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How States Are Improving Tax Incentives for Jobs and Growth

Michigan Financial Liability Reform Committee

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Why evaluate tax incentives

- Tax incentives are one of states' primary economic development tools
- Tax incentives collectively cost states billions of dollars per year
- Evaluation is a proven way to improve the effectiveness of incentives
- Evaluations can lead to a more constructive conversation about incentives

Year evaluation laws were adopted in states that are "leading" or "making progress"

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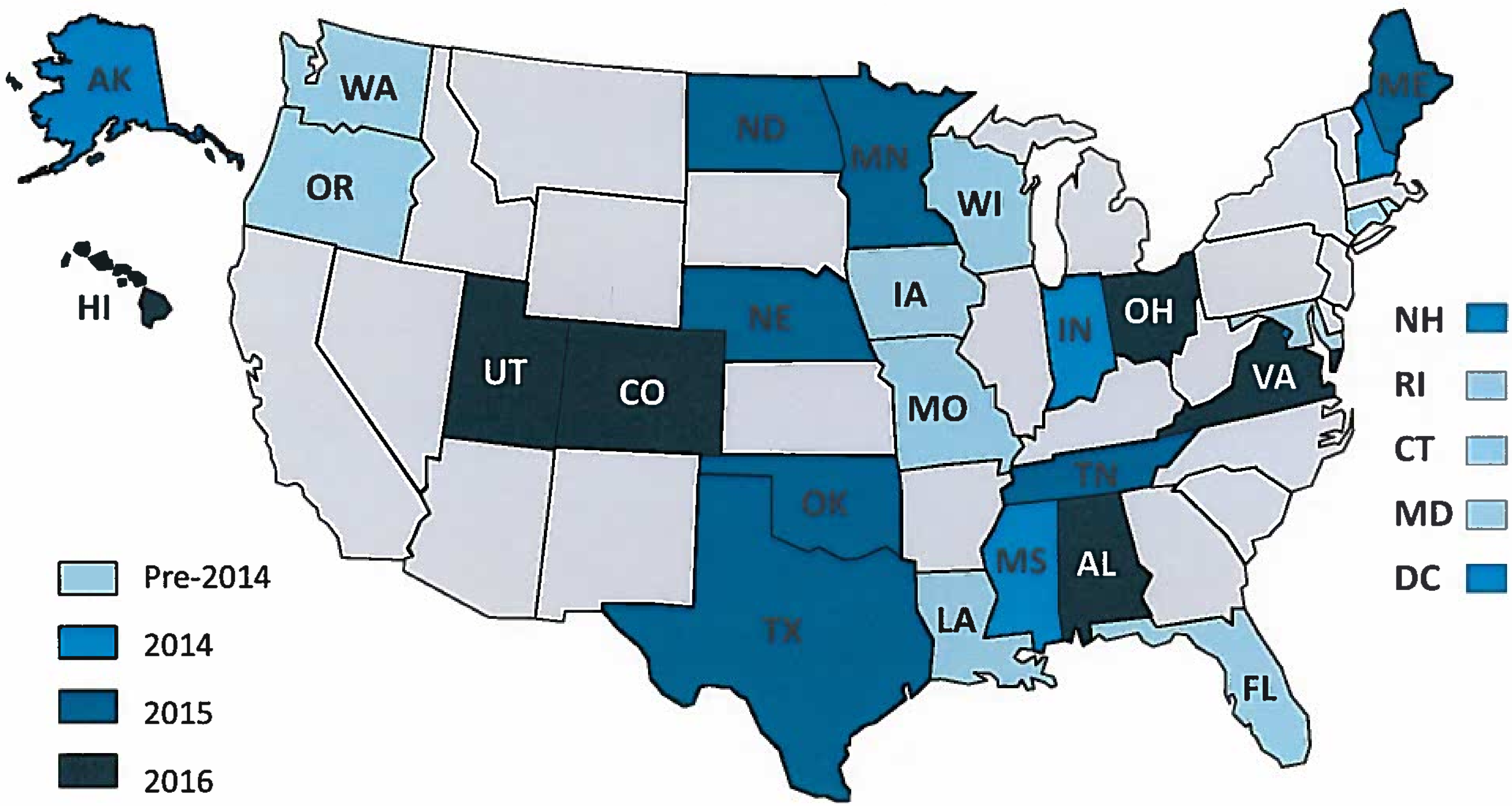

