

Department of Legislative Services
 Maryland General Assembly
 2021 Session

FISCAL AND POLICY NOTE
 First Reader

House Bill 805 (Delegate Palakovich Carr)
 Ways and Means

Economic Development - Enterprise Zone Program - Alterations

This bill prohibits the Secretary of Commerce from designating a new enterprise zone or granting an expansion of an existing zone in a calendar year if the aggregate amount of property tax credits claimed under the Enterprise Zone program exceeded \$50.0 million in the prior fiscal year or may be reasonably expected to exceed \$50.0 million in the current fiscal year. Additionally, the associated income tax credit under the program applies only to individuals hired by a business entity prior to July 1, 2021. The bill also allows more flexibility in the location of new enterprise zones; generally limits the size of enterprise zone expansions; requires local governments to report to the Department of Commerce (Commerce) and the State Department of Assessments and Taxation (SDAT) each year; requires Commerce and SDAT to develop formal metrics and a framework for analyzing each enterprise zone, as specified; relieves the Comptroller from related duties and assigns those duties to SDAT; and requires Commerce to adopt related regulations. **The bill takes effect July 1, 2021, and applies to all taxable years beginning after December 31, 2020.**

Fiscal Summary

State Effect: General fund expenditures decrease by a net of \$113,800 in FY 2022, escalating to a net \$907,100 reduction in FY 2026. State revenues increase by \$500,000 in FY 2022, \$700,000 in FY 2023, and \$1.0 million annually thereafter as fewer income tax credits are claimed. Assumptions for these estimates are discussed below.

| (in dollars) | FY 2022 | FY 2023 | FY 2024 | FY 2025 | FY 2026 |
|----------------|-------------|-------------|-------------|-------------|-------------|
| GF/SF Rev. | \$500,000 | \$700,000 | \$1,000,000 | \$1,000,000 | \$1,000,000 |
| GF Expenditure | (\$113,800) | (\$315,900) | (\$513,400) | (\$710,300) | (\$907,100) |
| Net Effect | \$613,800 | \$1,015,900 | \$1,513,400 | \$1,710,300 | \$1,907,100 |

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

Local Effect: Local revenues from State reimbursement of local property tax revenue loss decrease beginning in FY 2022 as fewer enterprise zones are designated and/or expanded, offset in part by increased income tax revenues. Expenditures are likely not materially affected.

Small Business Effect: Meaningful.

Analysis

Current Law: The enterprise zone tax credit program, established in 1982, is intended to encourage economic growth within economically distressed areas of the State and to increase employment of the chronically unemployed. Businesses located within an enterprise zone are eligible for local property tax credits and State income tax credits. Real property tax credits are 10-year credits against local real property taxes on a portion of the qualifying real property improvements in the enterprise zone. The income tax credit is based on wages paid to newly hired employees and can be taken over a 1- to 3-year period. The credits are based on the wages paid during the taxable year to each qualified employee and vary in value and length of time depending on whether the employee is certified by the Maryland Department of Labor as being economically disadvantaged and if the business is located in a focus area. There are also enhanced income tax credits available for businesses that are also located in opportunity zones.

The Secretary of Commerce may designate one or more State enterprise zones within 60 days of a political subdivision's submission for an enterprise zone designation. Once approved, the enterprise zone designation is effective for 10 years. At any time, a political subdivision may reapply to the Secretary to designate another area as an enterprise zone. The Secretary of Commerce may designate annually six enterprise zones and one extraordinary expansion. A county may not receive more than two enterprise zone designations in a calendar year.

The Secretary may approve the expansion of an existing enterprise zone by up to 50% in size without the expansion counting toward the statutory limit. Pursuant to Chapter 362 of 2006, any business located in a State enterprise zone may apply for the property tax credit for an additional five years following the zone's expiration.

SDAT reimburses local governments (through the department's annual general fund budget) for 50% of the property tax revenue decrease that results from the property tax credit. There is no established limit to the amount that the State may reimburse local governments.

