

EVALUATION OF THE ENTERPRISE ZONE TAX CREDIT



DEPARTMENT OF LEGISLATIVE SERVICES 2014

Evaluation of the Enterprise Zone Tax Credit

**Department of Legislative Services
Office of Policy Analysis
Annapolis, Maryland**

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF POLICY ANALYSIS
MARYLAND GENERAL ASSEMBLY

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Warren G. Deschenaux
Director

August 6, 2014

The Honorable Thomas V. Mike Miller, Jr., President of the Senate
The Honorable Michael E. Busch, Speaker of the House of Delegates
Honorable Members of the Maryland General Assembly

Ladies and Gentlemen:

The Tax Credit Evaluation Act of 2012 (Chapters 568 and 569) established a legislative process for evaluating certain tax credits. The Tax Credit Evaluation Committee created by that legislation was required to review and evaluate the Enterprise Zone tax credit by July 1, 2014. To assist the committee in its work, the Department of Legislative Services (DLS) was required to evaluate the tax credit on a number of factors, including (1) the purpose for which the tax credit was established; (2) whether the original intent of the tax credit is still appropriate; (3) whether the tax credit is meeting its objectives; (4) whether the goals of the tax credit could be more effectively carried out by other means; and (5) the cost of the tax credit to the State and local governments.

During the 2013 interim and 2014 session, the committee reviewed a draft of this report and also held a public hearing on the report. The report makes several recommendations as to how the tax credit may be more effectively claimed and administered. The report is divided into four chapters.

Chapter 1 provides an overview of State tax credits, the Tax Credit Evaluation Act, and the Enterprise Zone tax credit.

Chapter 2 provides an overview of the objectives of Enterprise Zone programs.

Chapter 3 assesses the economic impact of the credit, as well as its impact on State and local finances.

Chapter 4 summarizes the findings of the report and discusses recommended changes to the tax credit.

The Honorable Thomas V. Mike Miller, Jr., President of the Senate
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We wish to acknowledge the cooperation and assistance provided by various State agencies in the development of this report. DLS trusts that this report will be useful to members of the Tax Credit Evaluation Committee and the other members of the General Assembly in future deliberations about the Enterprise Zone tax credit.

Sincerely,

Warren G. Deschenaux
Director

WGD/mpc

cc: The Honorable Richard S. Madaleno, Jr. Co-chair, Tax Credit Evaluation Committee
The Honorable C. William Frick, Co-chair, Tax Credit Evaluation Committee
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Executive Summary

Since the mid-1990s, the number of State business tax credits has grown exponentially, as have related concerns about the actual benefits and costs of many of these credits. Although tax credits comprise a small percentage of total income tax revenues, the number and amount of credits claimed have increased over time. Since 1995, 28 primarily business tax credits and 14 primarily individual tax credits have been established; these numbers include temporary and/or expired tax credits.

In response to concerns about the impacts of tax credits on State finances, Chapters 568 and 569 of 2012 established the Tax Credit Evaluation Act, a legislative process for evaluating certain tax credits. The evaluation process is conducted by a legislative evaluation committee that is appointed jointly by the President of the Senate and the Speaker of the House. The Act requires that the Enterprise Zone tax credit be evaluated by the committee by July 1, 2014. To assist the committee in its work, the Department of Legislative Services (DLS) is required to evaluate each credit on a number of factors, including (1) the purpose for which the tax credit was established; (2) whether the original intent of the tax credit is still appropriate; (3) whether the tax credit is meeting its objectives; (4) whether the goals of the tax credit could be more effectively carried out by other means; and (5) the cost of the tax credit to the State and local governments.

Created in 1982, the Enterprise Zone tax credit program was designed to encourage and assist in economic growth within economically distressed areas and to improve the employment of the chronically unemployed in the State. In an effort to better understand the fiscal impacts and

effectiveness of the credit, this report provides an overview of the credit, how enterprise zones are designated, the economic challenges facing residents in and near enterprise zones, the impacts of the credit on residents and businesses in particular enterprise zones, and the costs of the tax credit.

DLS makes several recommendations as to how the effectiveness of the Enterprise Zone tax credit might be improved.

Enterprise Zone Tax Credits Are Not Effective in Creating Employment Opportunities for Enterprise Zone Residents

While Enterprise Zone tax credits may incentivize some businesses to create additional jobs within enterprise zones, the tax credit is not effective in providing employment to zone residents that are chronically unemployed and/or live in poverty. A number of factors contribute to this problem, including skills mismatches for new jobs created, lower than average educational attainment levels of zone residents, and labor mobility. As such, improved educational opportunities and/or additional job training programs for residents may be more effective in enabling those residents to better compete for jobs created in enterprise zones.

DLS recommends that the Department of Business and Economic Development (DBED) and the Department of Labor, Licensing, and Regulation (DLLR) propose statutory changes that will improve the likelihood that residents in enterprise zones and enterprise zone communities, particularly

those that are in poverty and/or chronically unemployed, can gain employment within enterprise zones. DBED and DLLR should also propose methods by which other State and local programs that seek to improve job skills and educational attainment levels, such as job training programs, can be better coordinated with the Enterprise Zone tax credit.

Annual claims for the Enterprise Zone income tax credit have been modest, particularly when compared to the property tax credit. DBED indicates that this could be in part due to administrative burdens that contribute to low utilization rates of the enhanced income tax credit that can be claimed for hiring members of an economically disadvantaged household.

DLS recommends that DBED, in consultation with the Comptroller's Office, propose statutory changes to the Enterprise Zone income tax credit that will help increase net employment, including reducing administrative burdens and a mechanism that incorporates job reductions at similar sites or other locations in the State.

In a Significant Number of Enterprise Zones, Few Businesses Are Claiming the Tax Credit

Of the 30 current enterprise zones, 13 zones have less than 10 businesses claiming Enterprise Zone property tax credits. Not only are these enterprise zones failing to attract many businesses, but a number of the businesses claiming the tax credit are not making significant investments in those zones. Each political subdivision is authorized to establish additional local standards to govern access

to the program. Many local jurisdictions generally require a minimum capital investment or a minimum number of jobs created, or both. A few enterprise zones also have additional standards limiting the type or category of business entity that is eligible to participate.

DBED should comment as to the potential reasons for the lack of activity in some enterprise zones, the variation in program effectiveness across zones, and the role of local standards in attracting businesses to enterprise zones, specifically as to whether those local standards are beneficial or a detriment to encouraging businesses to locate in enterprise zones.

DBED and the Comptroller's Office Do Not Assess the Effectiveness of the Enterprise Zone Tax Credit

DBED and the Comptroller's Office are required by law to annually assess the effectiveness of tax credits provided to businesses in enterprise zones, including the number and amount of credits granted and the success of the tax credits in attracting and retaining businesses within enterprise zones. While DBED tracks the number and amount of credits granted annually, it does not have a framework or metrics in place for measuring the actual effectiveness of the credit. There is also a lack of accurate data on the change in employment and number of businesses within enterprise zones, which makes assessing the impacts of the credit very difficult.

DLS recommends that DBED, in consultation with the Comptroller's Office and the State Department of Assessments and Taxation (SDAT), adopt formal metrics and a framework for analyzing the cost effectiveness of each

enterprise zone and the effectiveness of each zone in attracting businesses and increasing employment. DBED should identify clear outcomes and determine quantifiable measures, which could include project evaluation, employment trends, impacts on poverty and population, private-sector investment in communities, and overall community revitalization.

