A fact sheet from THE PEW CHARITABLE TRUSTS | Jan 2014

How to Inform Policy Choices

Evaluating State Tax Incentives

Tax incentives are central to most states' economic development strategies, with states collectively spending billions of dollars a year on them. But when incentives are enacted as permanent parts of state tax codes, lawmakers often have little impetus to review them. Unlike direct state spending, which must be renewed with each budget, tax incentives frequently continue indefinitely without policymakers revisiting their cost or effectiveness.

By integrating the evaluation of tax incentives into the policymaking process, states can ensure that incentives are reconsidered regularly and that elected officials make economic development decisions based on evidence. States such as Oregon, Washington, and Rhode Island now ensure that these important policy choices get the attention they deserve by implementing the following procedures:

- In Oregon, tax credits are given expiration dates.
- In Washington, legislative committees hold annual hearings on the results of evaluations.
- In Rhode Island, a new law ensures that incentives are reviewed alongside other state spending.

These approaches are models for policymakers in other states to consider as they work to make their tax incentive programs more effective and accountable.

Oregon

In Oregon, most tax credits expire every six years unless lawmakers renew them. These "sunsets" encourage policymakers to seek information about the effectiveness of incentives as they debate whether the programs should be extended, altered, or allowed to expire.

In 2011, the state's newly created Joint Committee on Tax Credits was given the task of reviewing 18 expiring credits and proposing changes. The committee requested evaluations of the programs and held hearings to review the evidence and hear testimony from key stakeholders. Ultimately, based on the committee's recommendation, the Legislature allowed some little-used credits to expire while extending or redesigning others. (See Figure 1.)

Figure 1

Sunsets Spur Review of Incentives' Results

In 2011, Oregon lawmakers used evaluations to make informed decisions about 18 tax credits that were due to expire and took the following action:

4 credits	Renewed without changes
5 credits	Redesigned and renewed
9 credits	Allowed to expire

Source: 76th Legislative Assembly, Interim Joint Committee on Tax Credits, "2011 Tax Credit Sunset Process"

One of the credits the state modified was an incentive program for renewable energy projects, such as wind and solar farms that had grown far more expensive than anticipated. The Legislature's 2011 changes redirected the program toward smaller-scale energy projects, which depended more heavily on the incentives for their financial success, according to an evaluation. The modifications to the renewable energy incentives were expected to save the state $20 million over the next two years and hundreds of millions of dollars after that.[1]

Washington

In Washington state, the Joint Legislative Audit and Review Committee is responsible for reviewing tax incentives on a 10-year cycle. The committee's nonpartisan staff submits detailed evaluations with recommendations on whether to continue, modify, or end specific tax incentives. Next, a citizens' commission considers the evaluations, holds public hearings, and develops its own recommendations. Finally, the committee and the citizens' commission together provide evidence and guidance to the Legislature's fiscal committees, which hold a joint hearing on the results.

This process has spurred lawmakers to act on evaluation findings. For example, they ended an incentive meant to support the state's beef processors after the committee's staff concluded that the industry was no longer experiencing the consequences of a mad-cow disease outbreak that had prompted creation of the program.[2]

Rhode Island

Rhode Island approved a law in 2013 that builds review of tax incentives into the annual budget process. Starting in 2014, each incentive will be evaluated by the state's tax office every three years. Informed by the findings, the governor's budget proposal will include a recommendation on whether to continue, change, or end the program. These gubernatorial recommendations will then be the subject of legislative hearings, providing lawmakers with opportunities to review evaluation results and consider tax incentives alongside other state spending.[3]

Endnotes

1 State of Oregon, 76th Legislative Assembly, Interim Joint Committee on Tax Credits, "2011 Tax Credit Sunset Process." In addition, the committee made changes to three credits not due to expire and created one new credit.

2 State of Washington, Joint Legislative Audit & Review Committee, "2013 Tax Preference Performance Reviews: Proposed Final Report," December 2013, http://www.leg.wa.gov/JLARC/AuditAndStudyReports/2013/Documents/2013TaxPreferenceReviewsProposedFinalReport.pdf; Joint Legislative Audit and Review Committee, "Tax Preference Performance Review: Beef Processors" (March 21, 2007), http://www.leg.wa.gov/JLARC/AuditAndStudyReports/2007/Documents/07-7.pdf#page=1, pg. 24.

3 Rhode Island Economic Development Tax Credit Accountability Act of 2013, http://webserver.rilin.state.ri.us/BillText/BillText13/SenateText13/S0734B.pdf.

Contact: Jeff Chapman, manager, economic development tax incentives project, The Pew Charitable Trusts
Email: jchapman@pewtrusts.org **Phone:** 202-540-6567 **Project website:** pewstates.org/taxincentives