Legislative Performance Audit Committee

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FOR IMMEDIATE RELEASE
Contact: Senator John Harms, (402) 471-2802

December 11, 2014

LR 444 Committee recommends tax incentive evaluation process

On Thursday, the Legislature's Tax Incentive Evaluation Committee released an interim study report on Nebraska's tax incentive programs recommending a new structure for evaluation. The Committee's report recommended regular evaluation by the Unicameral's Legislative Performance Audit Committee to make sure incentive programs meet the Legislature's goals and benefit Nebraska's economy.

The Committee also recommended that leadership of the Revenue Committee participate as members of the Performance Audit Committee for the tax incentive evaluations, and that each program be evaluated at least once every three years. Evaluators will be instructed to use the metrics the Committee identified to the extent possible and, the evaluation results would be presented to the Appropriations and Revenue Committees, and at the annual Legislative Council meeting, under other recommendations.

The incentive programs reviewed by LR 444 Committee are: the Nebraska Advantage Act, the Nebraska Advantage Rural Development Act, the Nebraska Advantage Microenterprise Tax Credit Act, the Nebraska Advantage Research and Development Act, the Beginning Farmer Tax Credit Act and, the Angel Investment Credit Act.

The Tax Incentive Evaluation Committee Chairman, Senator John Harms, said of the report: "Tax incentive programs have the potential for tremendous benefit to Nebraska, but also have significant costs. The goal of this interim study was to recommend an evaluation process that allows the Legislature to understand the value of these programs and to make improvements where programs are not meeting the needs of citizens and businesses. The Committee's report creates a framework for doing just that."

The Committee's report lays out three goals for programs:

- To strengthen the state's economy over all by attracting new business to the state, expanding existing businesses, increasing employment, creating high-quality jobs, and increasing business investment
- Revitalize rural and other distressed areas of the state

- Diversify the state's economy and position Nebraska for the future by stimulating entrepreneurial, high-tech, and renewable energy firms

The Committee proposes a number specific metrics for each of these goals.

Over the course of the summer, committee members sought input from tax incentive evaluation experts, Nebraska business leaders, interested citizens, and state agencies on how to tailor an evaluation program to Nebraska's economic needs. The Committee anticipates legislation will be introduced in January as a result of the interim study report.

The Tax Incentive Evaluation Committee was created by LR 444 in response to issues raised in a February 2013 Legislative Performance Audit Committee audit of tax incentive programs. The overarching finding of the audit was that the goals expressed by the Legislature were so general that evaluators could not assess whether programs were accomplishing those goals. LR 444 tasked the committee to come up with a way to measure program success.

LR 444

Tax Incentive Evaluation Committee Report
December 2014

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Sen. Greg Adams
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Sen. Galen Hadley
Sen. Bob Krist
Sen. Heath Mello
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Acknowledgements

The Tax Incentive Evaluation Committee thanks the following individuals, agencies, and organizations for their assistance:

Robert Zahradnik and Josh Goodman of The Pew Charitable Trusts

The Nebraska Department of Revenue

The Nebraska Department of Economic Development

The Nebraska Department of Agriculture

The Committee also wishes to thank the citizens and stakeholders who participated in Committee hearings across the state for their invaluable input during the interim study.

INTRODUCTION

The Tax Incentive Evaluation Committee was created by LR 444 in response to issues raised in a February 2013 Legislative Performance Audit Committee report regarding tax incentive programs. The overarching finding of the audit was that the goals expressed by the Legislature were too general to permit a meaningful evaluation of whether programs were accomplishing those goals. LR 444 tasked the Committee to develop recommendations for:

1. Specific and measurable goals for each tax incentive program, including:
    a. the Nebraska Advantage Act
    b. the Nebraska Advantage Rural Development Act
    c. the Nebraska Advantage Microenterprise Tax Credit Act
    d. the Nebraska Advantage Research and Development Act
    e. the Beginning Farmer Tax Credit Act and,
    f. the Angel Investment Credit Act
2. A process for the regular evaluation of tax incentives, including who should conduct the evaluations, what types of measures should be used, and how often the evaluations should be conducted, and
3. Proposed legislation to put requirements for ongoing evaluations in statute

In addition, the Committee established that its intention was to consider systematic evaluation of tax incentive programs in order to improve their effectiveness, not to eliminate the programs.

