments receive a portion of corporate income tax revenues to support the construction and maintenance of local roads and other transportation facilities. Job creation tax credits claimed against the corporate income tax will decrease local highway user revenues. Although only one-third of businesses claiming the credit file a corporate tax return, about 90% of the total amount of credits have been claimed against the corporate income tax through tax year 2014. Based on this data, local highway user revenues have decreased by an average of less than $10,000 annually in the last five tax years.

Chapter 7. Job Creation Tax Credit Program Activity

Credit Values and Reported Jobs

According to the Department of Commerce (Commerce), the job creation tax credit is the department's most widely used tax credit as it is available to a number of targeted industries and can be claimed throughout the State. On average, Commerce issues 14 certifications each year. A typical tax credit certification reports 51 jobs and has a value of $60,500. This translates to a credit of $1,200 for each job or 2.5% of the reported wages. Commerce issues a certification for each credit year in which the business facility (or establishment) reports creating the required minimum jobs. A little more than one-third of establishments received more than 1 certification, and overall there were 1.8 certifications for every establishment. In most instances, multiple certifications are issued to an establishment over several years, reflecting multi-year job expansions. Most frequently, these establishments received 2 certifications but ranged to a maximum of 8 certifications. Additional certifications increased the total credits received by each establishment – the establishment with 8 certifications received a total of $2.6 million in credits.

Almost every business claiming the credit operated only 1 establishment that received the credit, but a small number operated 2 establishments. In total, Commerce has issued 208 certifications to 117 establishments operated by 101 businesses. **Exhibit 7.1** shows the number of establishments and reported jobs by the value of the credit, the total number of certifications, and the total and median credit awarded by establishment and credit value.

Exhibit 7.1
Certifications and Credits Earned by Credit Amount
Fiscal 2002-2016

Credit Amount	Establishments	Certifications	Jobs	Credit Total	Credit Median
$0-$25,000	4	4	82	$100,000	$20,200
$25,000-$50,000	22	23	835	900,000	39,200
$50,000-$100,000	34	45	2,130	2,500,000	73,100
$100,000-$500,000	48	108	7,886	9,900,000	189,100
$500,000 or more	9	28	6,759	8,400,000	658,300
Total	**117**	**208**	**17,692**	**$21,800,000**	**$95,600**

Note: Credits are expressed in constant 2016 dollars.

Source: Department of Commerce; Department of Legislative Services

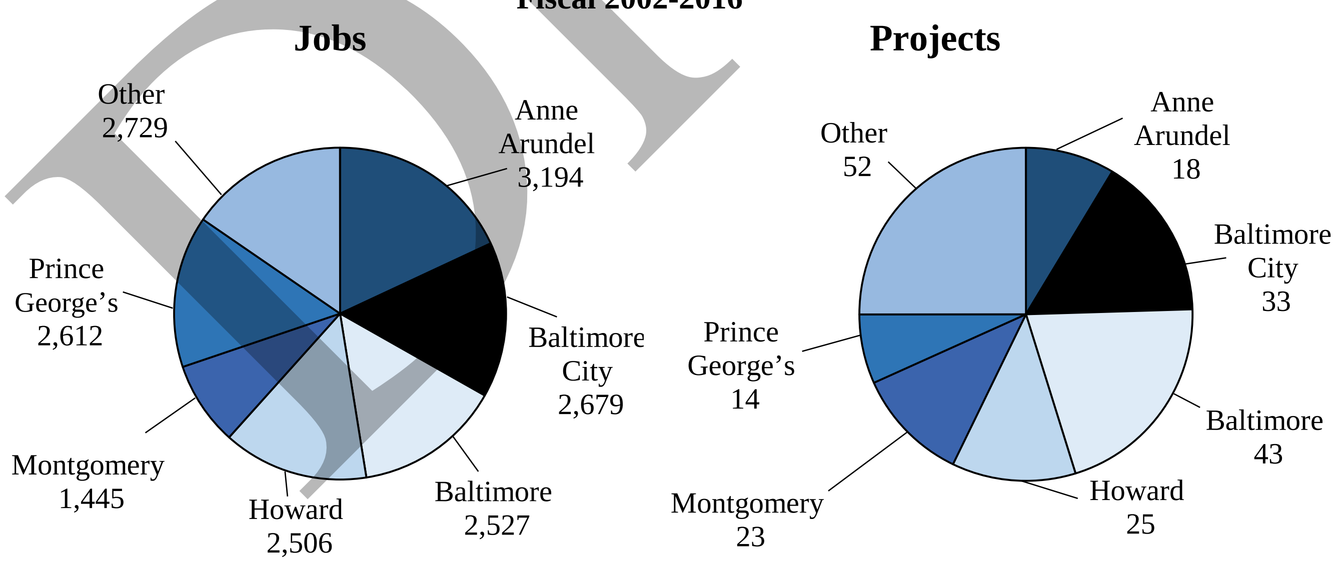
The long-term decrease in credit activity has also decreased the scope of the typical project and credit – in the last five fiscal years, the typical certification reported 40 jobs and a credit of $47,000 per certification, or just over $70,000 for each establishment or business. While no recent certification has exceeded $500,000, these certifications comprised about one-quarter of all credits issued before fiscal 2012.