Enterprise Zone Expansions Have Become More Prevalent in Recent Years, Diluting the Impacts of Zones and Increasing State and Local Credit Costs

State reimbursements to local jurisdictions for 50% of Enterprise Zone tax credit costs are subject to an annual appropriation in the State budget. However, there is no limit on the maximum amount of reimbursements. State reimbursements have greatly increased in recent years, from \$2.5 million in fiscal 2001 to \$13.9 million in fiscal 2014, an average annual increase of 14%. There are few limitations on zone expansions and no specific criteria related to zone expansion requirements. In addition, a handful of enterprise zones are large enough to have one or more focus areas within the zone. State reimbursement costs may also increase significantly as credits are granted for new development projects, particularly for the Harbor Point and Amazon.com developments in Baltimore City.

DLS recommends that DBED propose statutory changes that will provide for evaluation criteria that must be considered before an enterprise zone may be expanded. These criteria could include restrictions on the size of any expansion, whether businesses have expressed interest in locating within the potential

area of expansion, and whether basic infrastructure is in place in order to facilitate business development within the proposed expansion area.

DBED should comment on whether focus areas within enterprise zones have actually increased employment and economic development in those areas above and beyond what would have otherwise occurred within the zone with the general Enterprise Zone tax credit.

DBED should comment on whether a cap on the maximum amount of State reimbursements that may be granted each year should be imposed.

Some Baltimore City Enterprise Zone Property Tax Credits Have Been Erroneously Calculated

Recent press reports and a performance audit conducted by the Office of Legislative Audits determined that errors in several property tax credit programs including the Enterprise Zone, Homestead, and Baltimore City Historic Tax credits. These reports also documented that \$700,000 in improper Enterprise Zone property tax credits were granted to properties located in Baltimore City. For this report, DLS requested that SDAT provide Enterprise Zone property tax credit data – SDAT was only able to partially fulfill the request and only after a significant delay which prevented DLS from fully analyzing the data.

SDAT should comment on:

- **whether the department’s current tax credit calculation procedures are sufficient to properly (1) calculate the current credit assessment if a**

property owner successfully appeals an assessment; (2) value the pre-improvement base year property assessment of the property; (3) assign the correct percentage of the credit based on which year the property is claiming the credit; and (4) exclude the value of residential property from the credit.

- **the administration of the credit for properties in Baltimore City, including (1) the reasons for SDAT procedures differing from procedures used in other counties; (2) the sources of discrepancies between initial and final credit determinations; and (3) how tax credit calculations for properties will be handled going forward.**

DLS advises that the evaluation committee may wish to consider asking the Office of Legislative Audits to conduct a performance audit of the Enterprise Zone property tax credit program.

Collection of Enterprise Zone Property Tax Credit Data Is Not Standardized

SDAT provided DLS a summary report of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone. While the data contained in the summary report and computation worksheets should have been sufficient to evaluate the Enterprise Zone property tax credit, some of the data that

SDAT provided was incomplete and/or inaccurate.

There is a lack of standardization in the data that each county assessment office provides about properties claiming the Enterprise Zone property tax credit. Data errors included incorrect base year assessments, using the wrong percentage of the eligible assessment to calculate the credit, and basic data entry errors. The methodology and processes used for reporting data is generally unsophisticated and often necessitates the manual entry of information.

In addition, the summary reports of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone did not match the aggregate data that SDAT provided. With such disparities in the data, it was impossible for DLS to determine if SDAT correctly calculated the State's reimbursement for half of the Enterprise Zone property tax credit.

DLS recommends that SDAT adopt regulations to provide for uniform Enterprise Zone tax credit data collection procedures in each county. SDAT should also work with local assessment offices to reduce the amount of data that is manually entered and improve its ability to provide data in an accurate and timely fashion. SDAT should comment as to whether additional resources would be required to implement these changes.

Chapter 1. Overview and Background

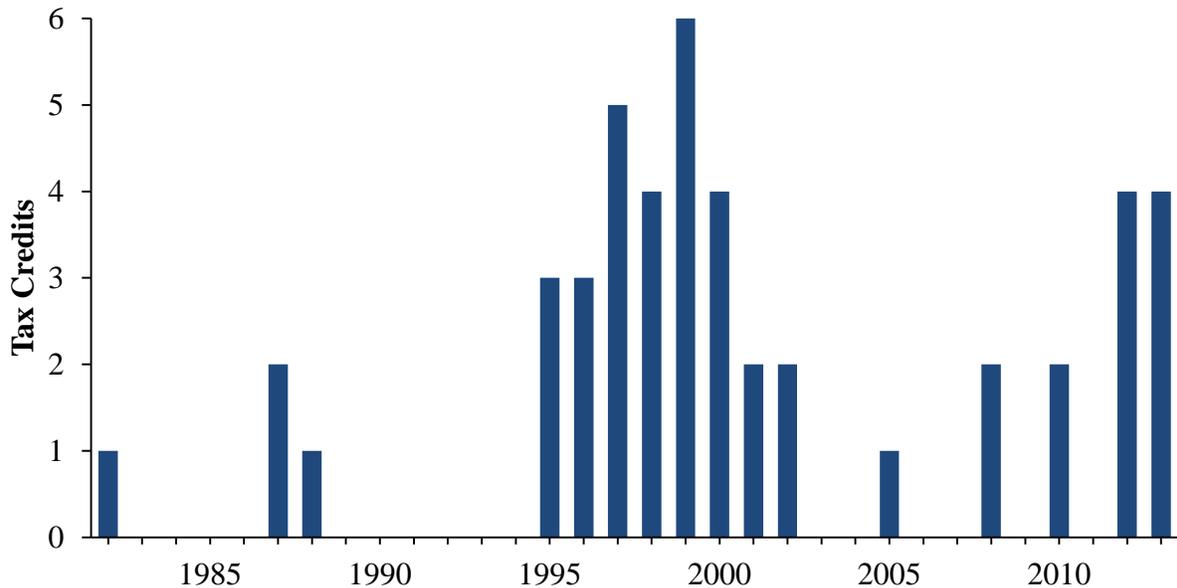
Introduction

Since the mid-1990s, the number of State business tax credits has grown exponentially, as have related concerns about the actual benefits and costs of many of these credits. Although the reduction in State revenues from tax credits are generally incorporated in the State budget, most tax credits are not subject to an annual budgetary appropriation as is required for most other State programs. However, a few credits are subject to an annual appropriation, such as the Biotechnology Investment and Sustainable Communities tax credits, as well as for State reimbursement for one-half of the local property tax revenue losses under the Enterprise Zone tax credit program. Information reported by State agencies for State tax credits varies by credit. Under certain tax credit programs, agencies are required to publish specified information about the credit on an annual basis. The Department of Budget and Management (DBM) is required to prepare every other year a tax expenditure report of the estimated amount by which exemptions from all types of State taxation reduce revenues.

Although tax credits comprise a small percentage of total income tax revenues (less than 3% in fiscal 2009), the number and amount of credits claimed has increased over time. Prior to 1995, there was one credit primarily for individuals (the Earned Income Credit) and two primarily business tax credits (Enterprise Zone and Maryland-mined coal credits). Since 1995, 28 primarily business tax credits and 14 primarily individual tax credits have been established; these numbers include temporary and/or expired tax credits.

As seen in **Exhibit 1.1**, the tendency has been for credits to be established in clusters by year. Twenty-nine of the credits were established between 1995 and 2002, and a resurgence of new credits occurred more recently, with 12 credits established since 2008, including 8 since 2012. The total amount expended for credits has increased from a little less than \$50 million in tax year 1994 to about \$250 million in tax year 2008. Most of this increase has been due to an increase in tax credits for individuals, which have increased by almost five-fold since 1994, primarily due to growth in the Earned Income Credit. Tax credits for businesses comprised about one-fifth of the total credits claimed in tax year 2008.

