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| PROPOSED MASSACHUSETTS TAX EXPENDITURES  EVALUATION SUMMARY |
| EVALUATION YEAR: 2020 |

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| **TAX EXPENDITURE TITLE** | Economic Development Incentive Program Credit (formerly referred to as Economic Opportunity Area Credit) |
| **TAX EXPENDITURE NUMBER** | 1.603 and 2.605 |
| **TAX EXPENDITURE CATEGORY** | Credit against tax *(personal income tax, corporate and business tax)* |
| **TAX TYPE** | Corporate and business excise, personal income tax |
| **LEGAL REFERENCE** | M.G.L. c. 63, § 38N; c. 62, § 6(g) |
| **YEAR ENACTED** | 1993 |
| **REPEAL/EXPIRATION DATE** | None |
| **ANNUAL REVENUE IMPACT** | Annual tax loss of $15.8 - $16.0 million from corporate and business tax filers and $3.5 - $3.7 million from personal income tax filers during FY18-FY22 |
| **NUMBER OF TAXPAYERS** | 131 claims from corporate and business tax filers, and 30 claims from personal income tax filers (tax year 2017) |
| **AVERAGE TAXPAYER BENEFIT** | About $103,900 per claim (tax year 2017) |

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| **Description of the Tax Expenditure:**  Under the provisions of the Economic Development Incentive Program (EDIP), the Economic Assistance Coordinating Council (EACC) may authorize taxpayers participating in certified projects to claim tax credits. To be eligible, a project must be certified by the EACC. The total dollar amount of the EDIP credit that may be authorized in a calendar year is $30 million. | **Is the purpose defined in the statute?**  The statute does not explicitly state the purpose of this tax expenditure. |
| **What are the policy goals of the expenditure?**  To provide incentives to invest in new or expanded business ventures in Massachusetts by awarding tax credits for such investments, thereby reducing the cost of capital and spurring economic growth. | **Are there other states with a similar Tax Expenditure?** |

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|  |
| Conclusion/Recommendations: [To be Entered by TERC] |

**INTRODUCTION**

Under the Economic Development Incentive Program (EDIP), the Economic Assistance Coordinating Council (EACC) may award tax credits to taxpayers that participate in a “certified project” (as defined in G.L. c. 23A, §§ 3A and 3F). The amount of credit allowed in each case is determined by the EACC based on numerous factors set forth in G.L. c. 23A, § 3D, including the number of jobs expected to be created, the amount of capital to be invested, and the net new economic benefit expected to be created. The EACC may designate the credit as refundable for any certified project, subject to a limitation that the EACC may not award more than $5 million in refundable credits per year.

Unless designated as refundable, the maximum amount of credit allowed in any one taxable year cannot exceed fifty percent of the excise due for the taxable year. The amount of credit allowed cannot reduce the excise below the minimum excise. The EACC is authorized to eliminate or limit carry-over of the credit. The EDIP credits used in a calendar year are subject to an annual cap of $30 million. Recapture is required if the EACC revokes a business project certification.

The credit is not transferable; however, if a certified project is sold or otherwise disposed of, the credit allowed may be transferred to the purchaser of the certified project, provided that the EDIP contract is assigned to and assumed by the purchaser and approved in writing by the EACC.

When it was first enacted in 1993, the credit was for a fixed 5 percent of the costs of qualifying tangible property, and the project had to be located in a designated “economic opportunity area”. In 2010, the statute was amended to increase the percentage to “up to 10 percent” and “up to a refundable forty percent” in some cases, eliminate the “economic opportunity area” requirement and impose an annual cap of $25 million. As of 2017, the credit is whatever amount is awarded by the EACC as part of the certification process.

**POLICY GOALS**

The statute does not explicitly state the purpose of this tax expenditure. However, the credit is designed to provide incentives to invest in new or expanded business ventures in Massachusetts. Credits for such investments reduce the cost of capital, thus spurring economic growth. The credit is a key component of the Economic Development Incentive Program created under G.L. c. 23A and administered by the Massachusetts Office of Business Development(“MOBD”). In its fiscal year 2020 annual report[[1]](#footnote-2), MOBD states that it has 4 missions, which are to “facilitate access to resources”, “promote job growth and job retention”, “stimulate private investments”, and “help businesses thrive in Massachusetts”.

