# HB 764

# Department of Legislative Services

Maryland General Assembly
2012 Session

## FISCAL AND POLICY NOTE
## Revised

House Bill 764 (Delegate Frick, *et al.*)
Ways and Means Budget and Taxation

### Tax Credit Evaluation Act

This bill establishes a process for evaluating State tax credits. The bill provides for a legislative committee evaluation process in consultation with the Comptroller's Office, the Department of Budget and Management (DBM), and the Department of Legislative Services (DLS). The tax credit evaluation dates are staggered over a four-year period from July 1, 2014, through July 1, 2017. The bill also requires that the tax credits must be reevaluated every five years.

The bill takes effect July 1, 2012.

## Fiscal Summary

**State Effect:** General fund expenditures increase by $255,500 in FY 2013 due to implementation costs at DLS. Future year estimates reflect annualization, inflation, and ongoing costs. Revenues are not affected.

| (in dollars) | FY 2013 | FY 2014 | FY 2015 | FY 2016 | FY 2017 |
|---|---|---|---|---|---|
| Revenues | $0 | $0 | $0 | $0 | $0 |
| GF Expenditure | 255,500 | 296,800 | 305,200 | 312,100 | 319,400 |
| Net Effect | ($255,500) | ($296,800) | ($305,200) | ($312,100) | ($319,400) |

*Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect*

**Local Effect:** None.

**Small Business Effect:** None.

## Analysis

**Bill Summary:** The bill establishes a legislative process for evaluating tax credits. The evaluation process is conducted by a legislative evaluation committee and must be done in consultation with the Comptroller's Office, DBM, and DLS. The committee is appointed jointly by the President of the Senate and the Speaker of the House and must include at least one member of the Senate Budget and Taxation Committee and one member of the House Ways and Means Committee.

The following credits are required to be reviewed by the date indicated:

- *July 1, 2014:* (1) enterprise zone; (2) taxes paid to another state; (3) installment sales; (4) earned income; (5) film production activity; (6) job creation; (7) sustainable communities; and (8) neighborhood and community assistance contributions.
- *July 1, 2015:* (1) qualified employees with disabilities; (2) Maryland-mined coal; (3) businesses that create new jobs; (4) certain residential real estate property; (5) telecommunication business property; (6) poverty level; and (7) employer-provided long-term care insurance.
- *July 1, 2016:* (1) work-based learning program; (2) One Maryland economic development; (3) employee commuter benefits; (4) child and dependent care expenses; (5) quality teacher incentive; (6) long-term care insurance; and (7) clean energy incentive.
- *July 1, 2017:* (1) research and development; (2) green buildings; (3) preservation and conservation easements; (4) aquaculture oyster floats; (5) biotechnology investment; (6) cellulosic ethanol technology; (7) bio-heating oil; and (8) qualified electric vehicle recharging property.

By June 30 of the year prior to a tax credit's evaluation date, the evaluation committee is required to meet with the Comptroller's Office, DBM, and DLS to prepare a plan for evaluation. By October 31 of the same year, DLS is required to publish a report evaluating the tax credit. The report submitted by DLS must discuss (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. By December 14 of the same year, the evaluation committee must hold a public hearing on the evaluation report.

By the twentieth day of the legislative session before the evaluation date of a tax credit, the committee is required to submit a report to the General Assembly that states whether or not the tax credit should be continued, with or without changes, or terminated.