Three steps to effective evaluation

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Step 1: Make a plan

Step 2: Measure the impact

Step 3: Inform policy choices

State tax incentive evaluation ratings

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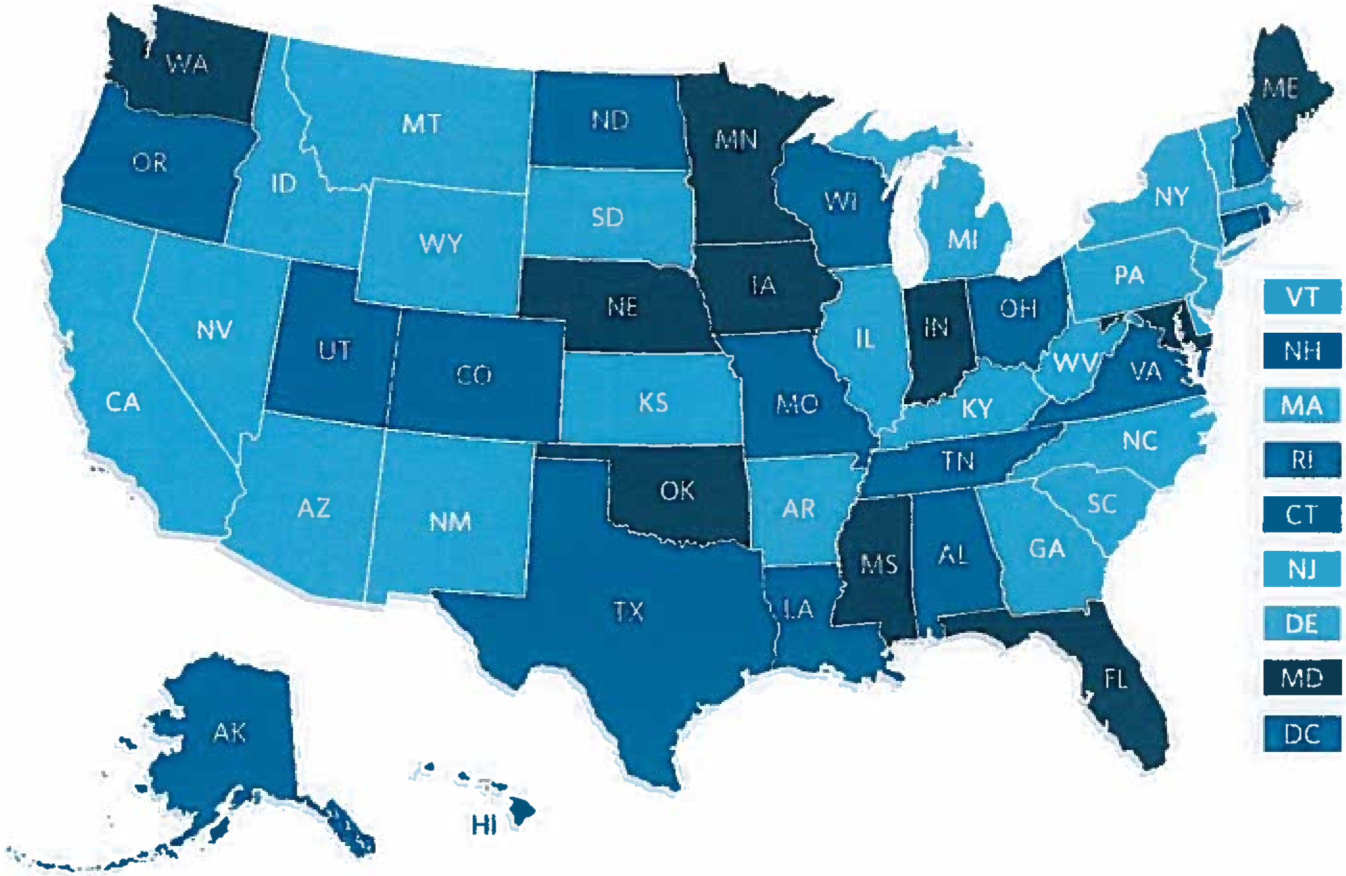
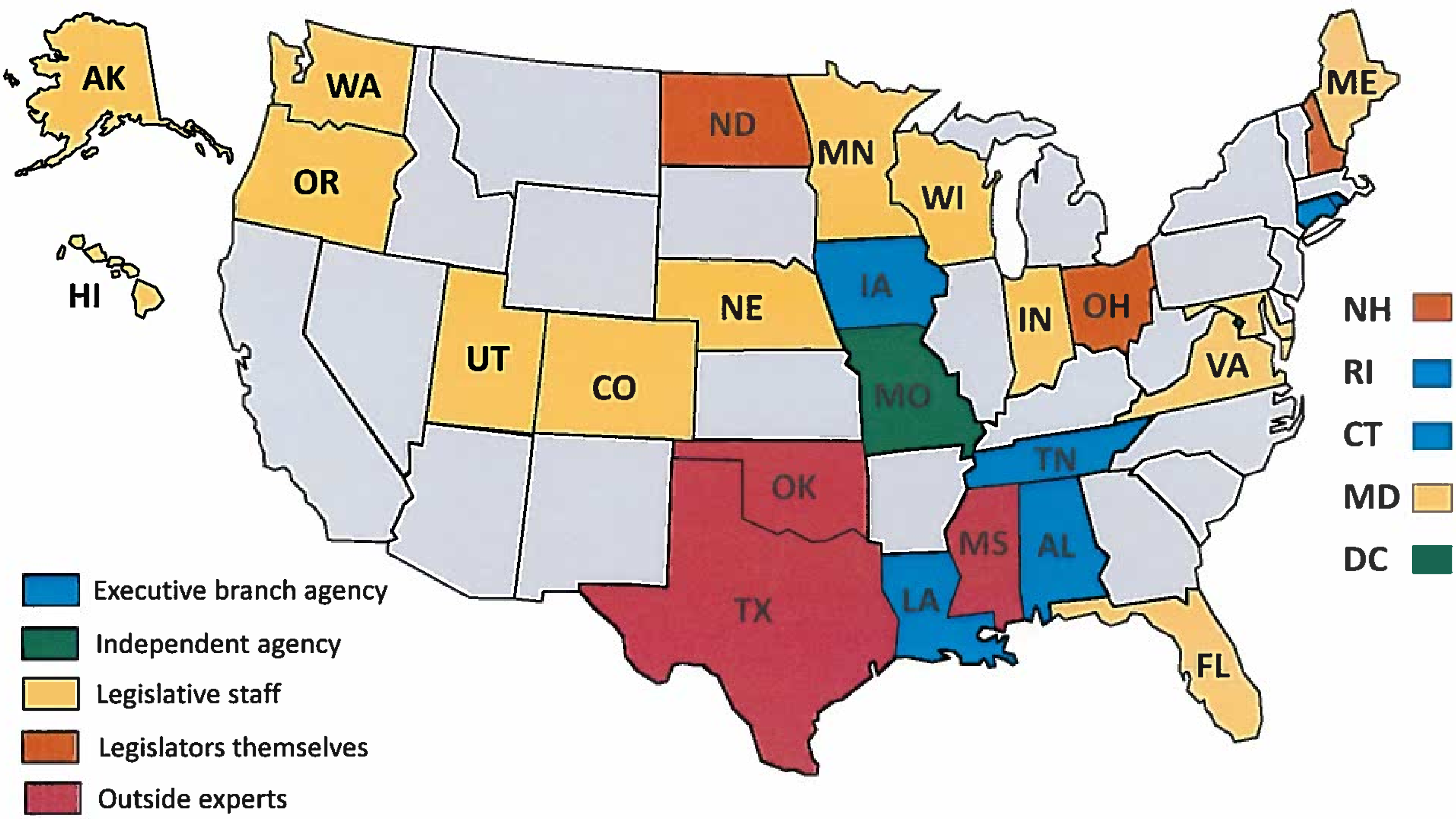