Exhibit 1.1
Number of Tax Credits Created Each Year
1982-2013



Source: Department of Legislative Services

Tax Credit Evaluation Act

Overview

In response to concerns about the impacts of certain tax credits, Chapters 568 and 569 of 2012 established the Tax Credit Evaluation Act, a legislative process for evaluating certain tax credits. The evaluation process is conducted by a legislative evaluation committee and must be done in consultation with the Comptroller's Office, DBM, the Department of Legislative Services (DLS), and the agency that administers each tax credit. The committee is appointed jointly by the President of the Senate and the Speaker of the House of Delegates and must include at least one member of the Senate Budget and Taxation Committee and one member of the House Ways and Means Committee.

The following credits are required to be reviewed by the date indicated:

- July 1, 2014: Enterprise Zone and One Maryland economic development credits;
- July 1, 2015: Earned Income and Film Production Activity credits;
- July 1, 2016: Sustainable Communities and Research and Development credits; and
- July 1, 2017: Businesses That Create New Jobs, Biotechnology Investment, and Wineries/Vineyards credits.

In lieu of the evaluation dates listed above, if a tax credit has a termination date provided for by law, an evaluation of that credit must be made on or before July 1 of the year preceding the calendar year of the termination date.

Department of Legislative Services' Evaluation

By June 30 of the year prior to a tax credit's evaluation date, the evaluation committee is required to meet with the Comptroller's Office, DBM, DLS, and the agency that administers the credit to prepare a plan for evaluation. By October 31 of the same year, DLS is required to publish a report evaluating the tax credit.

The report submitted by DLS must discuss:

- the purpose for which the tax credit was established;
- whether the original intent of the tax credit is still appropriate;
- whether the tax credit is meeting its objectives;
- whether the goals of the tax credit could be more effectively carried out by other means; and
- the cost of the tax credit to the State and local governments.

By December 14 of the same year, the evaluation committee must hold a public hearing on the evaluation report. By the twentieth day of the legislative session before the evaluation date of a tax credit, the committee is required to submit a report to the General Assembly that states whether or not the tax credit should be continued, with or without changes, or terminated.

Enterprise Zone Tax Credit

Background

Enterprise zones were first proposed and implemented in the late 1970s and early 1980s in the United Kingdom as an alternative to more traditional urban redevelopment programs and policies. The proposed purpose of these enterprise zones was to encourage industrial and commercial activity by promoting the development of damaged or vacant land. In the United States, according to a study conducted in 1988 by the U.S. General Accounting Office (GAO), "proposed and actual enterprise zone programs typically have two objectives: the revitalization of depressed urban or rural areas and the creation of jobs." The GAO study further states that "the philosophy behind the enterprise zone concept is simple: reducing governmental burdens on industry in targeted areas encourages private investment and growth there."

In the early 1980s, New York State Representatives Jack Kemp and Robert Garcia proposed federal enterprise zone legislation that later gained the support of the Reagan Administration as an urban revitalization tool. The initial proposals included a series of tax benefits for businesses located and locating in an enterprise zone. However, the initial federal legislation enacted at the time did not provide specific tax benefits, but rather allowed designated enterprise zones increased access to federal grant programs. At the time, no Maryland jurisdictions applied for this federal program. In the 1990s, the federal Enterprise Zone program was revised under the Empowerment Zone and Enterprise Community Program to include a package of tax benefits, federal financing assistance, and certain block grants.

Maryland was one of the first states to establish an Enterprise Zone program. Chapter 789 of 1981 authorized the establishment of enterprise zones in Maryland contingent upon federal Enterprise Zone legislation. Chapter 298 of 1982 repealed this contingency and created an Enterprise Zone program in Maryland to encourage businesses to locate in economically distressed areas and to hire residents from those areas. Chapter 298 established enterprise zone eligibility criteria and provided for special property tax and income tax credits for eligible businesses located in enterprise zones. The legislation also authorized loans to eligible businesses under the Maryland Industrial Land Act as well as grants and loans from the Maryland Industrial and Commercial Redevelopment Fund, and low-cost loan guarantees from the Enterprise Zone Venture Capital Guarantee Fund. In December 1982, the State designated its first four enterprise zones – Park Circle Industrial Park in Baltimore City as well as areas in Cumberland, Hagerstown, and Capital Heights in Prince George’s County.

As of September 2013, there are 30 enterprise zones in 12 counties and Baltimore City, as shown in **Exhibit 1.2**. Chapter 467 of 1999 expanded the State’s Enterprise Zone program to include a focus area tax credit in order to increase the amount of Enterprise Zone tax credits for businesses in particularly distressed parts of an enterprise zone. The Baltimore City and Prince George’s zones are the only zones which currently have focus areas.

Exhibit 1.2
Number and Size of Enterprise Zones by County
Calendar 2000 and 2013

	Enterprise Zones: 2000		Enterprise Zones: 2013	
	<u>Number</u>	<u>Acreage</u>	<u>Number</u>	<u>Acreage</u>
Allegany	4	7,833	3	8,438
Anne Arundel	0	0	0	0
Baltimore City	5	9,557	1	13,453
Baltimore	3	5,563	3	5,520
Calvert	1	253	0	0
Caroline	0	0	0	0
Carroll	0	0	0	0
Cecil	1	1,989	1	4,334
Charles	0	0	0	0
Dorchester	2	1,516	2	2,319
Frederick	0	0	0	0
Garrett	3	436	3	634
Harford	2	10,502	2	12,857
Howard	0	0	0	0
Kent	0	0	0	0
Montgomery	2	872	4	1,135
Prince George's	1	6,625	1	7,275
Queen Anne's	0	0	0	0
St. Mary's	1	3,155	0	0
Somerset	2	1,402	2	1,588
Talbot	0	0	0	0
Washington	4	6,104	3	6,637
Wicomico	2	2,985	2	4,353
Worcester	3	2,412	3	2,293
Total	36	61,204	30	70,836

Source: Department of Business and Economic Development; Department of Legislative Services

Designation of Enterprise Zones

State Standards

Section 5-704 of the Economic Development Article outlines the statutory requirements for obtaining an enterprise zone designation. In order to qualify as an enterprise zone, a political subdivision must first apply to the Secretary of Business and Economic Development for an enterprise zone designation. The Secretary may only designate an area as an enterprise zone if it is in a priority funding area (PFA) and satisfies one of the following criteria:

- for the most recent 18-month period, the average unemployment rate for the area is at least 150% of the average for the State or the United States (whichever is greater);
- the population in the area, or within a reasonable proximity to the area but in the same county, qualifies the area as a low-income poverty area;
- at least 70% of the families in the area, or within a reasonable proximity to the area but in the same county, have incomes that are less than 80% of the median family income of the political subdivision where the area is located; or
- the population in the area, or within a reasonable proximity to the area but in the same county, decreased by 10% between the most recent two censuses, and the political subdivision can demonstrate to the Secretary's satisfaction that (1) chronic abandonment or demolition of property is occurring in the area or (2) substantial property tax arrearages exist in the area.

The 1997 Priority Funding Areas Act directs State funding for growth-related infrastructure to PFAs, providing a geographic focus for State investment in growth. PFAs are existing communities and places where local governments want State funding for future growth. Growth-related projects include most State programs that encourage growth and development such as highways, sewer and water construction, economic development assistance, and State leases or construction of new office facilities. The Act legislatively designated certain areas as PFAs – municipalities (as they existed on January 1, 1997), Baltimore City, areas inside the Baltimore and Capital beltways, the Department of Housing and Community Development designated neighborhoods – and established criteria for locally designated PFAs. The criteria include permitted density, water and sewer availability, and designation as a growth area in the jurisdiction's comprehensive plan. A PFA also includes an area designated as an enterprise zone or an empowerment zone or enterprise community by the federal government.