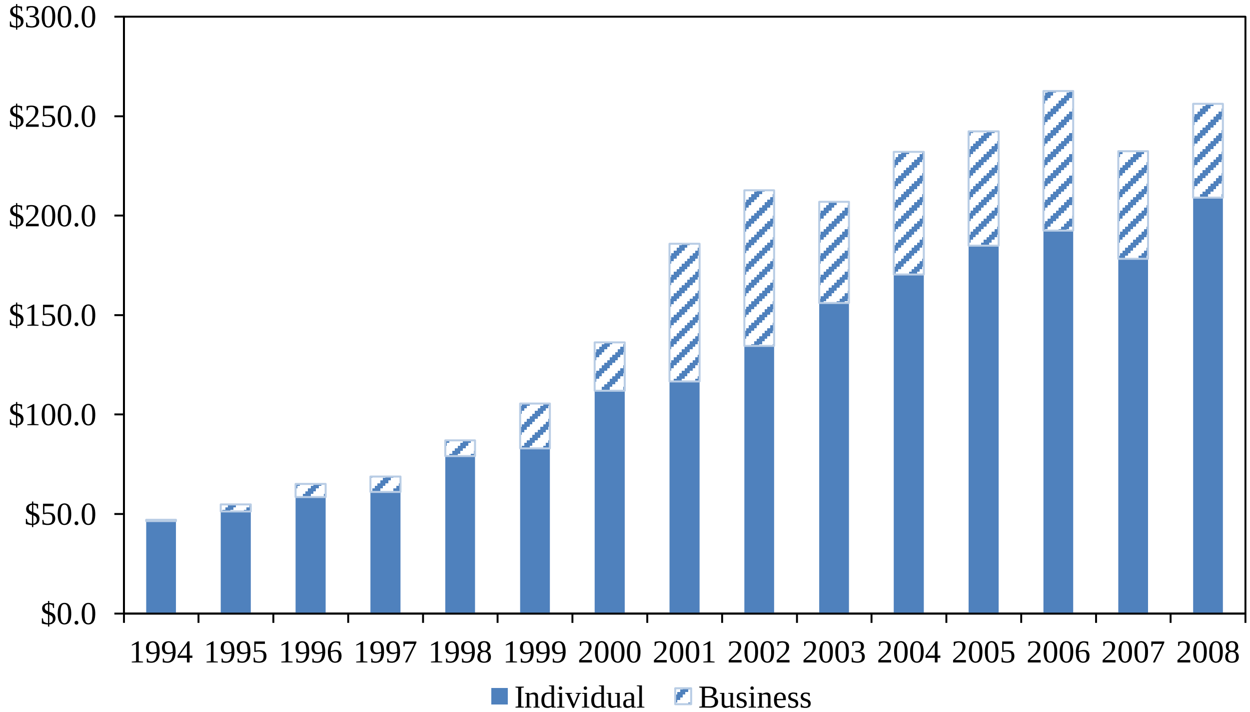
**Background:** Approximately 70 regulatory entities and activities are currently subject to periodic evaluation under the Maryland Program Evaluation Act. The Act establishes a process, known as "sunset review," as most entities evaluated are also subject to termination. The sunset review process begins with a preliminary evaluation conducted by DLS on behalf of the Legislative Policy Committee (LPC). LPC then decides whether to waive an entity from further (or full) evaluation. If waived, legislation to reauthorize the entity is typically enacted. Otherwise, a full evaluation is usually undertaken the following year. The evaluation year is typically one year before the termination date of the regulatory entity.

Although the reduction in State revenues from tax credits are generally incorporated in the State budget, most tax credits are not subject to an annual appropriation required for other State programs. Tax credits that are subject to an annual appropriation in the budget include the biotechnology investment and sustainable communities tax credits, and State reimbursement for one-half of the local property tax revenue losses 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 State Department of Assessments and Taxation reports information annually on certain property tax credit expenditures. 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.

The federal Joint Committee on Taxation (JCT) publishes annually an estimate of the cost to the federal government from special income tax provisions. JCT notes that these provisions are referred to as tax expenditures because they may be considered analogous to direct outlay programs, and the two can be considered as alternative means of accomplishing similar budget objectives. According to JCT, tax expenditure analysis can help both policymakers and the public to understand the actual size of government, the uses of government resources, and the tax and economic policy consequences that follow from the implicit or explicit choices made in fashioning legislation.

Although tax credits comprise a small percentage of total income tax revenues (less than 3% in fiscal 2009), the number and amount of credits claimed has increased over time. Prior to 1995, there was one credit primarily for individuals (the earned income credit) and two primarily business tax credits (enterprise zone and Maryland-mined coal credits). Since 1995, about 30 business credits and 10 tax credits for individuals have been established. This includes temporary and expired tax credits. 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, as shown in **Exhibit 1**. Most of this increase has been due to an increase in tax credits for individuals, and in particular earned income credits, which have increased by almost five-fold since 1994. Tax credits for businesses comprised about one-fifth of the total credits claimed in tax year 2008.

**Exhibit 1**
**Business and Individual Tax Credits**
**Tax Year 1994-2008**
**($ in Millions)**




Note: Returns processed as of January 2010. Does not include taxes paid to other states (about $200 million in tax year 2008). Amount is awarded or claimed and does reflect the impact of tax liability and carry-forwards.

Source: Comptroller's Office; Department of Legislative Services

**State Fiscal Effect:** General fund expenditures increase by $255,500 in fiscal 2013, which reflects a hiring date of January 1, 2013, for two full-time tax analysts in DLS and additional annual contracting costs for part-time employees and payments to consultants. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

| | |
|---|---|
| Positions | 2 |
| Salaries and Fringe Benefits | $46,009 |
| Equipment/Operating Expenses | 209,520 |
| **FY 2013 DLS Expenditures** | **$255,529** |

The Comptroller's Office and DBM report that any additional workload generated by the bill can be handled with existing budgeted resources.

## Additional Information

**Prior Introductions:** Similar legislation was introduced in the 2011 and 2006 sessions. HB 620 of 2011 passed the House but received an unfavorable report from the Senate Budget and Taxation Committee. HB 998 of 2006, a similar bill, received a hearing in the House Ways and Means Committee but was subsequently withdrawn.

**Cross File:** SB 739 (Senator Madaleno, *et al.*) - Budget and Taxation.

**Information Source(s):** Comptroller's Office, Department of Budget and Management, Department of Legislative Services

**Fiscal Note History:** First Reader - February 27, 2012
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