In an effort to ensure that recommendations would be educated and informed by experience of other successful states, the Committee reached out to evaluation experts at The Pew Charitable Trusts. The Pew experts presented the Committee with a proposal that included principles and recommendations for Nebraska's tax incentive evaluation process[1]. In the report the Pew experts identified six key issues that the Committee should address for a successful evaluation process:

Key Issues identified by Pew Charitable Trusts

1. Design a strategic evaluation schedule
2. Identify metrics
3. Collect and assess relevant data
4. Determine what office should conduct the evaluation
5. Measure the economic impact with and without economic models
6. Ensure the evaluations inform the policy process

[1] The Pew Report is available on the LR 444 Committee's website and at the Legislative Audit Office.

These key issues were the foundation for the Committee's work on LR 444. The Committee also held several open meetings and two public hearings to seek input from citizens and stakeholders, including Chambers of Commerce and policy-oriented groups across the state.

RECOMMENDATIONS

The Evaluation Process

The Committee makes six recommendations with regard to the evaluation process:

1. The Legislative Audit Office should perform evaluations with assistance from the Legislative Fiscal Office and state agencies as necessary. To ensure adequate expertise and staffing, the Audit Office will need to add another position dedicated primarily to tax incentive evaluations.
2. For the purposes of the tax incentive evaluations, the Performance Audit Committee should include in its deliberations the Chair of the Revenue Committee, or a designee, and one other member of the Revenue Committee, as determined by the Revenue Committee, as ex officio non-voting members. The evaluation process will not alter the jurisdiction of the Revenue Committee with regard to tax incentive program legislation.
3. Incentive programs should be evaluated on a 3 year cycle, on a schedule determined by the Audit Office. If a bill is passed in 2015 the first evaluation should be completed in late 2016.
    - The Legislative Audit Office should begin an analysis of necessary, relevant, and available data as soon as possible and should identify any potential legislation essential to ensuring that necessary data is available to evaluators.
    - The Audit Office should work with the Fiscal Office to determine where economic modeling is necessary and craft a plan to incorporate economic modeling into evaluations. This plan should include costs and staffing required to develop modeling capabilities within the Legislature.
4. Legislation introduced as a result of LR 444 should instruct evaluators to utilize this Committee's metric recommendations to the extent practicable for individual incentive programs.
5. Upon completion of an evaluation, evaluators should conduct a briefing for members of the Appropriations and Revenue Committees. Evaluation information should also be presented at the annual meeting of the Legislative Council.
6. The Legislative Audit Office staff should work with Bill Drafting to begin drafting tax incentive evaluation legislation based on the recommendations in this report.

Goals and Metrics

The Committee identified three overarching goals representing the range of policy priorities reflected in Nebraska's tax incentive programs.

1. To strengthen the state's economy over all by attracting new business to the state, expanding existing businesses, increasing employment, creating high-quality jobs, and increasing business investment
2. Revitalize rural and other distressed areas of the state
3. Diversify the state's economy and position Nebraska for the future by stimulating entrepreneurial, high-tech, and renewable energy firms

For each goal the Committee selected several metrics to measure whether goals are being met. Goals and metrics are intended to address the broader issues that inform the effectiveness of incentive programs. Some metrics will be more appropriate for evaluation of specific programs than others.

Goal 1: To strengthen the state's economy over all by attracting new business to the state, expanding existing businesses, increasing employment, creating high-quality jobs, and increasing business investment

Metric 1: How many net new full time jobs did the incentivized company create during the time period?

Discussion: Current statutes require the Department of Revenue to report full-time equivalent positions created for some incentive programs. This metric would measure the actual new positions that did not exist before the incentive, with adjustments for positive and negative employment impacts on non-incentivized businesses. Evaluators should also include an examination of indirect, and induced jobs while adjusting for displacement, opportunity cost, and timing.

Metric 2: What percentage of workers hired to incentivized jobs filed unemployment claims within two years after being hired?

Metric 3: What percentage of workers hired to incentivized jobs filed unemployment claims before beginning employment in the incentivized position?

Metric 4: How much job-creation related tax benefit (in dollars) did an incentivized company receive for each new full-time job it created during the period?

Discussion: Evaluators should seek to ensure that the time period selected for this analysis is sufficient to address the long term nature of job growth created by incentives. Because costs and benefits of tax incentives do not always occur immediately or simultaneously, evaluators should be wary of selecting a time period that is too short to provide accurate findings.

Metric 5: How much state revenue did the creation of an incentivized job generate?