The Secretary of Business and Economic Development 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. While State law limits the number of enterprise zones the Secretary may designate within a calendar year, Chapter 173 of 2006 granted the Secretary the authority to approve the expansion of an

existing enterprise zone by up to 50% in size without the expansion counting toward the statutory limit. State law limits the number of enterprise zones the Secretary may designate annually to six enterprise zones and one extraordinary expansion. A county may not receive more than two enterprise zone designations in a calendar year. At any time, a political subdivision may reapply to the Secretary to designate another area as an enterprise zone. Pursuant to Chapter 362 of 2006, any business located in a State enterprise zone may apply to obtain the Enterprise Zone tax credit for an additional five years following the enterprise zone's expiration.

Local Standards

In addition to the State standards that a business entity must meet to participate in the Enterprise Zone program, each political subdivision is authorized to establish additional local standards to govern access to the program. Each zone has a local administrator who determines if a business entity meets the required local standards. These additional local standards generally require a minimum capital investment or a minimum number of jobs created, or both. A few enterprise zones have additional standards limiting the type or category of business entity that is eligible to participate. **Appendices 1 and 2** identify the local standards that apply in each enterprise zone.

Focus Areas

Chapter 467 of 1999 provided additional incentives for businesses located in designated focus areas within enterprise zones. A focus area is an area located in an enterprise zone that meets at least three of the following criteria: (1) for the most recent 18-month period, the average unemployment rate for the area is at least 150% of the average for the State or the United States (whichever is greater); (2) the incidence of poverty for the population in the area is 150% of the national average; (3) the crime rate in the area is at least 150% of the crime rate in the political subdivision; (4) the percentage of substandard housing is at least 200% of the percentage of housing units in the State that is substandard; or (5) the percentage of square footage of vacant commercial property in the area is at least 20%.

Enterprise Zone Property Tax Credit

Businesses located or locating in an enterprise zone may receive a 10-year property tax credit against local real property taxes. The amount of the property tax credit is based on a specified percentage of assessment increases resulting from the value of real property improvements. As shown in **Exhibit 1.3**, the credit is applied to the tax imposed on 80% of the eligible assessment during the first five years, and decreases by 10% annually to 30% in the final year. Within a focus area, a business can receive the 80% credit for the full 10-year period. In addition, businesses in a focus area may be eligible for a 10-year, 80% tax credit against local personal property taxes on new investment. During the course of the property tax credit period, the State Department of Assessments and Taxation (SDAT) is responsible for reimbursing local

governments (through the department's annual general fund budget) for 50% of the property tax revenue lost as a result of the credit.

Exhibit 1.3
Enterprise Zone Property Tax Credit
Percentage of Eligible Property Assessment

<u>Taxable Year</u>	<u>Percentage</u>
1-5	80%
6	70%
7	60%
8	50%
9	40%
10	30%

Source: Department of Legislative Services

In order to obtain the property tax credit, a business located within a designated enterprise zone must contact the local enterprise zone administrator to determine whether a particular property meets specific requirements within a given enterprise zone. While State law indicates that businesses may qualify for the credit by making capital improvements or hiring new employees, local enterprise zones may establish additional requirements (*e.g.*, qualifying businesses must hire a certain number of new employees or that the jobs created must be in certain industries). Following a determination by the local administrator that a property qualifies for the credit, the administrator certifies this finding in writing to SDAT. SDAT will then calculate the amount of the assessment that is eligible to receive the credit. In addition to computing the amount of the eligible property assessment, SDAT is required to keep track of each property that has been certified by the local enterprise zone administrator and notify each local jurisdiction of its property tax credit obligation. It should be noted that the credit is granted to the owner of the qualifying property. In cases where a lessee makes the capital improvements, the lessee is responsible for executing an agreement with the owner of the property regarding the receipt of the property tax credit.

Enterprise Zone Income Tax Credit

There are two types of income tax credits for firms located within an enterprise zone: a general income tax credit and a larger income tax credit for hiring economically disadvantaged employees. As shown in **Exhibit 1.4**, the general income tax credit is a one-time \$1,000 credit per new employee filling a newly created position, or \$1,500 for each qualified new employee in a focus area. For economically disadvantaged employees, the credit increases to a total of

\$6,000 per new employee, or \$9,000 per new employee in a focus area. The tax credit for economically disadvantaged employees is claimed over a three-year period.

Exhibit 1.4
Enterprise Zone and Focus Area
Income Tax Credit

Enterprise Zone

Regular employee	\$1,000 per employee (one-time)
Economically disadvantaged employee	\$6,000 per employee (over three years)

Focus Area

Regular employee	\$1,500 per employee (one-time)
Economically disadvantaged employee	\$9,000 per employee (over three years)

Source: Department of Business and Economic Development

Similar to the property tax credit, businesses located in an enterprise zone must be certified by the local enterprise zone administrator in order to be eligible to receive the income tax credit (including the focus area credit). To qualify for the credit, businesses must hire at least one employee who (1) is hired after the business was located in the enterprise zone or after the enterprise zone was designated; (2) is employed by the business for at least 35 hours per week for 6 months (or 12 months in a focus area) before or during the taxable year in which the credit is taken; (3) spends at least 50% of the workday either in the enterprise zone or on an activity related to the enterprise zone; (4) is hired to fill a new position (*i.e.*, the firm's number of new full-time positions must increase by the number of credits taken); and (5) earns at least 150% of the federal minimum wage. Businesses claiming the credit for hiring an economically disadvantaged employee must obtain certification from the Department of Labor, Licensing, and Regulation. Once certified, a business may claim the income tax credit.

Studies of Maryland's Enterprise Zone Credit

In 1988, GAO undertook a study of state Enterprise Zone programs. The study focused primarily on Maryland's Enterprise Zone program due to its similarity to previously proposed federal legislation. GAO examined economic and employment data from the Cumberland, Hagerstown, and Salisbury enterprise zones. The study concluded that, generally, "the Maryland program did not stimulate local economic growth as measured by employment or strongly influence most employers' decisions about business location."

Chapter 467 of 1999 established an Enterprise Zone Task Force to study the effectiveness of the State's Enterprise Zone program and how it compares to programs in other states. The task force met during the 1999 interim and submitted a report to the Governor in December 1999. The task force "found insufficient data at either the State or county level to reach an empirical conclusion as to the effectiveness of the Enterprise Zone Program." The task force made six recommendations focused on increased incentives, additional State and local coordination and cooperation, and additional program accountability.

Chapter 464 of 2000 established a Task Force to Study the Maryland Enterprise Zone program. The task force was required to study further enhancements to the State's Enterprise Zone program including (1) allowing local authority to grant real estate credits for converting vacant commercial property to residential use; (2) the feasibility of State agencies favoring enterprise zones in the delivery of services; and (3) examination of other states' Enterprise Zone incentives. The task force made several recommendations including increased income tax credits, increased hourly wages (150% of the federal minimum wage) in order to qualify for the income tax credits, and increased hourly work requirements, as well as administrative issues to be addressed by the Department of Business and Economic Development and the Department of Housing and Community Development, including the submission of an annual report on the status of the State's Enterprise Zone program.

Similar Credits in Other States

Most of Maryland's nearby states have some form of enterprise zone or economic development zone tax credit to encourage businesses to locate in economically distressed areas. It is worth noting that most of the credits in these states are claimed against the income tax, while Maryland's credit is primarily taken as a property tax credit.