Geographic Distribution

Credit Activity Is Not Concentrated In A Single Jurisdiction or Region

As shown in **Exhibit 7.2**, Anne Arundel County, with 3,194 jobs or a little less than one-fifth of all jobs, had the highest number of reported jobs, while Baltimore County had the most projects at 43. Credit activity is not concentrated within these counties, however, as eight counties have 500 or more reported jobs. This lack of geographic concentration contrasts with other State business tax credits that have awarded a significant portion of funding to one local jurisdiction. For example, Baltimore City projects account for about two-thirds of recently awarded tax credits under the heritage structure rehabilitation, One Maryland, and enterprise zone property tax credit programs.

Exhibit 7.2
Job Creation Tax Credit
Jobs and Projects
Fiscal 2002-2016



Source: Department of Commerce; Department of Legislative Services

No Credits Have Been Certified in a Quarter of All Counties

The prevalence of credit activity across the State, however, is not uniform. The variation in credit activity includes no projects in about one-quarter of all counties. The likelihood that businesses participate in the program primarily depends on the (1) share of employment and job creation within targeted industries and (2) frequency of significant job expansions. State job creation is concentrated in urban areas – in 2013, metropolitan areas created over 95% of all Maryland jobs. The Baltimore and Washington, DC metropolitan areas comprise most of these areas. Within the same year, metropolitan areas increased net employment by 45,500 compared to a decrease of 1,106 in nonmetropolitan areas. Businesses in rural areas are typically smaller – 88% of all firms in nonmetropolitan areas have less than 50 employees – and are less likely to create a sufficient number of jobs to qualify for the credit. Another factor that may influence credit participation across counties is the share of businesses located within State priority funding areas (PFA) given a reduced minimum job creation requirement.

About 15,000 of the jobs, or approximately 85% of the total jobs created, are located within the State's six most populous counties. Compared to this region's share of total employment (75%), businesses in these counties more frequently participate in the program compared to the rest of the State. The credit is more frequently claimed in Howard and Anne Arundel counties but less so in Montgomery County.

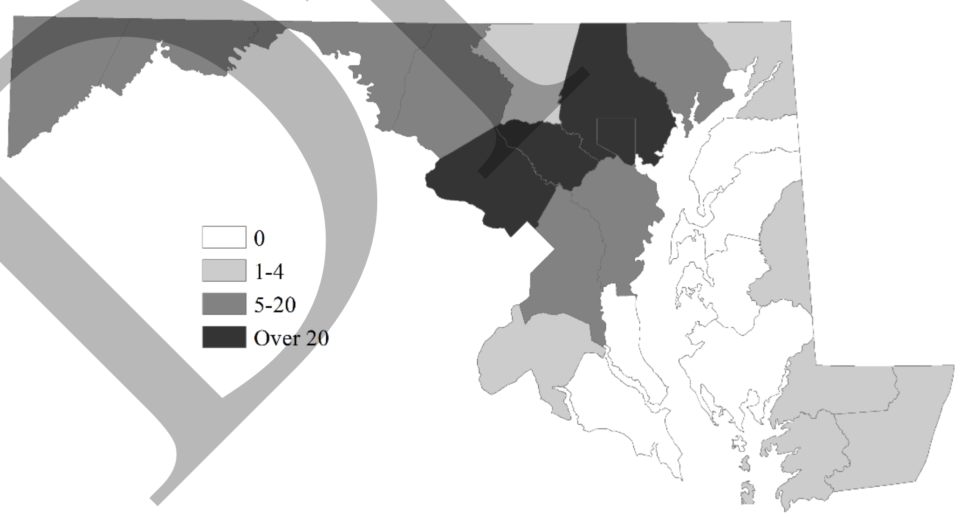
About 1,100 job creations are located in Western Maryland, which has a higher credit utilization, particularly within Washington County. Southern Maryland has the lowest credit utilization – only 37 jobs and none within Calvert and St. Mary's counties. Businesses located on the Eastern Shore (850 jobs) are also less likely to claim the credit. The vast majority of these jobs are located within Cecil and Somerset counties. No projects are located within Dorchester, Kent, or Queen Anne's counties.

Exhibit 7.3 illustrates the total jobs and projects within each local jurisdiction in fiscal 2002 through 2016. **Appendix 1** lists the total number of projects, jobs, and wages within each local jurisdiction. Average wages ranged from $22,414 in Allegany County to $72,316 in Wicomico County.

Exhibit 7.3
Number of Jobs and Projects by County
Fiscal 2002-2016

Jobs

Projects



Source: Department of Commerce; Department of Legislative Services

Priority Funding Areas and Revitalization Zones

The job creation tax credit promotes employment growth within (1) PFAs by lowering the minimum job creation threshold and (2) revitalization zones by providing enhanced credits.