Metric 6: Did incentivized companies create more or fewer full-time jobs during a certain time period than would likely have been created under alternative policies, including, but not limited to elimination of the corporate income tax, investments in education funding, and investments in roads and other infrastructure.

Metric 7: How many jobs were created by incentives as compared to job growth in non-incentivized companies?

Metric 8: How much did an incentivized company invest in selected business expenditure categories during a specific time period?

Metric 9: Were the average wages at incentivized companies higher or lower than the average wages of 1) all jobs in the county/counties in which the incentivized company's project was located and 2) all state jobs in the same industry during a specific period of time?

Metric 10: How much did an incentivized company pay for health insurance benefits for each new full-time job it created during a specific time period?

Metric 11: How much did an incentivized company pay for other benefits (such as paid leave, retirement, etc.) for each new full-time job it created during a specific time period?

Metric 12: How does the total cost of the incentives (tax revenue forgone) compare to the total benefit of the incentives (tax revenue increased)?

Discussion: The committee cautions future legislators and evaluators to be wary of using this metric as the sole mechanism for determining if tax incentive programs are effective. During the interim study process, the committee had discussions with the Pew experts about the importance of treating this metric as one indicator among many.

Metric 13: What is the dollar cost of administering each incentive program (or all of the programs administered by one agency), including costs for 1) promotion 2) the application process 3) auditing/verification and 4) reporting?

Metric 14: What is the cost to businesses to apply for and comply with requirements of incentive programs?

Goal 2: Revitalize rural and other distressed areas of the state

Metric 15: Do incentivized companies create more new full-time jobs in areas of the state identified in statute as “distressed” or in non-distressed areas? (See attached report for statutory definitions of “distressed”.)

Metric 16: What proportion of people who live in distressed areas of the state have the level of education needed to fill job vacancies in their area? How many of the incentivized jobs do not require a bachelor’s degree?

Goal 3: Diversify the state’s economy and position Nebraska for the future by stimulating entrepreneurial, high-tech, and renewable energy firms

Metric 17: For each calendar year, to what extent did businesses receiving incentives increase their patent production or engage in other activities that may be indicators of innovation, compared to companies that did not receive incentives?

Metric 18: Did companies participating in incentive programs receive financing from other sources as a result of the incentive benefits?

Metric 19: Do companies that receive incentives remain in business in Nebraska longer than companies that do not receive incentives?

Key Points for Legislation

1. Legislation should require Audit Office evaluation of each state tax incentive programs at least once every 3 years.
2. Legislation should modify sunset dates for the Advantage Act and the Advantage Research and Development Act to ensure that sunsets are consistent with the evaluation schedule.
3. Legislation should instruct evaluators to utilize this Committee’s metric recommendations to the extent practicable for individual incentive programs.
4. Legislation should include any statutory changes necessary to ensure relevant data is available to evaluators.
5. While not including exact details of the specific metrics recommended by this Committee, legislation should include language that clearly communicates the Legislature’s expectations for evaluations.
6. Legislation should modify the Legislative Performance Audit Act to include in the deliberations of the Legislative Performance Audit Committee the Chairperson of the Revenue Committee or a designee and one member of the Revenue Committee as selected by the Revenue Committee as ex officio non-voting members when the Committee considers tax incentive evaluations.

To: Legislative Performance Audit

From: Keisha Patent, Legal Counsel
Legislative Research Office

Re: Location definitions for tax incentive programs

Date: September 25, 2014

Included in this document are the definitions of “rural” and “distressed” in Nebraska tax incentive programs and some other examples of how these terms are defined at the federal level and in other states. Supporting documentation is attached, including maps for the relevant programs, which limit applications by geographic location. In addition, pdf or link files for the accompanying maps will be emailed to you.

Nebraska Advantage Rural Development Act

Neb. Rev. Stat. sec. 77-27,188 authorizes a tax credit pursuant to the Nebraska Advantage Rural Development Act for taxpayers who meet the investment and employment requirements in the following rural locations:

- Level 1 projects
    A. Any county in this state with a population of fewer than fifteen thousand inhabitants, according to the most recent federal decennial census,
    B. Any village in this state,
    C. Any area within the corporate limits of a city of the metropolitan class consisting of one or more contiguous census tracts, as determined by the most recent federal decennial census, which contain a percentage of persons below the poverty line of greater than thirty percent, and all census tracts contiguous to such tract or tracts; or
- Level 2 projects (with different investment and employment requirements) in any county in this state with a population or less than twenty-five thousand inhabitants, according to the most recent federal decennial census, or any city of the second class.