Delaware

Delaware maintains an Enterprise Zone credit program in which a business is eligible for a credit of \$750 for each new employee hired and each \$100,000 invested in a new or expanding facility in a targeted area. A targeted area is a census tract targeted for economic development based on the following criteria: percent of persons below poverty level; percent of households receiving public assistance; unemployment rate; median household income; significant presence of vacant property within the target area; character of the community; and population. In addition, a business may qualify if its real property is owned by the State, a nonprofit organization, or if it is within a federally approved foreign trade zone. The credit may be taken against the corporate or personal income tax, and any unused credit may be carried forward 10 years.

District of Columbia

The District of Columbia provides an Economic Development Zone tax credit, which offers a credit to businesses equal to 50% of the wages to certain employees during their first 24 months of employment, not to exceed \$7,500 per qualifying employee in each taxable year.

Generally, an eligible zone is one in which the:

- unemployment rate is at least 150% of the average in the district;
- family poverty rate is at least 20%; or
- income of 70% of the residents of the area is not more than 80% of the median income of district residents.

A qualifying employee must be a district resident with an annual income of no more than 150% of the lower living standard income level, as defined by federal law, for the 12 months immediately preceding the beginning of employment. The credit may be carried forward for five years. Currently, the credit is in abeyance until permitted by the federal government.

New Jersey

New Jersey has multiple tax incentives available to encourage employment and business growth in qualifying areas.

Under New Jersey's "Qualified Municipality Open for Business Incentive Program," businesses locating or expanding in a qualified municipality are eligible for a credit against their corporation business tax or the tax on insurers. The program offers a \$2,500 tax credit for each new full-time position in credit year one and \$1,250 for each new full-time position in credit year two. The credit may be carried forward for five years. Currently, the City of Camden is the only qualified municipality. A qualified municipality is one that:

- has been subject to the supervision of a financial review for at least one year;
- has been subject to the supervision of the Local Finance Board for at least one year; and
- is dependent upon state aid and other state revenues for not less than 55% of its total budget.

New Jersey also maintains an Urban Enterprise Zone program. For each new full-time permanent employee who is a resident of a qualifying municipality in which the enterprise zone is located, a certified qualified business may receive a one-time credit of \$1,500. A qualifying zone is one which, for the last full year prior, had an annual average of at least 2,000 unemployed persons and in which the municipal average annual unemployment rate for that year exceeded the state average annual unemployment rate. The employee must have been unemployed for at least 90 days or relied on public assistance as the employee's primary source

of income; otherwise, the one-time credit is \$500. The employee must be employed for at least six months for the business to be eligible.

New Jersey has considered eliminating its Urban Enterprise Zone Program since at least 2009. The state hired independent consultants that completed a study analyzing the effectiveness of the program. The study concluded that the program delivered a limited economic impact on the zones, and that it produced a negative return on state investment. Specifically, the study found only \$0.08 in new state and local revenue were generated per \$1 of state funding investment and only \$0.83 in “ripple effect” economic activity was generated per \$1 of state funding investment.

Additionally, New Jersey operates a credit for businesses operating at a location within a project associated with the New Jersey Urban Development Corporation in a qualified municipality. A qualified municipality must be eligible to receive state aid and also meet certain population and aid requirements. The program provides a credit against the corporation business tax in the amount of \$1,500 for each new employee for each of two years. The employee must be a resident of the qualified municipality and who immediately prior to employment was either unemployed for at least 90 days or for whom public assistance was the person’s primary source of income. The employee must be employed for at least six months for the business to be eligible.

Pennsylvania

Pennsylvania provides a tax credit for businesses generating employment in Keystone Opportunity Zones or Expansion Zones. The tax credit is \$1,250 per job, and the total value of the job credits for any year may not exceed \$1 million. The job credit is to be prorated if the total value exceeds this amount. The credit may not be carried forward.

For an area to qualify for designation as a Keystone Opportunity Zone or a Keystone Opportunity Expansion Zone, the area must meet two of the following criteria:

- at least 20% of the population is below the poverty level;
- the unemployment rate is 1.25 times the statewide average;
- at least 20% of all occupied housing within a certain radius of the proposed zone is deteriorated;
- the median family income is 80% or less of the urban median family income for that metropolitan statistical area; or for a nonurban area, of the statewide nonurban median family income;
- the population loss exceeds 10% in an area which includes the proposed zone, but is not larger than the county or counties in which the proposed zone is located, based on census data between 1980 and 1990, or census estimates since 1990 establishing a pattern of population loss;

- the political subdivision in which the proposed zone is located has experienced a sudden and/or severe job loss;
- at least 33% of the real property in the proposed zone in a nonurban area would otherwise remain undeveloped or nonperforming due to physical characteristics of the real property; and
- the area has substantial real property with adequate infrastructure and energy to support new or expanded development.

Pennsylvania also offers a Neighborhood Assistance Enterprise Zone Program credit, which provides a tax credit of up to 25% of the qualified investment or up to 35% of the qualified investment in a special program designated by the Department of Community and Economic Development. An enterprise zone is one in an “impoverished area,” which has a high incidence of unemployment, underemployment, residents receiving public assistance, crime and delinquency, infant mortality, school dropouts, “or other evidence of low educational attainment”; or overcrowded, unsanitary, or inadequate housing. The credit may be carried forward for up to five years. The total amount of tax credits granted may not exceed \$18 million in any fiscal year.

Virginia

Virginia offers a tax credit for businesses creating employment in an economically depressed area. An economically depressed area is a county or city with an unemployment rate for the preceding year at least 0.5% higher than the average statewide unemployment rate for that year or is an enterprise zone. The tax credit is capped at \$1,000 per qualified full-time employee. The credit may be carried forward for up to 10 taxable years.

Virginia also maintains an Enterprise Zone Grant Program, in which the Virginia Department of Housing and Community Development recommends an area to be an enterprise zone to the Governor, who may establish up to 30 enterprise zones for 10 years with two 5-year renewals. The department bases its recommendations upon economic distress factors within a county or city and a local government’s revitalization and development initiatives.

West Virginia

West Virginia does not appear to offer a comparable tax incentive program.

Recent Developments in Other States

In recent years, some states have completely eliminated or considered the elimination of their Enterprise Zone programs in favor of other economic development programs. On the other hand, some states have expanded their programs in recent years, extending zones and expanding eligibility.

California

Effective after 2013, California eliminated its existing Enterprise Zone program, replacing it with a new economic development program. California established three categories of incentives designed to encourage economic development in the state:

- A partial sales and use tax exemption for manufacturing and for companies that conduct certain types of research and development upon purchase of certain property.
- A hiring credit to allow some taxpayers located in specific enterprise zones and census tracts with high unemployment and poverty to claim a credit for hiring specific employees. The credit is only available for the hiring of new employees who are long-term unemployed, veterans, ex-felons, or recipients of the federal Earned Income tax credit or other similar assistance.
- The creation of a fund to negotiate agreements to provide tax credits for investments and employment expansion in California. The factors determining how much credit a taxpayer is allocated in a fiscal year includes the number of jobs created or retained; compensation levels paid to employees; investment amounts made in the state; levels of unemployment or poverty in the area where the business is located; other incentives available to the taxpayer; duration for which the taxpayer commits to remaining in the state; and the overall economic impact of the business and anticipated benefits to the state.

Kentucky

Kentucky decided to phase out its Enterprise Zone program by allowing for its enterprise zones to expire as of 2008. Legislation was introduced on multiple occasions to continue the program, including proposals to extend the expiration for those already receiving the credit, though these attempts were unsuccessful. A major criticism of the program was that data collected for evaluating the program was incomplete and did not allow for meaningful analysis of the program's effectiveness.