**DIRECT COSTS**

The revenue loss resulting from this tax expenditure is estimated to be $15.8 - $16.0 million per year from corporate and business tax filers and $3.5 - $3.7 million per year from personal income tax filers during FY18-FY22. See Table 1. The estimates are based on several factors, including historical claims, economic forecasts, and related law changes.

**Table 1. Tax Revenue Loss Estimates for EDIP Credit**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Fiscal Year | | 2018 | 2019 | 2020 | 2021 | 2022 |
| Estimated Revenue Loss ($Million) | Corporate excise | $15.8 | $15.9 | $15.9 | $16.0 | $16.0 |
| Personal Income tax | $3.5 | $3.6 | $3.6 | $3.7 | $3.7 |
| Total | $19.3 | $19.4 | $19.5 | $19.6 | $19.8 |

Table 2 below shows the amount and number of available, claimed, and shared credits in each year during the period 2015 through 2018. “Available credit” refers to the maximum amount of credit that a taxpayer can claim based on tax liability, provided there are no other restrictions. “Claimed credit” is the amount a taxpayer actually claimed. “Shared credit” is the amount of a taxpayer’s credit that was used by other members of the taxpayer’s combined group. “Count” refers to the number of credit claims.

There were 96 -173 claims per year from corporate and business tax filers, and 6 – 156 claims per year from the personal income tax filers during the tax years 2015 through 2018. The average claimed or shared amount varied from $85,600 in 2015 to $120,200 in 2018. It is unknown why the number of claims from personal income tax filers decreased from 156 in 2015 to 30 in 2017, and 6 in 2018. Please also note that the actual claimed or shared amounts of the credit were close to or significantly under 50% of the amounts of credits available. That means that tax filers did not have enough tax liabilities to take full advantage of the credit or certain statutory limitations[[2]](#footnote-3) prevented them from doing so.

**Table 2. Amount and Count of EDIP Credit by Tax Year**

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Calendar Year | | 2015 | | 2016 | | 2017 | | 2018 | |
| Amount ($000) | Count | Amount ($000) | Count | Amount ($000) | Count | Amount ($000) | Count |
| Corporate Business Tax | Available Credit - A | $114,070 | 369 | $107,463 | 322 | $62,063 | 289 | $23,191 | 202 |
| Claimed Credit | $22,025 | 157 | $20,716 | 113 | $11,921 | 111 | $10,050 | 85 |
| Shared Credit | $2,709 | 16 | $3,515 | 14 | $2,793 | 20 | $1,384 | 11 |
| Claimed plus Shared Credit - B | $24,734 | 173 | $24,230 | 127 | $14,714 | 131 | $11,434 | 96 |
| B/A | 21.7% | 46.9% | 22.5% | 39.4% | $23.7% | 45.3% | 49.3% | 47.5% |
| Personal Income Tax | Claimed Credit | $3,438 | 156 | $1,357 | 90 | $2,019 | 30 | $828 | 6 |
| All | Claimed plus Shared Credit | $28,173 | 329 | $25,587 | 217 | $16,733 | 161 | $12,262 | 102 |
| Average Claimed or Shared Amount | $85.6 | NA | $117.9 | NA | $103.9 | NA | $120.2 | NA |

Source: Massachusetts Department of Revenue.

Notes: 1. 2017 and 2018 data are preliminary and subject to change.

2. The count is the number of claims, not the number of claimants. The number of claims is either the same as or

slightly larger than the number of claimants.

3. “NA” means not applicable.

Note that, though the annual cap for the credit is $30 million, the actual claimed amounts for the credit have been lower than the cap and have varied by year. See Appendix I.

**DIRECT BENEFITS**

Tables 3 and 4 present statistics for corporate and business tax filers who claimed the credit in 2017, excluding insurance tax filers and personal income tax filers who claimed the credit. [[3]](#footnote-4)

In tax year 2017, there were about 117 claimants that were corporations.[[4]](#footnote-5) About 36.8% of them were corporations with taxable income greater than $0 but less than $10,000, and 49.6% of them were corporations with fewer than 100 employees. The average tax benefit per claimant was $108,665 for all corporations, $218,727 for the corporations with taxable income greater than $0 but less than $10,000 (highest among all income groups), and $181,439 for the corporations with 100-199 employees (highest among all employment level groups).