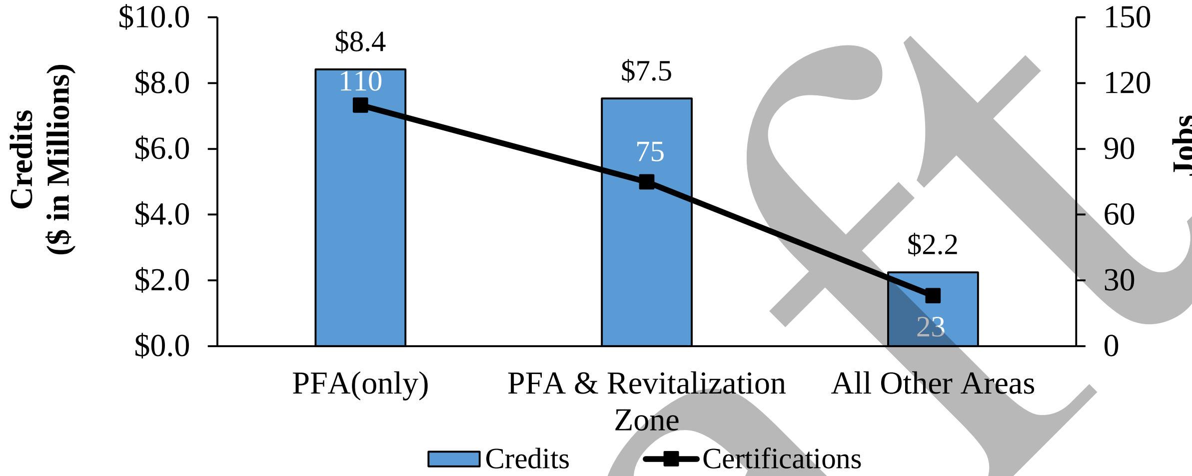
The Vast Majority of Credit Certifications Are Within Priority Funding Areas

Only 23 certifications to date have not been located within a PFA; as a result, about 90% of all credits have been certified for businesses in PFAs. Certifications within PFAs typically reported creating 21 fewer jobs and a credit value that was $11,500 less than certifications outside of a PFA.

Just Over One-third of Credit Certifications Are Within Revitalization Zones

Fewer credit certifications (just over one-third) have been within revitalization zones. The typical certification within a zone reported fewer jobs than other areas but had a larger average credit value of $100,400, about $20,000 greater than for credits outside revitalization zones, which reflects the impact of the enhanced credit. About 8 out of every 10 certifications within a revitalization zone are located within Baltimore City, the Eastern Shore, Western Maryland, and Harford County. About 90% of all certifications in these areas are located within a zone. Revitalization zone certifications are much less common in the rest of the State, particularly within Anne Arundel, Howard, Montgomery, and Prince George's counties. All of the 75 certifications located within a revitalization zone are within a PFA. **Exhibit 7.4** shows the total certifications and credits based on whether the establishment was located within a revitalization zone and also a PFA, a PFA only, and all other areas of the State.

Exhibit 7.4
Job Creation Tax Credits and Projects
Priority Funding Areas and Revitalization Zones
Fiscal 2002-2016



PFA: Priority Funding Area

Source: Department of Commerce; Department of Legislative Services

The enhanced credit increases provided an additional $33,400 per certification, an increase of about one-half. As a result, the total credits awarded to businesses within revitalization zones increased by a total of $2.5 million. Program costs increased by $167,100 annually, a 15% increase.

To determine the impact of the reduced minimum job requirement within a PFA, the Department of Legislative Services examined the 67 certifications issued to establishments that received only 1 certification. About one-half of these projects would not have qualified but for the lower job creation requirement. The lower threshold increased the total amount of credits awarded by about 25%.

The Definition of a State PFA for the Credit Is Different Than Under the Smart Growth Program

The definition of a PFA under the job creation tax credit conforms to the definition established by the Smart Growth Program with one exception. In addition to specified areas including municipal corporations, sustainable communities, enterprise zones, and areas within the Capital and Baltimore Beltway, a county may only designate one of the other areas designated as a PFA. This limitation may impact counties that have multiple, noncontiguous PFAs. According to Commerce, rural counties would benefit from being able to designate additional areas where businesses could be eligible for the credit, although it is not clear as to how this might impact credit utilization in these areas. In addition, the change could also impact some urban counties and the overall fiscal impact of the proposed change is unknown.

Types of Businesses Receiving the Credit

To be eligible for the job creation tax credit, a business must establish or expand a business facility that is primarily engaged in one or more of the following industries: (1) manufacturing or mining; (2) transportation or communications; (3) agriculture, forestry, or fishing; (4) research, development, or testing; (5) biotechnology; (6) computer programming, information technology, or other computer-related services; (7) central services for a business entity engaged in financial services, real estate services, or insurance services; (8) the operation of a public utility; (9) warehousing; (10) entertainment, recreation, cultural, or tourism-related activities if the business is located within a multi-use facility located in a revitalization zone if the facility generates at least 1,000 positions within 24 months and is not primarily used by a professional sports franchise or for gaming; or (11) other business services. In addition to these specific industries, a qualifying activity includes either the operation of central administrative offices or a company headquarters, other than the headquarters of a professional sports organization.