10 leading 18 making progress 23 trailing

Make a plan: Who evaluates in states that are "leading" or "making progress"



Make a plan: Developing a strategic schedule

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- Include all major incentives
- Use a rotating multi-year cycle
- Study incentives with similar goals in the same year
- Coordinate evaluations with sunset dates

Measure the impact: High-quality evaluations include…

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- A description of the incentive, its history, and goals
- An assessment of the incentive's design and administration
- An estimate of the incentive's economic and fiscal impact
- Policy recommendations

Evaluation example: Indiana

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Table 12: Taxpayer Discount Scenario – Solar-Powered Roof Vent/Fan Installation Deduction

Item	Tax Incentive
Solar Vent Fan Cost	$600
Installation Cost	300
Total Cost	**$900**
Deduction Amount (50% of Total Cost)	(450)
Indiana State and Local Tax Savings	**($21)**
Total Projected Cost After Savings	**$879**
Discount %	**2.33%**

Evaluation example: Alabama

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Component	CAPCO Grade	HRTC Grade
Efficiency: a well-defined *return on investment* to the state of Alabama.	D	C
Transparency: clear benefits to taxpayers and costs to the state.	D	A
Certainty: defined impact on state budget and program beneficiaries.	C	B
Prospective: encourage future activity rather than reward previous decisions.	D	B
Simplicity: *easy to administer and easy to comply with.*	B	B
Targeted: focused and provided on a *discretionary* basis to promote new activity.	C	B
Protection of Public Funds: through caps or time limits on the use of credits.	C	A
Leverage: to encourage additional public or private resources.	B	A
Accountability: *performance-based incentives* should be built into the program.	D	B
Evaluation: to identify the extent to which incentives induced new activity.	F	C
Ownership: to ensure proper administration and to support a thorough evaluation.	D	A
OVERALL	**D**	**B**

With evaluations, states can…

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- Make subtle changes to incentives to increase their return on investment

- Identify programs that are working well, so that the state can invest in them with confidence

- Repeal or replace ineffective or obsolete incentives

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