**Table 3. 2017 EDIP Credit Claims by Taxable Income Level**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Taxable Income Range | Tax Liability after Credit ($000) | Claimed Credit ($000) | Shared Credit ($000) | Number of Claimants | *% of Total Number of Claimants* | Tax Saving Per Claimant ($) |
| Less than $0 | $160 | $152 | $57 | 13 | *11.1%* | $16,087 |
| $0 to $9,999 | $209 | $6,892 | $2,513 | 43 | *36.8%* | $218,727 |
| $10,000 to $99,999 | $22 | $86 | $0 | 8 | *6.8%* | $10,742 |
| $100,000 to $999,999 | $167 | $744 | $0 | 12 | *10.3%* | $62,026 |
| $1,000,000 to $9,999,999 | $3,469 | $1,592 | $222 | 36 | *30.8%* | $50,409 |
| $10,000,000 or more | $7,264 | $454 | $0 | 5 | *4.3%* | $90,881 |
| Total or average | $11,291 | $9,921 | $2,793 | 117 | *100.0%* | $108,665 |

Source: Massachusetts Department of Revenue (2017 corporate excise return data)

Notes: 1. Personal income tax filers and insurance tax filers were excluded from this table.

2. The data are preliminary and subject to change.

**Table 4. 2017 EDIP Credit Claims by Taxpayer Size (Number of Employees)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Employees Range\* | Tax Liability after Credit ($000) | Claimed Credit ($000) | Shared Credit ($000) | Number of Claimants | *% of Total Number of Claimants* | Tax Saving Per Claimant ($) |
| Less than 5 | $307 | $2,019 | $257 | 15 | *12.8%* | $151,728 |
| 5 to 49 | $1,353 | $426 | $18 | 18 | *15.4%* | $24,686 |
| 50 to 99 | $363 | $265 | $ | 25 | *21.4%* | $10,589 |
| 100 to 199 | $1,740 | $2,896 | $370 | 18 | *15.4%* | $181,439 |
| 200 to 499 | $682 | $1,278 | $105 | 10 | *8.6%* | $138,340 |
| 500 or more | $6,845 | $3,037 | $2,043 | 31 | *26.5%* | $163,854 |
| Total or average | $11,291 | $9,921 | $2,793 | 117 | 100.0% | $108,665 |

Source: Massachusetts Department of Revenue (2017 corporate excise return data)

Notes: 1. \* Information is based on number of employees as reported by taxpayers.

2. Personal income tax filers and insurance tax filers were excluded from this table.

3. The data are preliminary and subject to a slight revision later.

On the other hand, according to the EDIP Fiscal Year 2020 Annual Report,[[5]](#footnote-6) in the fiscal year 2020, there were 23 projects approved, 2,854 jobs to be created, 1,386 jobs to be retained, $900 million in private investment, and $1.695 million EDIP credit awarded. Of the 23 projects approved, 5 projects were for manufacturers, 12 projects were located in gateway cities, and 11 projects were for small businesses with fewer than 200 employees. A key criterion that EACC uses in approving a project and corresponding credit is whether the project would not occur “but for” the EDIP tax credit incentive. For this purpose, EACC considers answers to questions including “Is property already purchased?”, “Is lease already signed?”, “Has news article appeared on front page of local paper?”, “Has a groundbreaking ceremony been held?”, “Is equipment already placed on order?”, “Has a public announcement been made?”, and “Has construction begun?”.

To better understand the numbers in MOBD’s annual reports as related to this evaluation report, we should note that: (1) According to MOBD, when applying for the EDIP credit, companies commit to creating certain number of jobs over several number of years. Hence, the numbers are cumulative. (2) More importantly, although EACC uses the “but for” criterion to choose projects, there is still possibility that some of the money the companies invest in the EDIP projects could have been invested in other projects in Massachusetts even if the tax incentive had not existed, because investors would not let their money sit idle. Or in other words, the investments in EDIP projects are not necessarily all “net new” investment to Massachusetts. They could be shift from other parts of Massachusetts or shift from future investments. (3) Some of committed investments and job creation/retention might not actually be realized due to changes in situation later. (4) EDIP program has components other than the credit though the latter is the key component.