Specifically, the following are considered qualified locations by the Department of Revenue for purposes of the Nebraska Advantage Rural Development Act:

- Level 1 projects
  - Locations within all counties, except Adams, Buffalo, Cass, Dakota, Dawson, Dodge, Douglas, Gage, Hall, Lancaster, Lincoln, Madison, Otoe, Platte, Sarpy, Saunders, Seward, Scotts Bluff, and Washington counties;
  - Locations within the following villages:
    - Adams, Alda, Alvo, Amherst, Arlingston, Avoca, Ayr, Barneston, Beaver Crossing, Bee, Bennet, Boys Town, Brady, Burr, Cairo, Cedar Bluffs, Cedar Creek, Ceresco, Clatonia, Colon, Cordova, Cornlea, Cortland, Creston, Davey, Denton, Dodge, Douglas, Dunbar, Duncan, Eagle, Eddyville, Elm Creek, Elmwood, Emerson, Farnam, Filley Firth, Garland, Goehner, Greenwood, Hallam, Henry, Herman, Hershey, Holstein, Homer, Hubbard, Inglewood, Ithaca, Jackson, Juniata, Kenesaw, Kennard, Leshara, Liberty, Lindsay, Lorton, Lyman, Malcolm, Malmo, Manley, Maxwell, McGrew, Mead, Meadow Grove, Melbeta, Memphis, Miller, Monroe, Morrill, Morse Bluff, Murdock, Murray, Nehawka, Nickerson, Odell, Otoe, Overton, Palmyra, Panama, Pickrell, Platte Center, Pleasant Dale, Pleasanton, Prague, Prosser, Raymond, Riverdale, Roca, Roseland, Shelton, Snyder, South Bend, Sprague, Staplehurst, Sumner, Sutherland, Talmage, Tarnov, Uehling, Unadilla, Union, Valparaiso, Virginia, Wallace, Washington, Wellfleet, Weston, and Winslow.
  - Locations within the following census tracts in the Omaha metropolitan area:
    - 2, 3, 4, 5, 6, 7, 8, 11, 12, 16, 18, 19, 20, 21, 23, 24, 25, 28, 29, 30, 31, 32, 33, 34.01, 34.02, 35, 36, 37, 38, 39, 40, 42, 43, 45, 46, 47, 48, 49, 50, 51, 52, 53, 54, 55, 58, 59.01, 59.02, 60, 61.01, 61.02, 62.02, 63.01, 63.02, 68.06, 69.06, 70.01, 70.02, 70.03, 73.04 in Douglas Co., and
    - 101.07, 101.08, 105.01 in Sarpy Co.
- Level 2 projects
  - Locations within all counties, except Adams, Buffalo, Cass, Dodge, Douglas, Hall, Lancaster, Lincoln, Madison, Platte, Sarpy, and Scotts Bluff.
  - Locations within the following second class cities:
    - Battle Creek, Bennington, Blue Springs, Doniphan, Gibbon, Gretna, Hickman, Hooper, Humphrey, Louisville, Madison, Minatare, Mitchell, Newman Grove, North Bend, Ravenna, Scribner, Springfield, Terrytown, Tilden, Valley, Waterloo, Waverly, Weeping Water, and Wood River.
- Livestock modernization projects may be in any county in the state.

Maps for Level I and Level II projects were developed by the Department of Economic Development and are attached to this memorandum.

Nebraska Microenterprise Act

Neb. Rev. Stat. sec. 77-5903 defines “distressed area” for purposes of tax credits pursuant to the Nebraska Microenterprise Act as a municipality, county, unincorporated area within a county, or census tract in Nebraska that has (a) an unemployment rate which exceeds the statewide average unemployment rate, (b) a per capita income below the statewide average per capita income, or (c) had a population decrease between the two most recent federal decennial censuses.

Specifically, the following are considered qualified locations by the Department of Revenue for purposes of the Nebraska Microenterprise Act:

- Locations in all counties, except census tracts 9549 and 9550 in Cheyenne County and census tracts 502.01 (outside of the village of Kennard) and 502.02 in Washington County.

Maps for eligible areas for 2014 and proposed areas for 2015 were developed by the Department of Economic Development and are attached to this memorandum.

