Julie Palakovich Carr
Legislative District 17
Montgomery County

Ways and Means Committee

The Maryland House of Delegates
6 Bladen Street, Room 202
Annapolis, Maryland 21401
410-841-3037 · 301-858-3037
800-492-7122 *Ext.* 3037
Julie.PalakovichCarr@house.state.md.us

THE MARYLAND HOUSE OF DELEGATES
Annapolis, Maryland 21401

Testimony in Support of HB 148
Economic Development – Enterprise Zone Program – Alterations

This bill would reform the Enterprise Zone tax credits to make the program more targeted to economically distressed areas and to put financial guardrails on the program. The bill is follow-up legislation to a bill enacted in 2022 after an informal summer study that included representatives of the House Ways and Means Committee, Maryland Association of Counties, the Maryland Municipal League, several local economic development officers, and the Department of Commerce.

The Enterprise Zone program is one of the most expensive state and local business tax credit programs in Maryland, with over $628 million in tax credits awarded over the past twenty years. Costs for the enterprise zone tax credit have been growing at an average rate of 13% a year and the program has no statutory restraints on future costs.

Evaluations Show Limited Effectiveness

The Enterprise Zone Tax Credit program has had very limited effectiveness in meeting its goal of trying to spur revitalization of economic distressed areas. The Department of Legislative Services (DLS) conducted reviews of the enterprise zone tax credits in 2022 and 2014. The most recent evaluation recommended consolidation of the enterprise zone tax credits with other similar programs, or if not feasible, then major legislative reforms to the program.

Both DLS evaluations concluded that “Enterprise Zone tax credits are not effective in creating employment opportunities for Enterprise Zone residents.”[1,2] Additionally, the program criteria are “poorly designed” and “...limit the program’s effectiveness in promoting economic activity within distressed areas...” Monies spent in the program are poorly targeted, with only one dollar of tax credits going to the most distressed neighborhoods for every three to four dollars going to the least distressed communities.

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[1] “Evaluation of the Enterprise Zone Tax Credit,” 2014, Department of Legislative Services.
[2] “Evaluation of the Enterprise Zone Tax Credit,” 2022, Department of Legislative Services.

DLS also found that the income tax credit continues to be underutilized, with only 12 employers certified in the last five years.

In response to the 2014 DLS report, the Department of Commerce proposed legislative reforms to the program, including reducing the time that a business could receive the property tax credit from ten years to five years and eliminating the employment-based tax credit. These reforms were not enacted and to date, none of DLS's substantive recommendations regarding the program have been implemented.[3]

The Center for Regional Economic Competitiveness evaluated Maryland's EZ program, finding:[4]

- Maryland is among a small number of US states that does not impose an overall cap on the statewide or even local use of enterprise zone credits. Nearly every other state invokes an annual cap on total credits along with caps on the value of credits that can be used for a single project or company.
- Maryland does not have a regular schedule in place for reviewing or updating zone designations to ensure that the program is being utilized and that the designated zones meet established criteria for economic distress.
- Maryland's threshold for receiving benefits—the creation of one full time job in the zone—is fairly low. Many other states use higher thresholds before zone benefits commence. This may include a higher number of new jobs or higher levels of new investment.

Additionally, national studies find fault with enterprise zone tax credits. The National Conference of State Legislatures reports that "academic reviews of enterprise zones, often prepared using econometric models, have found little evidence that programs actually result in net job creation and increased community investment."[5]

Economist David Neumark, a professor at the University of California, Irvine, conducted an encompassing review of the research on enterprise zones and concluded that: "it is very hard to make the case that the research establishes the effectiveness of enterprise zones in terms of job creation, poverty reduction, or [economic] welfare gains."[6]

Good Jobs First, a national think tank with expertise on tax policy, writes that enterprise zone subsidies "cost state and local treasuries a lot of lost revenue, and like many

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[3] In the 2022 session, the General Assembly enacted HB 478, which made minor changes to the program, but did not address the most substantive problems.
[4] CREC Maryland Economic Development Finance Program Study, January 2016.
[5] "Enterprise Zones: Development for Distressed Communities," 2005, National Conference of State Legislators.
[6] "Rebuilding Communities Jobs Subsidies," 2018, David Neumark, The Hamilton Project.

subsidy programs, it is often unclear whether the developments would have happened in the area anyway."[7]

The ineffectiveness of enterprise zones has prompted further review in other states and led the California and Kentucky legislatures to end their state's enterprise zone tax credits. Nine other states have also allowed their EZ programs to sunset in recent years.

1,200% Cost Increase Since 2001

Local governments have the ability to request the designation of a new enterprise zone or the expansion of an existing zone. As long as the area meets the criteria outlined in state law, the Department of Commerce *has* to approve it. The state is then required to pay for 50% of the costs of the property tax credits claimed by businesses within the enterprise zone; the other half of the cost is borne by the local government.

Once Commerce approves a new enterprise zone or expansion of an existing zone, there are *no limitations* to how many businesses can participate or limits on the program's cost.

This has been a recipe for unrestrained growth in terms of geographic size and the cost of the tax credit. <u>The state's share of the program's cost has grown from $2.5 million in FY 2001 to nearly $30 million in expected FY 2024 expenditures—an increase of 1,200%.</u>

The cost of the program will likely continue to increase in future years since there are no guardrails on the cost of the program. Simply put, the state cannot afford to continue to pay these greatly escalating costs, especially when the program has not shown to be effective.

What This Bill Does

This legislation would implement common sense reforms to the enterprise zone tax credits. Most elements of the bill were recommended by DLS in its 2022 and 2014 program evaluations.

This legislation maintains the Enterprise Zone tax credits as independent credits and does not combine it with another state tax credit. Additionally, it maintains the flexibility of the program to be applicable to all types of businesses and retains both the property

[7] https://www.goodjobsfirst.org/accountable-development/enterprise-zones

tax credit and the income tax credits, but makes some modifications to the program's details.

- Sets an overall cap of $60 million per year for property tax credits. If the program exceeds that amount, no new zones or large expansions of existing zones can occur that year.
    - Businesses that are already certified to receive the tax credit would continue to receive it, in spite of the cap.
    - New businesses in existing zones could apply for and receive the tax credit, in spite of the cap.
- Caps the property tax credit at $500,000 per property.
    - Current recipients of the tax credit would be grandfathered and not subject to the cap.
    - 95% of properties received less than $500,000 in FY 2022.
- Caps the income tax credit at $250,000 per business and $2 million for the program in total.
    - Current recipients of the tax credit would be grandfathered and not subject to the cap.
- Focuses measurements of economic distress on individual Census tracts, rather than looking at surrounding areas.