Exhibit 7.5 shows the total amount of projects and credits by industry as well as the average wages within each industry. Four industries – transportation and warehousing (about one-quarter of all credits); manufacturing (one-fifth); finance and insurance (16%); and professional, scientific, and professional services (12%) – account for three-quarters of all credits certified by Commerce. In general, the portion of reported jobs for all industries was equal to the industry's share of the total credits awarded.

Exhibit 7.5

Job Creation Tax Credit Certifications by Industry
Total Credits, Jobs, and Wages
Fiscal 2002-2016

Industry	Certifications	Credits Awarded Amount	Credits Awarded % Total	Reported Jobs Amount	Reported Jobs % Total	Average Wages
Mining, Quarrying, and Oil and Gas Extraction	1	$35,800	0.2%	34	0.2%	$164,000
Utilities	1	287,000	1.3%	159	0.9%	136,500
Manufacturing	51	4,372,800	20.1%	3,409	19.3%	64,500
Wholesale Trade	12	830,500	3.8%	907	5.1%	34,800
Retail Trade	4	310,900	1.4%	276	1.6%	34,800
Transportation	16	4,841,700	22.2%	3,688	20.8%	49,300
Warehousing	19	929,300	4.3%	948	5.4%	35,600
Information	22	1,584,400	7.3%	1,637	9.3%	50,600
Finance and Insurance	23	3,646,500	16.7%	2,398	13.6%	63,800
Professional, Scientific, and Technical Services	45	2,635,900	12.1%	2,301	13.0%	78,900
Administrative and Support Services	6	334,200	1.5%	235	1.3%	38,700
Health Care and Social Assistance	2	215,400	1.0%	179	1.0%	117,500
Accommodation and Food Services	4	1,533,200	7.0%	1,367	7.7%	49,900
Other Services	2	234,400	1.1%	154	0.9%	30,400
Total	**208**	**$21,792,200**		**17,692**		**$57,900**

Source: Department of Commerce; Department of Legislative Services

Chapter 8. Economic Impacts of the Job Creation Tax Credit

Analyzing the true economic impact of a tax credit requires isolating the impact of the credit from other factors that influence the business undertaking the qualifying activity. This approach will provide an estimate of how much economic activity resulted solely from the credit and was not due to other factors or that would have occurred even without receipt of the tax credit. An additional step requires an estimate of the net impact to State revenues – the cost of foregone revenue plus any additional State revenue that was generated by economic activity that would not have occurred without the credit. Since a balanced budget is required each year, revenue that is foregone under the credit requires either a corresponding reduction in State spending or an increase in revenue from individuals or businesses, both of which dampen economic activity. Lastly, any spillover impacts should be captured. Positive spillover impacts include a business using the reduction in taxes to increase production and purchase additional goods from Maryland businesses. Conversely, a negative spillover impact includes the competitive advantage conferred to businesses that receive tax credits. An increase in sales and jobs at these businesses might be at the expense of sales and jobs at other businesses that do not receive the tax benefit.

The REMI Model

The Department of Legislative Services (DLS) estimated the economic impacts of the job creation tax credit by using the REMI PI+ software. The REMI PI+ software is an economic impact tool that uses historical data and forecasts to create a dynamic model of the Maryland economy. The REMI model is a macroeconomic impact model that incorporates and integrates aspects of four major modeling approaches: (1) input-output; (2) general equilibrium; (3) econometric; and (4) economic geography. The REMI model, at its core, has the inter-industry relationships found in input-output models. As a result, the industry structure of a particular region is captured within the model, as well as transactions between industries. Changes that affect industry sectors that are highly interconnected to the rest of the State and regional economy will often have a greater economic impact than those that are not closely linked.

The REMI model generates year-by-year estimates of the total regional effects of a specific policy initiative or combination of initiatives. The model used by DLS is calibrated to the Maryland and District of Columbia region. Each calibrated region has economic and demographic variables as well as variables that test the economic impact of policy changes. Model simulations can estimate comprehensive economic and demographic effects of policies and programs for economic development, infrastructure, environment, energy, natural resources, and state and local tax changes. The primary national, state, and county data source for the REMI model is the State Personal Income and Local Area Personal Income series from the Bureau of Economic Analysis (which also include employment and total population data). This data is available for the United States and states at the summary level (94 industries), and for counties at the sector level (24 industries).

Model Data and Assumptions

Using the REMI PI+ software, DLS estimated the impact of the credit on the Maryland economy using the total job creation tax credit activity that has occurred through July 1, 2016. Tax credit claims are projected through tax year 2018 given that credits are generally claimed in the following two years. DLS assumed that the jobs associated with the program are maintained for four years as required by the program. To the extent that these jobs continue beyond this period, the economic benefits of the program will be greater than estimated.