State Fiscal Effect:

Property Tax Reimbursements

The Governor’s proposed fiscal 2022 budget includes \$25.2 million in local property tax reimbursements, equating to \$50.4 million in aggregate property tax credits based on the existing 50% State reimbursement. Therefore, effective July 1, 2021, the Secretary of Commerce is likely prohibited from designating or expanding new enterprise zones until such time as property tax credits decrease below the allowable threshold. Accordingly, general fund expenditures for SDAT decrease, beginning as early as fiscal 2022, from what they otherwise would have been for reimbursements. While the actual amount is ultimately unknowable, based on recent growth in property tax credits, this estimate assumes general fund expenditures decrease by \$0.2 million in fiscal 2022 and by an additional \$0.2 million each year thereafter, as shown in **Exhibit 1**, so that by fiscal 2026 the reduction is \$1.0 million.

Exhibit 1
General Fund Expenditures for Property Tax Reimbursements
Fiscal 2022-2026
(\$ in Millions)

| | <u>FY 2022</u> | <u>FY 2023</u> | <u>FY 2024</u> | <u>FY 2025</u> | <u>FY 2026</u> |
|---------------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| General Fund Expenditures | (\$0.2) | (\$0.4) | (\$0.6) | (\$0.8) | (\$1.0) |

Source: Department of Legislative Services

Income Tax Credits

In recent years, an average of about \$1.0 million in income tax credits has been claimed. Credits can be taken over a one- to three-year period. Assuming the bill phases out credits over a three-year period, State revenues increase by about \$0.5 million in fiscal 2022, \$0.7 million in fiscal 2023, and \$1.0 million annually thereafter. Actual revenue increases may vary from this estimate. The amount in any year will ultimately depend on how quickly the phase-out occurs and the amount of credits that would have been claimed under current law.

Administrative Costs

Commerce can generally handle the bill’s requirements with existing budgeted resources, although the department advises that there is a significant operational impact related to analyzing each enterprise zone. The Comptroller’s Office may realize efficiencies due to having fewer duties related to enterprise zones. However, SDAT has new duties under the bill and cannot absorb them with existing staff. SDAT needs additional staff to work with Commerce, as required by the bill, in assessing the effectiveness of tax credits, developing metrics and a framework for analyzing them, receiving reports from counties, and submitting a report to the General Assembly. Accordingly, general fund expenditures increase by \$86,231 in fiscal 2022, which accounts for a 30-day start-up delay to have an administrator in place for the fall. This estimate includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses:

| | |
|--|-----------------|
| Position | 1.0 |
| Salary and Fringe Benefits | \$80,288 |
| Operating Expenses | <u>5,943</u> |
| Total FY 2022 Administrative Expenditures | \$86,231 |

Future year expenditures reflect a full salary with annual increases and employee turnover and ongoing operating expenses.

Local Fiscal Effect: Local revenues from State reimbursement of local property tax revenue loss decrease from what they otherwise would have been if more enterprise zones were designated and/or expanded. The revenue losses may be offset to a limited extent by fewer enterprise zone income tax credits being claimed. Of note, even with a State reimbursement, local governments still experience a net loss in revenue from property tax credits under the program.

In fiscal 2020, Baltimore City received 71% of all property tax reimbursements; Eastern and Western Maryland combined for 7% of reimbursements, with the balance going to the remaining central portion the State.

Local governments can likely comply with the bill’s enhanced reporting requirements with existing budgeted resources.

Small Business Effect: Small businesses that are no longer eligible to receive property and/or income tax credits under the enterprise zone program are negatively affected.

Additional Information

Prior Introductions: None.

Designated Cross File: None.

Information Source(s): Department of Commerce; State Department of Assessments and Taxation; Comptroller's Office; Anne Arundel, Charles, and Frederick counties; Department of Legislative Services

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