Louisiana

Louisiana's Enterprise Zone program provides income and franchise tax credits to businesses located in designated enterprise zones that create new jobs and hire at least 35% of their new jobs from one of four targeted groups based on residency within a zone, eligibility for public assistance, disability, or employability. Louisiana's program also provides sales tax exemptions for materials and equipment purchased and used on the zone site. In 2012, Louisiana provided approximately \$67 million in Enterprise Zone tax incentives, compared to \$91 million in 2011 and \$110 million in 2010.

Minnesota

Minnesota's JOBZ program is intended to increase employment and to attract and retain businesses in the state, but a 2008 study by the state's Program Evaluation Division found many problems with this program. The study found that "economic distress" was defined too broadly, allowing the majority of businesses in the state to be located in geographically eligible areas. Additionally, the study noted reporting deficiencies, concluding that at least one-third of businesses had not hired as many employees as they had certified. The study also found that only 5% of businesses receiving the credit had moved from out of state, and it concluded that since many businesses are competing against other businesses in the state, subsidizing those in areas of economic distress hurt businesses elsewhere in the state. Although the legislature did not act on most of the recommendations, the study highlighted important conclusions that can benefit other states.

North Carolina

In 2013, North Carolina's Department of Commerce released a report analyzing the effectiveness of the state's tax credits, including those related to economic development and job creation. The report concluded that most of the credits were ineffective and actually created a negative impact on the state's economy. As a result, the legislature implemented comprehensive tax reform in 2013, eliminating most of the state's tax credits.

Chapter 2. Objectives of Enterprise Zone Programs

Economic Revitalization and Job Creation

Enterprise Zone programs typically have two objectives: the revitalization of economically depressed areas and the creation of jobs. Maryland's Enterprise Zone program, established in 1982, includes these objectives and specifies that the program focus both local and State resources on achieving the objectives. Specifically, under COMAR 24.05.01:

The objective of the Enterprise Zones Program is to focus local and State resources on the encouragement of economic growth in economically distressed areas and employment of the chronically unemployed in the State.

In the subsequent three decades Maryland has made progress by many measures – education, economic growth, and the average well being of its residents. The Maryland economy in real terms is 2.4 times larger than it was in 1982 and the income of the typical household has increased by 22% to \$71,780, the highest in the nation. However, the progress has been uneven with a marked dissimilarity within economically distressed areas.

A number of academic studies have attempted to determine whether enterprise zones have been effective in achieving their objectives of promoting business development and job creation in economically distressed areas. These studies have reviewed the economic theory behind enterprise zones, how enterprise zone incentives factor into business location decisions, the impacts of incentives on residents, businesses, and property values within zones, and the costs of enterprise zone incentive programs. Despite the increased popularity of enterprise zones over time, these studies have not provided definitive evidence that enterprise zones achieve their stated goals of economic revitalization and job creation. **Appendix 3** provides a more detailed overview of some of the studies that have attempted to gauge the effectiveness of enterprise zone programs.

In addition, several states have recently evaluated their enterprise zone programs and determined that in most cases the program's impact on job creation and economic development have been overstated. **Exhibit 2.1** highlights the key findings of four recent state analyses of enterprise zone programs and whether the analysis found that job creation impacts had been overstated. The analyses found that the overestimation of jobs resulted from inaccurate or inadequate recordkeeping, and not taking into consideration jobs that would have been created without the incentive. Some states have found that only a small percentage of qualified businesses take advantage of enterprise zone programs, while other states have found that businesses that utilize the enterprise zone program do not generate much economic activity. Generally, states that have evaluated their enterprise zone programs have been skeptical of the economic activity claimed by program administrators.

Exhibit 2.1
Recent Evaluations of State Enterprise Zone Programs

<u>State</u>	<u>Economic Impact/Job Creation Issues</u>	<u>Key Findings</u>
MN	Actual increase in employment at JOBZ businesses was at least 20% less than the number of reported new jobs.	Two-thirds of JOBZ businesses would have expanded to some extent without JOBZ assistance. Program should be used more selectively.
LA	Job creation overstated by over 300% when taking into consideration jobs that would have occurred without the incentive and job losses from increased competition of EZ projects.	Over 95% of the value of EZ incentives has been provided to large businesses (more than 500 employees). Despite being one of the state's most active incentive programs, less than 1% of employers have historically accessed the program. Incentives provided to industries which are dependent on local demand (such as retail) do not increase jobs.
NJ	NJ collects EZ data from 6 different systems causing data to be incomplete and unreliable.	Only 20% of qualified businesses participate in the program. Every \$1.00 invested by the state in the program is estimated to generate around \$0.08 in new State and local tax revenue. Recommended program termination and replacing it with a new place-based community and economic development program.
PA	Job figures are self-reported and include anticipated jobs. Some businesses were double-counted and some job losses were not included.	Program lacked accountability and transparency. Three-quarters of program participants did not report any job creation activity and most businesses have generated little capital investment.

Source: Louisiana Economic Development Office; Minnesota Office of the Legislative Auditor; State of New Jersey Community Affairs; Pennsylvania Legislative Budget and Finance Committee

Chronic Unemployment Is Difficult to Measure

Economic and demographic data provide insight on Maryland's economically distressed areas and chronically unemployed individuals. Precise data, however, is not available on the "chronically unemployed." The chronically unemployed include the long-term unemployed; however, researchers differ over how long-term unemployment should be defined and precise geographic data is limited. The unemployment rate, including long-term unemployment, captures only those individuals actively looking for a job and who are therefore included in the labor force. In addition to the long-term unemployed, the chronically unemployed also include

discouraged workers who have left the labor force because they believe that there is little hope of finding a job. Accounting for these individuals requires using broader measures of labor utilization such as the labor-force participation rate, which measures the percentage of the civilian noninstitutional population age 16 or older that is employed or actively seeking employment. This measure includes those who are not in the labor force by choice (retired individuals, students, parents staying home to raise children). Many analysts, however, believe it more accurately measures the amount of underemployment in the economy. For example, labor force participation among prime-age men has fallen as employment prospects worsen due to a decreased demand for less-skilled workers.

It is also possible to identify areas within the State that are likely to have a large number of chronically unemployed and higher level of economic distress by other measures such as levels of poverty. Although some individuals who live in poverty are employed, it is a useful proxy for determining areas with high levels of economic distress and joblessness. As discussed below, areas of economic distress and high poverty are often concentrated and there is a strong correlation between economic distress, long-term joblessness, poverty, and other social ills.

Sources of Unemployment and Policy Implications

Unemployment that results from individuals who want to work but are unable to find a job is typically thought of within a supply and demand framework as an insufficient supply of jobs for the population seeking employment. This source of unemployment, which can measure the extent to which the economy is underperforming relative to its potential or the level of economic distress within an area, is referred to as cyclical unemployment. Another source of unemployment results not from an imbalance between the quantity of jobs and people seeking work but reflects structural problems within the labor market. This can result from a mismatch between the available jobs and individuals seeking employment. Firms may be hiring but cannot fill the positions due to a variety of factors including (1) the time that it takes workers to successfully search for jobs and (2) geographic, skill, and industry mismatches.

The source of the unemployment has important policy implications for policies that strive to increase employment through economic development, including the Enterprise Zone tax credit. If unemployment merely reflects an imbalance between the labor demand and supply, then policies that aim to stimulate business and job creation, such as the Enterprise Zone tax credit, will alleviate the unemployment if it is effective in increasing economic development and net employment within the distressed area. However, if the unemployment results from structural problems within the labor market, *i.e.* a mismatch between the skills employers need and those possessed by residents, policies designed to increase the total amount of jobs will not effectively decrease the target population unemployment. Active labor market policies such as job retraining and job search assistance, if well designed and implemented, might be more effective in addressing the problem of structural unemployment.