**EVALUATION: COMPARING COSTS AND BENEFITS**

In the previous sections, we report the direct costs (to the Commonwealth, or to the residents and businesses who ultimately bear the costs when the Commonwealth cuts government spending or increases tax to finance the EDIP credit) and direct benefits (to taxpayers who claim the credit) of this tax expenditure. Since the direct costs to the Commonwealth are the direct benefits to taxpayers, they are equal.

However, when looking at the broader economy, there are, in addition to direct impacts, indirect and induced impacts on other residents and businesses in Massachusetts. See appendix II for more discussion.

To determine the net impact of the tax expenditure, i.e., the total benefits (including direct, indirect and induced benefits) offset by the total costs (including direct, indirect and induced costs), we employed the model of “Tax-PI” developed by Regional Economic Models Incorporated (“REMI”).[[6]](#footnote-7) See appendix II for details.

The estimated net impact of the tax expenditure for fiscal years 2018 through 2022 are shown in Tables 5 and 6. As shown, the EDIP credit combined with an assumed corresponding cut in state government spending results in less economic activity in general, with real state GDP changing by -$21 million to +$3 million. The net impact on total employment is negative, decreasing by 80 – 274 jobs annually. The net additional impact on state revenues[[7]](#footnote-8) is also negative, decreasing by $0.1 million to $0.7 million annually.

**Table 5. Net Additional Revenue Impact of EDIP Credit\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Fiscal Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Net additional revenue impact ($000) | -$388 | -$694 | -$494 | -$308 | -$137 |

\* assuming state government spending is cut by the same amount as the revenue loss due to EDIP credit to balance budget.

**Table 6. Net Economic Impacts of EDIP Credit by Selected Economic Measure\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Calendar Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Impact on total employment | -274 | -206 | -156 | -112 | -80 |
| Impact on private non-farm employment | -54 | 10 | 51 | 85 | 106 |
| Impact on GDP ($000), real dollars (2012) | -$21,000 | -$13,000 | -$7,000 | -$1,000 | $3,000 |
| Impact on personal income ($000) | -$20,000 | -$16,000 | -$14,000 | -$10,000 | -$7,000 |

\* assuming state government spending is cut by the same amount as the revenue loss due to EDIP credit to balance budget.

Because the tax expenditure has its own specific purpose, the net negative impacts do not necessarily imply that the tax expenditure is not desirable. The statute does not explicitly state the purpose of this tax expenditure; however, we assume that the purpose is to encourage investment, job creation and economic development in Massachusetts, which seem achieved according to MOBD’s annual report as discussed in the previous section. See Appendix II for more discussion.

**Similar Tax Expenditures Offered by Other States**

Most states have some form of economic development incentive. This is a widely adopted tax incentive.

**IS THE INCENTIVE AS DESIGNED ACCOMPLISHING ITS PURPOSE?**

[FOR TERC TO COMPLETE]

# References

Felix, R. A. (2009, Second Quarter). *Do State Corporate Income Taxes Reduce Wages?,* Economic Review, FEDERAL RESERVE BANK OF KANSAS CITY.

*Fiscal Year 2020 Annual Report: Economic Development Incentive Program (EDIP).* Boston: Massachusetts Office of Business Development.

Keith R. Ihlanfeldt, David L. Sjoquist. (2001, August). Conducting an Analysis of Georgia’s Economic Development Tax Incentive Program. *ECONOMIC DEVELOPMENT QUARTERLY, 15*(3), 217-228.

*MODELS: TAX-PI*. (n.d.). Retrieved from Regional Economic Models, Inc.: https://www.remi.com/model/tax-pi/

**Appendix I: More Background Information on EDIP**

In the text we note that, though the annual cap for the credit is $30 million, the actual claimed amounts for the credit have been lower than the cap and varied by year. To understand why that has occurred, it is necessary to review the history of the credit. The data and description of credit history in this appendix are based on information provided by MOBD.