Angel Investment Act

Neb. Rev. Stat. sec. 77-6302 defines “distressed area” for purposes of tax credits pursuant to the Nebraska Angel Investment Act as a municipality, county with a population of fewer than one hundred thousand inhabitants according to the most recent decennial census, unincorporated area within a county, or census tract in Nebraska that has (a) an unemployment rate which exceeds the statewide average unemployment rate, (b) a per capita income below the statewide average per capita income, or (c) had a population decrease between the two most recent federal decennial censuses.

Specifically, the following are considered qualified locations by the Department of Revenue for purposes of the Nebraska Microenterprise Act:

- All counties, except certain census tracts in Cheyenne, Douglas, Lancaster, Lincoln, and Sarpy counties.

A map for the eligible locations under the act was developed by the Department of Economic development and is attached to this memorandum.

Other Nebraska Tax Incentive Programs

The Nebraska Advantage Act, the Nebraska Advantage Research and Development Act, and the Beginning Farmer Tax Credit Act do not limit applications by geographic area of the state in which the taxpayer lives by statute or regulation. Therefore, anyone in the state can apply so long as the other conditions for qualifying for the tax credit are met.

Definitions of Rural

Throughout Nebraska's statutes, "rural" is defined in different ways. In a statute governing critical access hospitals, "rural" is defined as any county with a population of less than 100,000 residents. In statutes related to electric utilities, "rural" means any area not within the boundaries of any incorporated city, town, or village.

Federally, both the U.S. Census Bureau and the Office of Management and Budget (OMB) define rural, albeit in different ways. The Census Bureau uses population size and density in determining which areas are rural. Based upon the 2010 decennial census, rural areas are considered to be open country with population density of less than 500 people per square mile and settlements with fewer than 2,500 inhabitants. OMB identifies counties as metropolitan, micropolitan, and nonmetropolitan based on population. The two agency definitions result in different areas being considered rural.

Definitions vary from state to state in their tax incentive programs as well. The following are some examples:

- Arizona Jobs Training Program defines "rural" as counties with a population of less than 750,000 and municipalities of less than 50,000 within counties of more than 750,000.
- Missouri Quality Jobs program defines "rural" as a county with a population of less than 75,000 or that does not contain an individual city with a population greater than 50,000.
- New Mexico Rural Jobs Tax Credit defines "rural" as any part of the state except Los Alamos County and certain municipalities (Albuquerque, Rio Rancho, Farmington, Las Cruces, Roswell, and Santa Fe) and the 10 mile zone around those municipalities.
- Florida Economic Development Initiative defines "rural" as (1) a county with a population of 75,000 or fewer, (2) a county with a population of 125,000 or fewer which is contiguous to a county with a population of 75,000 or fewer, a municipality within a county described in subparagraph 1. or subparagraph 2, or (4) an unincorporated federal enterprise community or an incorporated rural city with a population of 25,000 or fewer and an employment base focused on traditional agricultural or resource-based industries, located in a county not defined as rural, which has at least three or more of the economic distress factors verified by the department.

Definitions of Distressed

Nebraska statutes define distressed for purposes of the Business Innovation Act as well as the tax incentive programs. In the Business Innovation Act, distressed is defined as it is in the Angel Investment Act.

Similarly to definitions of rural, state definitions of distressed vary. The following are a few examples:

- Mississippi Job Tax Credit defines “economically distressed community” as an area within a municipality that contains groupings of census tracts that include and are contiguous to the central business district, where within such census tract groupings at least thirty percent (30%) of the residents have incomes that are less than the national poverty level as published by the United States Bureau of the Census in the most recent decennial census for which data is available; in which the unemployment rate is at least one and one-half (1- 1/2) times greater than the national average, as determined by the most recent data from the United States Bureau of Labor Statistics, including estimates of unemployment developed using the calculation method of the United States Bureau of Labor Statistics Census Share.
- Florida Economic Development Initiative defines “economic distress” as conditions affecting the fiscal and economic viability of a rural community, including such factors as low per capita income, low per capita taxable values, high unemployment, high underemployment, low weekly earned wages compared to the state average, low housing values compared to the state average, high percentages of the population receiving public assistance, high poverty levels compared to the state average, and a lack of year-round stable employment opportunities.