Another important assumption is estimating the gross number of jobs created by the program – those jobs that would not exist but for the tax credit incentive – relative to which jobs would have been created in the absence of the program. For the jobs that are created by the program, DLS assumes that a business that receives the tax credit spends the money on hiring additional workers. This impact is modeled by adding the additional jobs and wage information based on the industry of the employer. For the remaining jobs it is assumed that the tax credit received by a business results in lower business taxes. This is also modeled based on the industry of the business.

DLS assumes that the credit was a decisive factor in 5% of the jobs associated with the program based on the value of the credit relative to employee costs, the economic literature reviewed by DLS, and an examination of the overlap between the job creation tax credit and other state employment tax credits. This research includes Bartik and Erickcek's study on Michigan's MEGA tax credit program, which included three REMI scenarios assuming that between 2% and 8% of MEGA credits were decisive in hiring decisions. DLS notes that the Michigan credit provides a more significant incentive than the job creation tax credit. As detailed in previous tax credit evaluations, a business that qualifies for the job creation tax credit may also receive other federal, State, and local financial assistance. This includes State tax credits such as the enterprise zone and One Maryland tax credits and financial assistance from the Department of Commerce (Commerce). DLS examined a sample of the businesses that claimed the job creation tax credit and found that a significant portion also claimed the One Maryland or enterprise zone tax credits. In most instances, the financial assistance provided by these programs was significantly greater than that provided by the job creation tax credit.

Tax Credit Provides Modest Incentive

The job creation tax credit is unlikely to increase employment unless a business believes there is sufficient demand for their products. Businesses not only factor in current conditions but are forward looking – for example, business confidence about the direction of the economy can significantly influence hiring decisions. In addition, the job creation tax credit incentive is minor relative to the total cost of employing an individual. On average, each business received a job creation tax credit of $1,237 for each employee. This represents a little more than 2% of the average wages ($58,105) paid to these employees. The credit comprises even less of an employer's total costs after considering additional compensation costs and additional years of unsubsidized employment.

According to the U.S. Bureau of Labor Statistics, wages comprise 71% of an employee's total compensation in the region. Using this estimate and the assumption that a business employs the individual for four years, the credit subsidizes less than 0.4% of the employer's total costs, as shown in **Exhibit 8.1**.

Exhibit 8.1
Value of Job Creation Tax Credit
Relative to Total Employment Costs

Average Wage	$58,105
Paid Leave	5,835
Supplemental Pay	2,219
Insurance	6,493
Retirement and Savings	3,287
Social Security and Medicare	4,849
Unemployment Insurance	411
Workers' Compensation	986
Total Annual Compensation	**$82,185**
Total Four-year Compensation	$328,740
Average Job Creation Tax Credit	$1,237
Credit %/ Total Compensation	**0.4%**

Source: Bureau of Labor Statistics; Department of Commerce; Department of Legislative Services

Estimated Economic Impacts

Positive Effects of Tax Credit Spending

Exhibit 8.2 shows the maximum positive economic impacts of the job creation tax credit based on the assumptions described previously. Employment increases by approximately 476 jobs annually relative to a baseline employment of about 3.7 million. There is a net State gross domestic product (GDP) average annual increase of $69 million and disposable personal income across the entire State increases annually by $39 million.

Exhibit 8.2
Job Creation Tax Credit Impacts
Employment, Income, and Gross Domestic Product

	Annual Average
Employment (Individuals)	
Baseline	3,690,298
After Credit	3,690,774
Net Effect	**476**
Gross Domestic Product ($ in Millions)	
Baseline	$420,380
After Credit	420,449
Net Effect	**$69**
Disposable Personal Income ($ in Millions)	
Baseline	$366,663
After Credit	366,702
Net Effect	**$39**

*May not sum to total due to rounding.

Note: REMI defines a "job" as a unit of labor equivalent to 12 months of employment in a given year. REMI determines the number of jobs based on the amount of output for an industry and the labor productivity of the area. Specifically, the number of "jobs" in any given year is an industry's output, divided by the average labor productivity of the industry. Effectively what this means is that "jobs" are relative to the average labor productivity of an industry and do not represent specific individuals in that industry.

Source: Department of Legislative Services

Offsetting Foregone Tax Revenue

To accurately reflect the full economic impact – which includes the requirement to maintain a balanced budget – a reduction in tax revenue from a job creation tax credit must be offset by (1) decreased government spending; (2) increased revenue from other sources; or (3) a combination of both revenue increases and spending decreases**.** The job creation tax credit was likely offset by a reduction in government spending, rather than an increase in revenue from other sources.

To balance the State budget, DLS assumed there was a corresponding reduction in government spending equal to the total amount of job creation tax credits issued. The effects of this decreased government spending are shown in **Exhibit 8.3** below. For example, Commerce approved tax credits totaling $0.6 million in 2014; this requires a corresponding decrease in government spending to balance the State budget. Government spending is relatively labor intensive; more of each dollar spent by the State is allocated to employee compensation than in most private-sector industries. Reducing government spending reduces both government employment and, through lower overall demand in the economy, some private-sector jobs.