The EDIP program was changed significantly by the Acts of 2009 and was administered on annual budget. Prior to that, there was no limit on the amount of EDIP projects that could be approved. Economic Opportunity Area Credit (EOAC) was the tax credit approved prior to tax years beginning on or after January 1, 2010. The amount was equal to 5% of the cost of any property that qualified for the Investment Tax Credit (ITC) allowed by M.G.L. c. 63, § 31A. EOAC had long carryforward provisions which made the claimed amount very difficult to forecast. In 2010, the first EDIP Credits were granted under entirely new rules. To reduce the chance that EDIPC would exceed budget due to the unknown carryforward liability of EOAC, it was decided that EACC would not award the full cap amount of EDIP credit. As a result, there was always some amount of tax credits withheld to account for the EOAC carryforward liability. Table A1-1 shows how much the EDIP credit was held in reserve by year. The award for EDIP credit has been adjusted down by the amount held in reserve each year. This finally expired in 2020.

**Table A1-1. The Amount Held in Reserve for EDIP Credit**

|  |  |
| --- | --- |
| Year | Amount Held in Reserve |
| 2010 | $ 20,016,178 |
| 2011 | $ 17,860,953 |
| 2012 | $ 14,475,661 |
| 2013 | $ 11,368,616 |
| 2014 | $ 9,745,425 |
| 2015 | $ 8,107,788 |
| 2016 | $ 6,578,150 |
| 2017 | $ 5,701,478 |
| 2018 | $ 4,082,960 |
| 2019 | $ 1,610,158 |
| 2020 | $ 0 |

Source: Massachusetts Office of Business Development (MOBD)

Additionally, the Acts of 2016 called for every EDIP project ever awarded tax credits to be under contract with the EACC by December 31, 2016. This was for the purpose to estimate how much potential EOAC carryforward was still out there. Any company that did not sign a contract now gets booted from the tax system if they want to use EOAC and do not have a contract. From 2010 to 2014, the total combined annual calendar year tax credits budget for EDIP and HDIP (Housing Development Incentive Program) was $25 million in which $20 million was for EDIP and $5 million for HDIP. In 2015, the budget became $30 million for both programs combined, and the cap for HDIP was raised to $10 million from $5 million. The first year HDIP granted awards were in 2014 for $1,167,825. In 2015, HDIP made $0 in awards. In 2016, the two programs became separated. HDIP funding was clearly $10 million annually. Subsequently, the statute was revisited and the annual cap for EDIP increased to $30 million. However, the Administration & Finance (A&F) dictated that EACC could award only $20 million annually regardless of the statutory cap of $30 million. EACC continues to award only $20 million of EDIPC to this day.

A reform of the EDIP credit occurred in 2017 for the purposes of more accountability, increased flexibility, and wiser investment of public funds. We will not discuss every detail of the reform in this report but will highlight key points of the EDIP reform before and after the 2017 reform in Table A1-2 below. We expect the credit to be used closely to the cap going forward.

**Table A1-2. EDIP before the 2017 reform and after the 2017 reform**

|  |  |
| --- | --- |
| **Before the reform** | **After the reform** |
| Certified projects had to meet the criteria for one of four kinds of projects: EP, EEP, MRP and JCP. | One category: certified project. |
| For most project categories, the amount of credit was limited by the company’s capital expenditures. | Amount of credit is determined by the EACC based on job creation and other relevant considerations. |
| Local incentives were required for some projects. | A local incentive is optional for all projects; and there is more flexibility for the amount of a local incentive. |
| Project certification could be revoked if there was a “material variance” from projections; revocation was required where a company created less than half of the new jobs promised | EACC has more discretion to decertify a nonperforming project; and upon decertification, the loss of tax credits may be proportional to actual job creation. |
| Difficult for DOR to recapture tax credits that were claimed but not earned | DOR has better tools to recoup credits the company claimed but did not earn. |

Source: Massachusetts Office of Business Development (MOBD)

**Appendix II: Further Discussion on Costs and Benefits**

The text of the report discusses the direct costs (to the Commonwealth, or more specifically, to the Massachusetts residents or businesses who benefit from state expenditures[[8]](#footnote-9)) and direct benefits (to taxpayers who claim the benefits) of this tax expenditure. It also summarizes indirect and induced costs and benefits associated with this tax expenditure. This appendix will discuss the indirect and induced, as well as other costs and benefits in more detail.