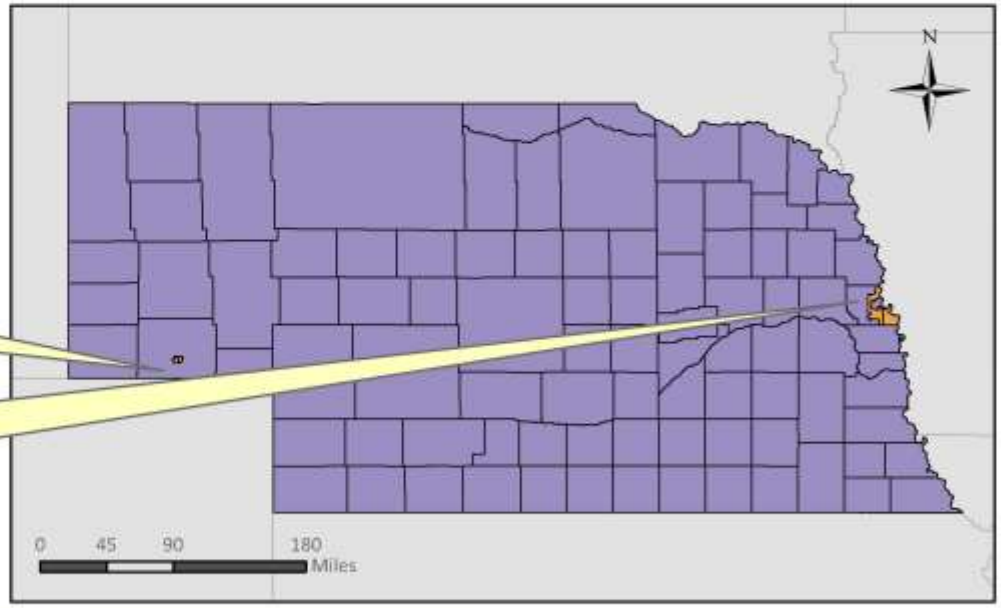
I hope you find this helpful. If you have any questions, please let me know.

Nebraska Advantage Microenterprise Tax Credit: Qualified Locations

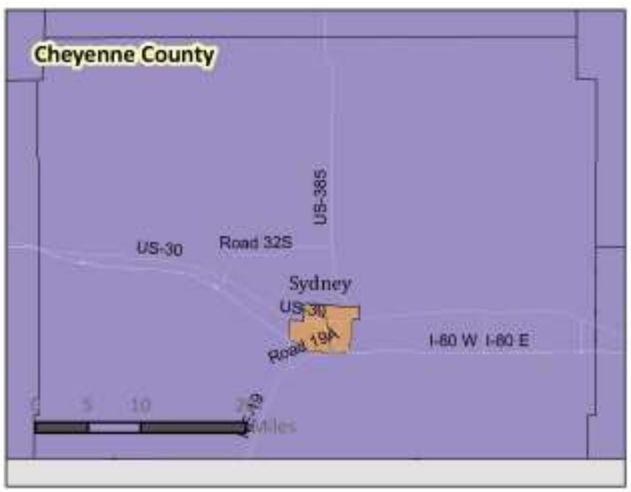
Qualified Locations - For applications filed on or **after January 1, 2014**, all Nebraska counties are eligible areas **EXCEPT** portions of Cheyenne County and Washington County.

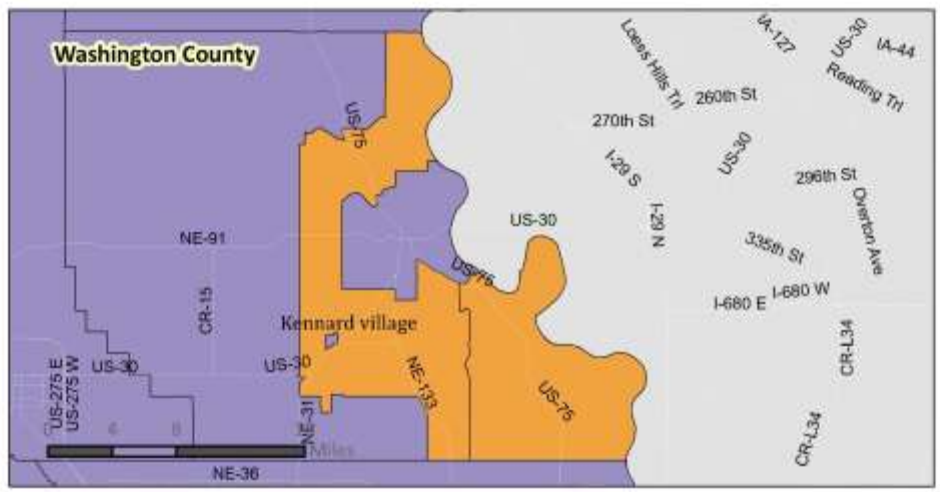
In **Cheyenne County**, Census Tracts 9549 and 9550 are not eligible.