On average, the required reduction in government spending as a result of the job creation tax credit decreases employment by 22 jobs, GDP by $2.0 million, and disposable personal income by $1.8 million. This also represents the worst case scenario of the credit. If the credit does not actually change an employer's behavior so all of the businesses eligible to receive the credit would have created the jobs in Maryland without the credit, then employment decreases by approximately 22 jobs annually.

Exhibit 8.3

Job Creation Tax Credit
Reduction in Government Spending Impact
Employment, Income, and Gross Domestic Product

	Annual Average
Employment (Individuals)	
Baseline	3,690,298
After Credit	3,690,275
Net Effect	**(22)**
Gross Domestic Product ($ in Millions)	
Baseline	$420,380
After Credit	420,378
Net Effect	**($2.0)**
Disposable Personal Income ($ in Millions)	
Baseline	$366,663
After Credit	366,661
Net Effect	**($1.8)**

Note: REMI defines a "job" as a unit of labor equivalent to 12 months of employment in a given year. REMI determines the number of jobs based on the amount of output for an industry and the labor productivity of the area. Specifically, the number of "jobs" in any given year is an industry's output, divided by the average labor productivity of the industry. Effectively what this means is that "jobs" are relative to the average labor productivity of an industry and do not represent specific individuals in that industry.

Source: Department of Legislative Services

The net impact of the job creation tax credit is summarized in **Exhibit 8.4**. Overall, the program has a minor impact on employment, GDP, and disposable personal income, primarily reflecting the limited scope of the incentive as well as the impact of the overlap between other State employment tax credit programs.

Exhibit 8.4

Job Creation Tax Credit
Net Economic Impacts
Employment, Income, and Gross Domestic Product

	Annual Average
Employment (Individuals)	
Baseline	3,690,298
After Credit	3,690,752
Net Effect	**454**
Gross Domestic Product ($ in Millions)	
Baseline	$420,380
After Credit	420,447
Net Effect	**$67**
Disposable Personal Income ($ in Millions)	
Baseline	$366,663
After Credit	366,700
Net Effect	**$37**

Numbers may not sum to total due to rounding.

Note: REMI defines a "job" as a unit of labor equivalent to 12 months of employment in a given year. REMI determines the number of jobs based on the amount of output for an industry and the labor productivity of the area. Specifically, the number of "jobs" in any given year is an industry's output, divided by the average labor productivity of the industry. Effectively, what this means is that "jobs" are relative to the average labor productivity of an industry and do not represent specific individuals in that industry.

Source: Department of Legislative Services

Chapter 9. Findings and Recommendations

Based on the information and analysis provided in this report, the Department of Legislative Services (DLS) makes a number of findings and recommendations about the job creation tax credit, as discussed below.

The Job Creation Tax Credit Provides a Modest Incentive to Large Businesses and Overlaps with Other State Employment Tax Credits

The job creation tax credit incentive is minor relative to the total cost of employing an individual, so the credit is unlikely to increase employment in most instances. On average, each business received a job creation tax credit of $1,237 for each employee. This represents a little more than 2% of the average wages paid to these employees and less than 0.4% of an employer's total costs after considering additional compensation costs and additional years of unsubsidized employment. Thus, it is unlikely that the credit significantly influences hiring decisions. Few businesses claim the credit in each year. In each year, less than 10 businesses that report creating about 1,100 jobs are certified for the job creation tax credit. By comparison, within the last three years an average of 11,400 new establishments in the State created 92,500 jobs each year, so the vast majority of businesses do not benefit from the tax credit.

Those businesses that do claim the credit are generally not reflective of the overall Maryland economy. Minimum job creation and other eligibility requirements limit the ability of new or smaller businesses to receive the credit, so participating businesses are much more likely to be large established companies. State employment growth, however, is the result of a number of factors and represents a diverse spectrum of companies. Most of the job creation tax credits have been claimed by businesses in the manufacturing, transportation and warehousing, and finance and insurance industries, so businesses in many industries have not benefited from the tax credit.

Furthermore, there is significant overlap between the job creation tax credit and other State employment tax credits. Most employment tax credits require that a minimum number of jobs be created in order to qualify; as a result, companies claiming other employment tax credits are also often large established companies. The industries that qualify for the job creation tax credit also generally qualify for the enhanced businesses that create new jobs, One Maryland, and enterprise zone credits.

There is a significant overlap and lack of coordination of the goals and objectives of these credits. The job creation tax credit provides an enhanced credit for businesses that are located within a revitalization zone. The total amount of additional incentives provided to these distressed areas is minor relative to the two State programs – enterprise zone and One Maryland – that specifically aim to increase economic activity and employment in distressed areas of the State. In addition, multiple programs providing inconsistent incentives do not provide clear signals that help influence business decisions in the desired manner.

The State also has two credits – the enhanced businesses that create new jobs and aerospace, electronics, and defense contract credits – that have the primary aim of job retention by large businesses. However, these credits have complex and differing eligibility requirements.