**Other costs and benefits: Indirect and Induced**

*Indirect and Induced Costs*

Regardless of its size, the existence of a specific tax incentive means less revenue for other spending given the Commonwealth’s balanced budget requirement, assuming that there is no increase in state revenues. Reduced spending on other expenditure items means forgone benefits from those items. This is an **“opportunity cost”** to the Commonwealth. The opportunity cost to the state includes not only the impact on the businesses and their employees that directly benefit from those expenditure items (this is called “direct impact”), but also the indirect impact on the chain of businesses that provide intermediate products and services to the directly impacted businesses (this is called “indirect impact”). In addition, there is the cost to the chain of businesses that benefit when the employees working for the directly impacted businesses spend their wages and salaries to buy goods and services (this is called “induced impact”). The total forgone benefits to the whole economy are larger than the initial forgone benefits. This phenomenon is called the “Multiplier Effect”.[[9]](#footnote-10)

To estimate the total forgone benefits of the reduced spending, we employed Tax-PI, an economic analysis tool for evaluating the total fiscal and economic effects of tax policy changes. Tax-PI is built on over 30 years of experience in modeling the economic effects of tax policy changes, according to MODELS: TAX-PI in the reference. The popularity of the model has grown substantially since it was introduced. Note that while the tax incentive has a specific purpose, the reduced spending is assumed to be proportionally distributed across the Commonwealth’s current expenditures.

*Quantifying total costs (direct, indirect and induced)*

The period of study is limited to the five years from 2018 through 2022, for which we prepared input data to run the model. Tables A2-1 and A2-2 report the model results. The figures for 2018 and 2019 are estimates of forgone benefits (opportunity costs) that the Massachusetts economy experienced due to having the expenditure, and those for 2020, 2021 and 2022 are projections of forgone benefits that the Massachusetts economy will experience going forward. The effects are displayed as negative numbers as reduced spending has a negative impact on the state economy.

Tables A2-1 and A2-2 show that the reduction in state government spending results in lost economic activity, with real state GDP declining by $42 million - $46 million and total employment declining by 464- 526 jobs annually. Lost economic activity results in further loss of state revenues, ranging from $0.9 million to $2.4 million annually. Note that the revenue impact reported in Table A2-1 does not include the estimated direct impact of the tax expenditure from Table 1, but only the additional indirect/induced impact.

**Table A2-1. Additional Revenue Impact due to Decreased Government Spending\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Fiscal Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Additional revenue impact ($000) | -$941 | -$2,047 | -$2,266 | -$2,406 | -$2,438 |

\* This table reports the lost revenues from the foregone economic activity as the state reduced government spending to finance the EDIP credit.

**Table A2. Economic Impacts due to Decreased Government Spending by Selected Economic Measure\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Calendar Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Impact on total employment | -511 | -518 | -526 | -498 | -464 |
| Impact on private non-farm employment | -282 | -285 | -291 | -271 | -246 |
| Impact on GDP ($000), real dollars (2012) | -$44,000 | -$45,000 | -$46,000 | -$44,000 | -$42,000 |
| Impact on personal income ($000) | -$37,000 | -$41,000 | -$46,000 | -$47,000 | -$47,000 |

\*This table reports the lost economic activity as the state reduced government spending to finance the EDIP.

*Indirect and Induced Benefits*

The cost savings due to the EDIP credit encourage the directly affected businesses to invest, expand, hire additional workers, etc. Such decisions would increase demand for goods and services provided by other individuals and businesses in the economy, or put another way, generate a “Multiplier Effect” (see discussion in the previous section) from the initial or direct benefits as reported in the text. As a result, the total benefits of the EDIP credit would be larger than the initial or direct benefits.

*Quantifying total benefits (direct, indirect and induced)*

To quantify the total benefits, including indirect/induced benefits, we again employed Tax-PI. A summary of the revenue impact of the EDIP credit is reported in Table A2-3, and the economic benefit from the EDIP credit is reflected in Table A2-4 below. The figures for 2018 and 2019 are estimates of benefits that the Massachusetts economy experienced and those for 2020, 2021 and 2022 are projections of the benefits that the Massachusetts economy will experience going forward.