In **Washington County** Census Tracts 502.01 and 502.02 are not eligible, with one exception: In Census Tract 502.01, any area within the village of Kennard is eligible.

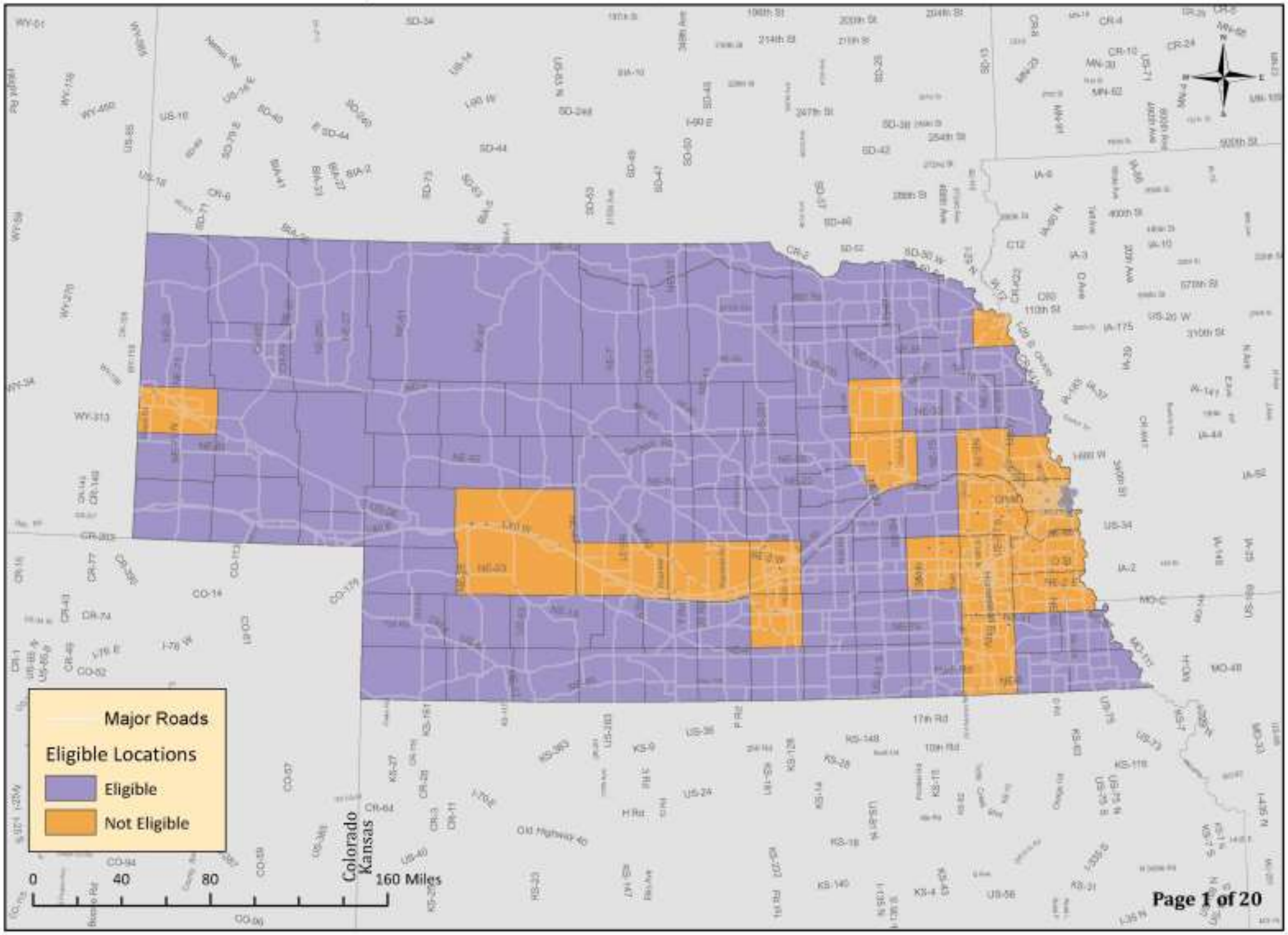


Elegible   Not Elegible

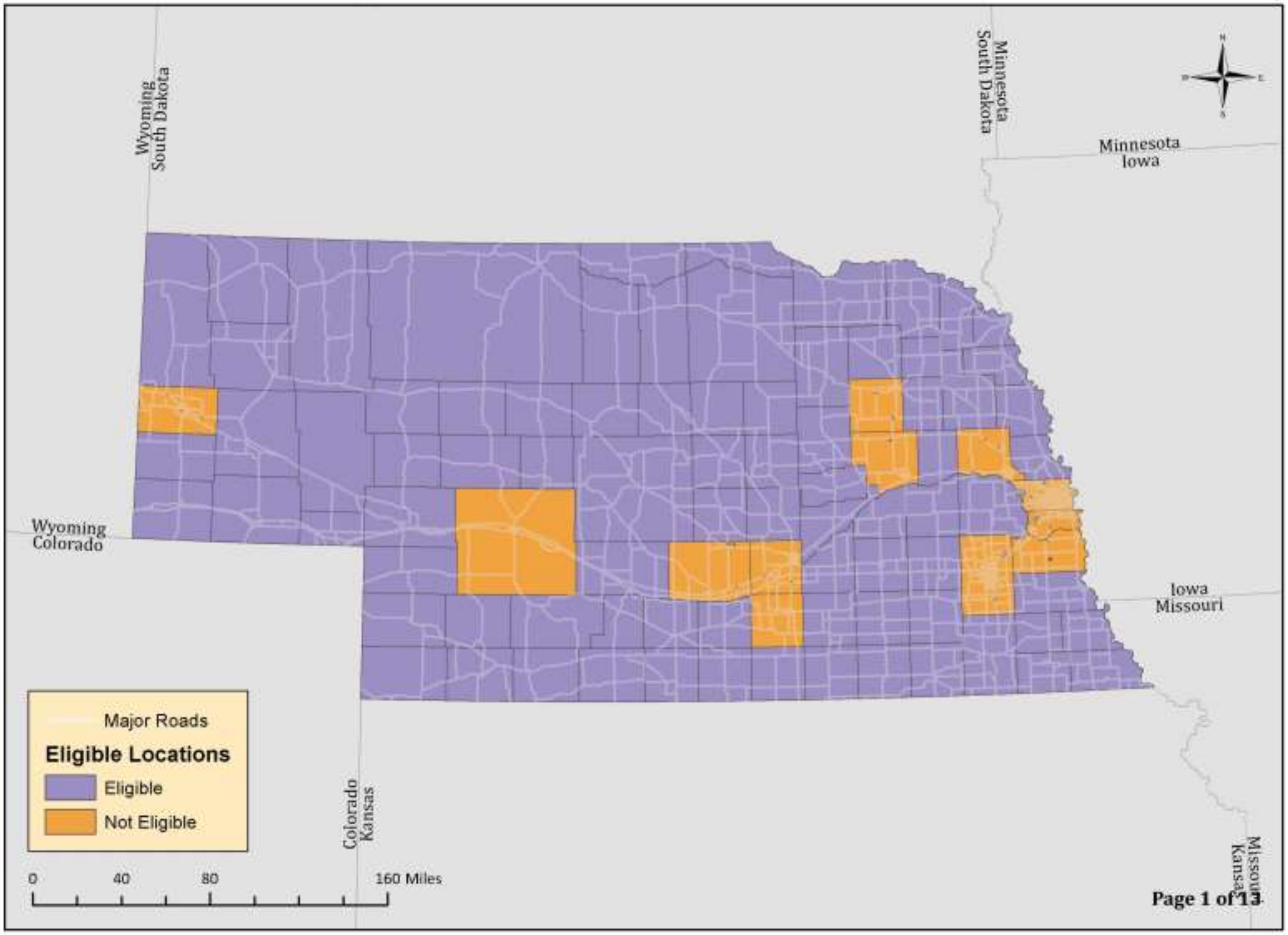




Nebraska Rural Development Act Level I Qualified Locations in Nebraska



Nebraska Rural Development Act Level II Qualified Locations in Nebraska



Nebraska Angel Investment Tax Credit Act: 2014 Qualified Locations

Qualified Locations - For applications filed on or **after January 1, 2014**, all Nebraska counties are eligible areas **EXCEPT** portions of Cheyenne County and Washington County.

In **Cheyenne County**, Census Tracts 9549 and 9550 are not eligible.

In **Washington County** Census Tracts 502.01 and 502.02 are not eligible, with one exception: In Census Tract 502.01, any area within the village of Kennard is eligible.

Elegible   Not Elegible