The long-standing debate over whether cyclical or structural unemployment is the most important factor in contributing to overall unemployment has intensified recently given the large and persistent increase in unemployment. Recent research by the U.S. Federal Reserve and

International Monetary Fund (IMF) examined the relative importance of cyclical and structural factors in explaining U.S. unemployment and identified the sources of structural unemployment.

The U.S. unemployment rate rose sharply during the recent recession, increasing from 4.4% in May 2007 to 10.1% in October of 2010 and was accompanied by a striking increase in the duration of unemployment. There was a disproportionate increase in unemployment among low-skilled workers; young workers; and in certain sectors including manufacturing, construction, and finance. As of August 2010, labor force participation was 64.7%, down from the pre-recession level of about 66%. This decline reflects a large-scale exit of workers from the labor force over the past few years. The labor force participation of men age 25 to 54 has also declined steadily in recent decades, albeit at a much slower rate than that of teenagers. At the end of 2009, it reached 88.9%, almost 9 percentage points below its peak in the mid-1950s. Many prime-age men who leave the labor force during downturns stay out even after the economy recovers, although not to the same extent as teenagers. Although the unemployment rate and duration of unemployment have subsequently improved, they have not returned to pre-recession levels, and the labor participation rate has not improved.

The U.S. Federal Reserve concluded that the severity and persistence of output declines was the dominant factor in pushing up unemployment, contributing to three-quarters of the increase in unemployment; structural factors contributed to the remaining one-quarter. The International Monetary Fund reached a similar conclusion, finding that structural factors might have raised the natural rate of unemployment by about one and a half percentage points since 2007. Although the research concluded that cyclical factors are responsible for a majority of the increase in the U.S. unemployment rate, it identified important sources of structural unemployment and variation in the importance among the population.

The Federal Reserve found that structural unemployment was a larger factor in explaining unemployment among the long-term unemployed. According to IMF, factors that cause structural unemployment include:

- a mismatch between the skills demanded by employers and the supply of residents;
- a variation in the demand for labor across industries, particularly if there is a sharp decrease in some industries and increased demand in other industries which require different skills; and
- other mismatches including the lack of geographic mobility in the labor force.

The recent recession caused a significant decline in employment within the manufacturing and construction sectors, as well as sectors of the financial industry. Yet demand for skilled labor within industries such as professional science and technical services, health care, and education remains relatively strong. This shift in the composition of labor demand requires a reallocation of labor; the speed at which this occurs depends on several factors, including the ability of workers to have the skills necessary in growth industries.

Poverty Is Often Concentrated and Persistent In Certain Areas

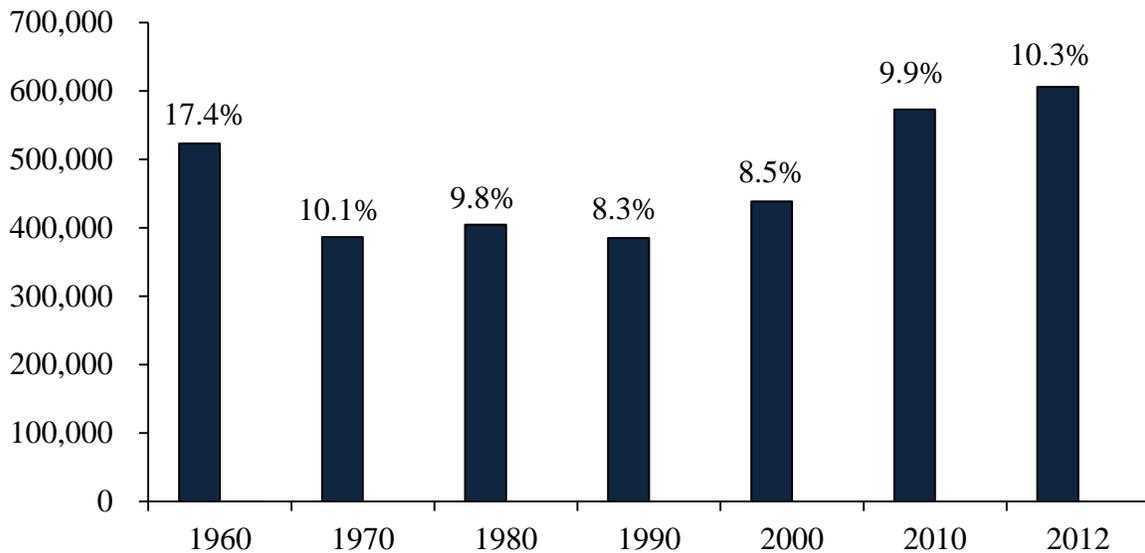
Research indicates that poverty is often concentrated and persistently present in many areas. People living in poverty tend to be clustered in certain neighborhoods rather than being evenly distributed across geographic areas. Concentrated poverty has been described as the coincidence of a number of social ills including poverty, joblessness, crime, depressed economic conditions, and low levels of skills in small geographic areas. Factors that have contributed to the concentration of poverty include the dramatic decline in blue-collar employment caused by de-industrialization, out-migration, and a growing mismatch between the educational levels of residents and the skill levels demanded in growth industries.

Persistent poverty is often associated with inner cities, but it is also a problem in many rural areas. According to recent research conducted by the Population Reference Bureau, metropolitan areas accounted for more than three-fourths of children living in persistently poor neighborhoods. However, children in rural (nonmetropolitan) counties were more likely to live in persistently poor neighborhoods (15%) than were their metropolitan counterparts (11%). In 2000, the study found that there were 8.3 million children living in persistently poor neighborhoods – defined as neighborhoods with poverty rates of at least 20% in 1980, 1990, and 2000. Moreover, a recent study conducted jointly by the U.S. Federal Reserve and the Brookings Institution found that poverty is spreading and may be re-clustering in suburbs, where a majority of America’s metropolitan poor now live.

The recent U.S. Federal Reserve and Brookings Institution study examined the challenges, trends, and impacts of concentrated poverty. The study stated that concentrated poverty presents some of the deepest economic and social challenges facing America today as concentrated poverty and joblessness exact a grave toll on people who continue to live in its midst and threatens to perpetuate disadvantage across generations. Other research indicates that children growing up in poor neighborhoods are at a higher risk of health problems, teen pregnancy, dropping out of school, and other social and economic problems than are children living in more affluent communities. Long-term joblessness is associated with deep, permanent reductions in future earnings as well as decreased mental and physical health. This body of research argues that concentrated poverty places additional burdens on poor families that live within them, beyond what the families’ own individual circumstances would dictate. In addition, concentrated poverty can have wider effects on surrounding areas that limit overall economic potential and social cohesion.

Exhibit 2.2 shows the number of Marylanders living in poverty and the poverty rate since 1960. After decreasing through the 1990s, poverty in Maryland has since increased in both absolute and percentage terms. This increase has been exacerbated by the recent economic recession.

Exhibit 2.2
Number and Percentage of Maryland
Residents Living in Poverty
1960-2012



Source: U.S. Census Bureau; Department of Legislative Services

Although concentrated poverty persists in Maryland, it is less prevalent in Maryland than in the rest of the nation. About 9% of Maryland's population lives in areas with poverty rates of 20% or more, compared with a little less than one-quarter nationally. In addition, the percentage of population living in poverty areas is lower in Maryland than in each surrounding state.

Numerous Business Incentives Are Designed to Encourage Development
In Economically Distressed Areas

The intent of the Enterprise Zone credit in promoting economic development and jobs within distressed areas of the State is still applicable today given (1) the economic and social consequences of concentrated areas of economic distress/poverty and long-term joblessness on both on individuals and the wider community and (2) that significant areas of the State continue to exhibit economic distress and joblessness.