Tables A2-3 and A2-4 show that, the EDIP credit results in more economic activity, with real state GDP increasing by $23 million - $45 million and total employment increasing by 237 – 386 jobs annually. More economic activity results in more state revenues, ranging from $0.6 million to $2.3 million annually, which partially offsets the cost of this tax incentive.

**Table A2-3. Additional Revenue Impact of EDIP Credit**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Fiscal Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Additional revenue impact ($000) | $553 | $1,353 | $1,772 | $2,098 | $2,301 |

**Table A2-4. Economic Impacts of EDIP Credit by Selected Economic Measure**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Calendar Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Impact on total employment | 237 | 312 | 370 | 386 | 384 |
| Impact on private non-farm employment | 228 | 295 | 342 | 356 | 352 |
| Impact on GDP ($000), real dollars (2012) | $23,000 | $32,000 | $39,000 | $43,000 | $45,000 |
| Impact on personal income ($000) | $17,000 | $25,000 | $32,000 | $37,000 | $40,000 |

Note that the overall economic impact reported in this section, especially job creation, is much smaller than the job creation reported in MOBD’s EDIP FY2020 annual report. The reasons for such big differences may include: (1) In this analysis, REMI Tax-PI model captures only the businesses’ general response to cost saving due to EDIP credits (but not specific features of the EDIP program) whereas in real world other components of the EDIP program may be also important, such as facilitation to resources (workforce training, financing, export assistance, infrastructure support, etc) and other help to businesses. (2) As discussed in the text, numbers in MOBD’ annual report may be not as large as they appear to be. More importantly, the number of job creation and retention may be not necessarily all “net new” jobs and could be jobs shifted from other part of the state or from future.

**Comparison of costs and benefits**

Ignoring the opportunity cost of the tax incentive, total benefits are greater than costs. Considering the opportunity cost means asking what benefits would be reaped if the Commonwealth used the dollars spent on the tax incentive for other purposes. Those dollars could be spent in many other ways, and examining them is beyond the scope of the current evaluation report. Nonetheless, we reported net impacts of the tax incentive in Tables A2-5 and A2-6 below under the balanced budget requirement, which are the combined effects in Tables A2-1 to A2-4.

Tables A2-5 and A2-6 show that the EDIP credit combined with a cut in state government spending results in less economic activity in general, with real state GDP changing by -$21 million to +$3 million. The net impact on total employment is negative, decreasing by 80 – 274 jobs annually. The net additional impact on state revenues is also negative, decreasing by $0.1 million to $0.7 million annually.

**Table A2-5. Net Additional Revenue Impact of EDIP Credit\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Fiscal Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Net additional revenue impact ($000) | -$388 | -$694 | -$494 | -$308 | -$137 |

\* assuming state government spending is cut by the same amount as the revenue loss due to EDIP credit to balance budget.

**Table A2-6. Net Economic Impacts of EDIP Credit by Selected Economic Measure\***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Calendar Year | 2018 | 2019 | 2020 | 2021 | 2022 |
| Impact on total employment | -274 | -206 | -156 | -112 | -80 |
| Impact on private non-farm employment | -54 | 10 | 51 | 85 | 106 |
| Impact on GDP ($000), real dollars (2012) | -$21,000 | -$13,000 | -$7,000 | -$1,000 | $3,000 |
| Impact on personal income ($000) | -$20,000 | -$16,000 | -$14,000 | -$10,000 | -$7,000 |

\* assuming state government spending is cut by the same amount as the revenue loss due to EDIP credit to balance budget.

Because the tax expenditure has its own specific purpose, the net negative impacts do not necessarily imply that the tax expenditure is not desirable. The statute does not explicitly state the purpose of this tax expenditure; however, we assume that the purpose is to encourage investment, job creation and economic development in Massachusetts, which seem achieved according to MOBD’s annual report as mentioned in the text.

**Other unquantified costs and benefits:**

Besides the additional costs and benefits quantified in the previous sections, there are other costs and benefits that are hard to quantify due to lack of data or other challenges. In this section we will enumerate some of these costs and benefits.

Ihlanfeldt and Sjoquist (2001), a published study for the state of Georgia, summarizes some of the other costs and benefits as follows:

*Loss of competitiveness.* Providing tax incentive such as credits to selected firms may diminish the competitiveness for existing similar firms.