Recommendation: Considering the tax credit's modest incentive and overlap with other employment tax credits, DLS recommends that the General Assembly consider eliminating the job creation tax credit or consolidating the credit with other employment tax credits. If considering the consolidation of the employment tax credits, DLS recommends that the General Assembly consider establishing one program to increase economic growth within distressed areas and one program to promote broad-based job creation across the State, including provisions that target job creation for small and newly established businesses and businesses in high-growth industries. If the General Assembly considers job retention a goal, DLS recommends consolidating the existing job retention credits into one program with less complex and more streamlined eligibility requirements.

While Credit Activity Has Occurred in Every Region of the State, No Credits Have Been Certified in a Quarter of All Counties

No businesses located within Calvert, Dorchester, Kent, Queen Anne's, St. Mary's, and Talbot counties have been certified for any credits through fiscal 2016. One factor explaining the lack of activity in some parts of the State is that it may be more difficult for businesses in rural areas to create the minimum number of required jobs. Of the firms in nonmetropolitan areas in the State, 88% of those firms employ less than 50 employees, so job creation in these areas is less likely to meet the minimum threshold of 60 jobs. Unlike the businesses that create new jobs tax credit, the job creation tax credit does not have a lower job creation threshold for rural and less populated areas of the State.

Recommendation: DLS recommends that the General Assembly consider lowering the minimum threshold for the number of jobs created by businesses in rural counties. DLS also recommends that the Department of Commerce (Commerce) comment on any impacts such a change could have on the overall fiscal cost of the credit.

The Number of Businesses Claiming the Credit Has Declined Over Time

The job creation tax credit has a limited impact on overall job creation in the State. Moreover, its impact has decreased significantly over the last 15 years. Due to the Great Recession and long-term trends that predated the recession, the total number of jobs created in the State has slowed in the last several years. However, the number of job creations reported by businesses claiming the credit has decreased by a significantly greater amount. In fiscal 2002 through 2006, a business claimed a job creation tax credit for 1 out of every 189 jobs created in the State – this has subsequently decreased within the last five years to 1 out of every 380 job creations.

Recommendation: Commerce should comment on the reasons for the decrease in credit activity, including its efforts to conduct outreach and inform businesses about the credit.

Commerce Does Not Certify the Value of the Job Creation Tax Credit

Commerce is required by statute to certify that a business meets program requirements. While a business is required to provide Commerce with any information needed to verify that the business is eligible, Commerce is not required to certify the actual value of the credit. Consequently, Commerce certifies the number of qualified positions but not the value of the credit.

Recommendation: DLS recommends that the General Assembly require that Commerce certify the credit amount for each eligible business.

No Businesses That Qualified for the Credit Created At Least 30 New Jobs with Highly Paid Average Salaries

If not located within a priority funding area (PFA), an eligible business must create 60 new jobs within a two-year period to claim the tax credit. The minimum number of required jobs is lowered to 30 if the average salaries of the new jobs are highly paid as determined by a sliding scale relative to the average State salary. In fiscal 2002 through 2016, Commerce issued a total of 208 certifications, about 90% of which were issued to businesses within a PFA and thus required 25 new jobs. All of the businesses that were not located within a PFA met the 60 new job threshold. It does not appear that any business has qualified for the credit by creating 30 highly paid jobs.

Recommendation: Since the credit does not appear to provide a strong incentive to hire highly paid workers, DLS recommends that the General Assembly eliminate the eligibility standard that a business can qualify for the credit by creating 30 new jobs if the average salaries of the new jobs are highly paid.

The Legislative Intent of the Credit Contained in Statute Differs from the Intent Stated in Regulation

The legislative intent of the credit as stated in statute is to increase the number of new jobs in the State by encouraging (1) the expansion of existing private-sector enterprises and (2) the establishment or attraction of new private-sector enterprises. Commerce has, through regulation, expanded the objectives of the tax credit to increase the number and quality of new jobs in the State by encouraging (1) significant expansions of existing private-sector enterprises; (2) establishment of new private-sector enterprises; (3) creation of family supporting jobs; and (4) revitalization of neighborhoods and commercial areas. However, Commerce does not view the credit as a community revitalization program.

Recommendation: Since Commerce does not view the credit as a community revitalization program, DLS recommends that Commerce amends its regulations to remove the objective of revitalizing neighborhoods and commercial areas.

The Definition of a State Priority Funding Area for the Job Creation Tax Credit Is Different Than Under the Smart Growth Program

A State priority funding area is defined as (1) a municipal corporation, including Baltimore City; (2) a sustainable community; (3) an enterprise zone as designated by Commerce or by the U.S. government; (4) those areas of the State located between Interstate Highway 495 and the District of Columbia or Interstate Highway 695 and Baltimore City; and (5) no more than one area in a county, as designated by the county. Under the Smart Growth program, the definition is generally the same except that a county may designate any area as a PFA and is not limited to one area only. According to Commerce, conforming the definition to the one used for the Smart Growth Program would reduce confusion and could increase program participation in rural areas.

Recommendation: DLS recommends that Commerce comment on how conforming the definition of a PFA would impact each county, particularly rural counties, and any impacts this change could have on the overall fiscal cost of the credit.