*Compliance costs.* They think that the costs to the firm may be substantial.

*Improved business climate.* Tax incentive improves the perception of the business climate in the state and is used by site location specialists in screening alternative sites.

*Synergistic or clustering effects.* Tax incentive may attract a firm in an industry new to the state, which then serves as a magnet for attracting additional firms in the industry.

EDPIC is in general deployed to areas such as gateway cities where economic development is needed socially, and it creates desirable social benefits.

Another hard to quantify cost is the administrative cost. The administrative cost to the Department of Revenue attributable to this incentive should be relatively small because the Department of Revenue administers the credit with existing staff as part of its overall mission. There is also administrative cost of the credit to EACC and MOBD as a key component of the EDIP program.

**Other issues related to costs and benefits**

The burden of a tax does not necessarily fall on those responsible for remitting the tax. It is known through economic theories that corporate taxes change the allocation of capital between corporations and noncorporate businesses and among states because capital would flee from states of higher corporate taxes if all other considerable factors are not significantly different.

Felix (2009) finds that labor bears a significant burden from the state corporate tax in the form of lower wages. Her study further suggests that a one-percentage-point increase in the marginal state corporate tax rate reduces wages by 0.14% to 0.36%, that labor’s burden from the state corporate tax has trended upward over time due to increased global competition and increased competition among states to attract businesses, and that state corporate taxes reduce the wages of highly educated workers more than that of less-educated workers.

The EDIP credit reduces the effective tax rate of its direct beneficiaries. The findings imply that the incentive may have benefited workers who were employed by the corporations in the form of higher wages. The incentive may have further benefited the shareholders and clients due to the growth of businesses.

1. EDIP annual reports can be found on this site: <https://www.mass.gov/service-details/economic-development-incentive-program-edip>. [↑](#footnote-ref-2)
2. In Massachusetts, for some credits such as EDIPC and ITC (investment tax credit), the claimed amount may not exceed 50% of a tax filer’s tax liability. The rule is not applicable for personal income tax filers. [↑](#footnote-ref-3)
3. There were about 30 claims (15 for EOAC and 15 for EDIPC) from personal income tax filers in 2017. There were 2 claims from insurance tax filers. The reason why we excluded insurance tax filers and personal income tax filers was that they did not report comparable detailed information such as number of employees or they are taxed somewhat differently than other corporations. For example, for insurance tax filers, their tax liability is largely based on their insurance premiums. However, the amount of excluded credit is relatively small. [↑](#footnote-ref-4)
4. Tables 3-4 show that there were 117 *claimants* for the credit in 2017, which is slightly lower than the 131 *claims* reported in Table 2. There are two reasons for this difference besides the exclusion of insurance taxpayers in tables 3-4. First, for combined reporting corporate tax filers, the data sets for credits include only the parent corporation’s identification number. So, we were not able to match with other data sets that include information on employees, NAICS codes, etc. at the subsidiary company level. Second, there were rare cases in which a claimant had more than one claim. For example, some taxpayers within a combined group might have taken part of the available credit and shared the remainder with other members (all claims are counted under the name of the parent corporation). [↑](#footnote-ref-5)
5. <https://www.mass.gov/doc/edip-fy2020-annual-report/download> [↑](#footnote-ref-6)
6. Regional Economic Models, Inc. is a recognized leader in economic analysis at the state level. See their website for background information and further details <https://www.remi.com/> [↑](#footnote-ref-7)
7. Including both tax and non-tax revenues but excluding the revenue loss reported in Table 1. [↑](#footnote-ref-8)
8. Spending on a specific tax incentive means less spending on other expenditure items for the Commonwealth under balanced budget requirement if there is no increase in state revenues. Reduced spending on other expenditure items means forgone benefits from those items. This is an opportunity cost to the Commonwealth, which, more specifically, is borne by the Massachusetts residents or businesses who benefit from those expenditure items. [↑](#footnote-ref-9)
9. For an illustration of “Multiplier Effect”, see Slide 4 of: <https://www.ilw.com/seminars/JohnNeillCitation.pdf> [↑](#footnote-ref-10)