The Job Creation Tax Credit Must Be Claimed Over Two Tax Years

The calculation of the job creation tax credit and administration of the credit are relatively straightforward. However, unlike other credits a business claiming the credit must claim the credit over two tax years.

Recommendation: Commerce should comment on whether the advantages from eliminating the two-year requirement, including increased benefits to businesses and enhanced tax administration, are outweighed by tax compliance issues or other considerations.

The State Minimum Wage Should Be Used as a Criterion for Determining a Qualified Position

In order to qualify for the tax credit a qualifying position must meet several requirements, including the requirement that the position pay at least 150% of the federal minimum wage. State law currently requires that employers pay a minimum wage of $8.75 per hour (scheduled to increase to $10.10 on July 1, 2018) whereas federal law requires a minimum wage of $7.25 per hour.

Recommendation: DLS recommends that the General Assembly specify that a qualified position pay at least 150% of the greater of the federal or State minimum wage. DLS also recommends that other employment tax credits with this requirement be altered in the same fashion.

Commerce Should Provide Additional Information about the Job Creation Tax Credit

Commerce currently reports specified information about the job creation tax credit, including the companies claiming the credit and the number of certified jobs created, on an annual basis. In the final tax credit application Commerce collects additional information, including whether the company is a minority business enterprise or women-owned firm.

Recommendation: In order to better assess the credit's effectiveness in promoting job creation in different types of businesses, DLS recommends that Commerce collect and report the following information for each applicant: (1) whether the credit resulted from a business expansion, new business, or relocation; (2) whether the business had a presence in Maryland before claiming the credit; (3) the total employment of the establishment; and (4) the total number of years the company has been in business.

Recommendation: Considering the General Assembly's interest in providing business opportunities for small, minority-, and women-owned businesses, DLS recommends that the General Assembly require Commerce to report on the number of businesses that qualify as small, minority-, and women-owned businesses.

The Comptroller's Office Can Only Provide Partial Information on the Total Amount of Credits Claimed

The Comptroller's Office provided DLS with data on the total number of returns claiming the credit and the amount of total credits claimed. However, the Comptroller's Office advises that the data reflects only credits claimed by a business in the first two tax years and does not include any amounts that may be carried forward to future tax years. In addition, the Comptroller's Office advises that current law does not currently provide for the treatment or priority of carry forwards if a business carries forward more than one tax credit from a previous year.

Recommendation: DLS recommends that the General Assembly specify the treatment or priority of tax credit carry forwards if the business is claiming multiple tax credits. In addition, the Comptroller's Office should adopt procedures to track tax credit carry forwards for all tax credits in order to more accurately report the amount of credits claimed each year.

The Maryland Insurance Administration Did Not Provide Any Information on Insurance Premium Tax Credits Claimed in Recent Years

The job creation tax credit can be claimed against the insurance premium tax. The Maryland Insurance Administration administers this tax but was unable to provide any recent data on the amount of credits claimed or the number of businesses that claim the credit.

Recommendation: DLS recommends that the General Assembly require the Maryland Insurance Administration to report annually for each credit that can be claimed against the insurance premium tax, the total amount of the credits claimed, and the number of businesses claiming the credit.

Requiring A Business to Have a Certified Public Accountant Verify the Credit Can Be Costly, Particularly for Small Businesses

An independent certified public accountant (CPA) selected by the business must provide Commerce and the appropriate taxing authority with a written statement stating that the credit amount claimed by the business is correct. Thus, the business covers the cost of compliance instead of the State. According to Commerce, a CPA audit can be costly for businesses and can cost between $10,000 and $30,000 for more complicated audits.

Recommendation: DLS recommends that the General Assembly consider options to simplify the credit verification process. One option would be to have Commerce verify the information by establishing a payroll record data-sharing agreement with the Department of Labor, Licensing, and Regulation.

Appendix 1. Job Creation Tax Credit Projects, Jobs, and Wages by County Since Inception

	Projects	Jobs	Wages	Average Wage
Allegany	5	187	$4,191,358	$22,414
Anne Arundel	18	3,194	150,504,310	47,121
Baltimore City	33	2,679	156,640,092	58,470
Baltimore	43	2,527	124,057,934	49,093
Calvert	0	0	0	0
Caroline	2	59	1,384,536	23,467
Carroll	1	63	2,595,138	41,193
Cecil	3	289	6,711,374	23,223
Charles	2	37	2,037,044	55,055
Dorchester	0	0	0	0
Frederick	6	387	19,177,924	49,555
Garrett	6	132	8,928,804	67,642
Harford	9	544	20,217,096	37,164
Howard	25	2,506	137,772,680	54,977
Kent	0	0	0	0
Montgomery	23	1,445	84,327,718	58,358
Prince George's	14	2,612	113,866,718	43,594
Queen Anne's	0	0	0	0
St. Mary's	0	0	0	0
Somerset	3	184	4,376,053	23,783
Talbot	0	0	0	0
Washington	13	796	26,756,958	33,614
Wicomico	1	26	1,880,215	72,316
Worcester	1	25	1,360,495	54,420
Total	**208**	**17,692**	**$866,786,447**	**$48,993**