The validity of the credit's intent and objectives must be viewed, however, with additional information in mind. The State and local jurisdictions have expanded the number of tax credits and incentives targeting job creation in and near economically distressed areas. The Enterprise Zone program established the first State business tax credit in 1982; since that time the State has created almost 30 additional business tax credits. Though the intent of the Enterprise Zone program remains valid, numerous State, federal, and local programs with a

similar focus and objective have been enacted since the program's inception. The State has subsequently enacted numerous incentives that aim to increase employment or economic development within distressed areas or similar areas to enterprise zones including the One Maryland and Job Creation tax credits, the Base Realignment and Closure (BRAC) revitalization incentive program, Brownfields tax credit, Community Investment tax credit, and Sustainable Communities Rehabilitation tax credit. Of the current business tax credits, about one-quarter are employment tax credits and one-half are related to economic development.

In addition to these tax credits, State business assistance programs with similar objectives include:

- *Maryland Economic Development Assistance Authority and Fund:* MEDAAF was established by the General Assembly under Chapter 301 of 1999 as a revolving loan fund. The fund provides below market, fixed-rate financing in the form of loans, grants, conditional loans, conditional grants, and direct investment to local jurisdictions and businesses.
- *Economic Development Opportunities Program Fund (Sunny Day):* This program provides conditional loans and investments to take advantage of extraordinary economic development opportunities, defined in part as those situations which create or retain substantial numbers of jobs and where considerable private investment is leveraged.
- *Maryland Economic Development Corporation:* MEDCO is a nonbudgeted entity that allows the State to own or develop property for economic development purposes. MEDCO was created in 1984 with the mission to help expand, modernize, and retain existing Maryland business and to attract new business to the State.

One of the objectives of the Enterprise Zone tax credit is to boost unemployment of the long-term unemployed. In addition, jurisdictions seeking designation of a zone must meet at least one of four criteria. Three of these criteria – number of low-income households, unemployment, and poverty – overlap with the objectives and impacts of the federal and State Earned Income Credits (EIC). The federal EIC was enacted in 1975; however, the program has been expanded significantly since enactment of the State Enterprise Zone program. In addition, the State has enacted an Earned Income Credit (1987), Refundable Earned Income Credit (1998), and Poverty Level Credit (1998). Most researchers agree that Earned Income Credit programs have successfully reduced poverty and increased labor force participation and employment of low-income individuals by incentivizing work.

Numerous federal and local economic development programs have also been enacted. Local governments have established and expanded the use of financial assistance, job creation and economic development tax credits, tax increment financing (TIFs), payment-in-lieu-of tax agreements (PILOTs), and special taxing districts in order to subsidize infrastructure and development within targeted areas. The federal government has established and expanded numerous business financial assistance, loan, and job training programs.

Several federal programs have significant overlap with the State's Enterprise Zone Program, including the Empowerment Zone and Enterprise Community Program. The Baltimore Empowerment Zone extends over 6.8 square miles, covering three separate areas of east, west, and south Baltimore, and containing over 50,000 people and 2,000 businesses. Benefits include federal employment tax credits. Other federal programs with similar business utilization include the New Markets Tax Credit, employment tax credits, and historic rehabilitation tax credits.

Targeted Business Incentives May Not Increase Net Employment in Economically Distressed Areas

An assumption of the credit is that promoting economic development within distressed areas will benefit residents and also boost employment of the chronically unemployed. This linkage crucially depends on the nature and causes of chronic unemployment. Although the intent of promoting economic development is a valid one, it is not clear if the existing Enterprise Zone credit is the most effective approach to increasing overall *net* economic development and employment. Academic and other research has raised significant questions as to whether tax credits, and state and federal Enterprise Zone programs specifically, are effective in promoting economic development and increased employment. In addition, research has also indicated that within smaller geographies (county-to-county versus across the U.S.) tax incentives are generally more effective. This research indicates that, to the extent Enterprise Zone tax credits are effective, they are more likely to redistribute economic activity within Maryland. Given the intent is to promote economic development within distressed areas, the State as a matter of policy may accept this redistribution in order to assist distressed areas.

Chapter 3. Evaluating Maryland's Enterprise Zones

Overview

Analyzing the true economic impact of a tax credit requires isolating the impact of the credit from other factors that influence the business undertaking the qualifying activity. This approach will provide an estimate of how much economic activity resulted solely from the credit and was not due to other factors or that would have occurred even without receipt of the tax credit. An additional step requires an estimate of the net impact to State revenues – the cost of foregone revenue plus any additional State revenue that was generated by economic activity that would not have occurred without the credit. Since the Governor is required to submit a balanced budget every year, revenue that is foregone under the credit requires either a corresponding reduction in State spending or an increase in revenue from individuals or businesses, both of which dampen economic activity. Lastly, any spillover impacts should be captured. Positive spillover impacts include a business using the reduction in taxes to increase production and purchase additional goods from Maryland businesses. Conversely, a negative spillover impact includes the competitive advantage conferred to businesses that receive tax credits. An increase in sales and jobs at these businesses might be at the expense of sales and jobs at other businesses that do not receive the tax benefit.

Enterprise Zone Data Limitations Make Precise Evaluations Difficult

Local governments, with Department of Business and Economic Development (DBED) approval, establish enterprise zone boundaries that generally do not correspond to geographic areas with readily available data, such as defined geographies within the U.S. Census Bureau. Due to data limitations, boundary data were not available before 2000; the Department of Legislative Services (DLS) was only able to review a sample of 2000, 2007, and 2013 boundary data due to the amount of work required by DBED and the Department of Information Technology to collect the information. The boundary data were paired with data from the State Department of Assessments and Taxation (SDAT) containing business locations, U.S. Census Bureau data, and information from the National Employment-Time Series Database in order to identify businesses within enterprise zones. This identification and data analysis was generally precise, with the outer limit of accuracy at the block level within U.S. Census Bureau data.

This data provided information about all businesses within enterprise zones, including information detailing the extent to which enterprise zone workers live in enterprise zone communities and demographic information about those workers, including education levels. The nature of aggregated information at the U.S. Census Bureau and a delay in DLS receiving data from SDAT limited the ability to analyze only those businesses claiming the credit. However, the intent of the Enterprise Zone tax credit is to promote economic development and employment of the chronically unemployed (in totality) within the enterprise zone and community, not just that related to businesses claiming the credit.

In order to assess the effectiveness of the program, DLS uses two geographies referred to as the enterprise zone and enterprise zone community. The enterprise zone is the exact boundary of the zone and is used to assess business activity in the zone. When applying to establish or expand an enterprise zone, local jurisdictions are required to submit data providing evidence that the proposed zone meets statutory requirements, including that the area or area within reasonable proximity to the proposed zone but still within the same county meets at least one criterion related to poverty, low-income households, population loss, or unemployment. Unless the Secretary of Business and Economic Development approves another source of data, local jurisdictions are generally required to use U.S. Census Bureau American Community Survey five-year estimates or unemployment data from the Department of Labor, Licensing, and Regulation.

The geography of an enterprise zone community does not correspond exactly to the enterprise zone, primarily because enterprise zones are usually only parts of a county or municipality. The economic distress of these communities, however, is used to justify the creation of the zones and subsequent tax credit benefits. DLS uses the community geography to assess the level of economic distress within communities, social and economic changes over time, and the impact of the zones on chronically unemployed individuals. These geographies are defined by linking the enterprise zone boundaries to the most appropriate census geography – municipalities, census designated places (CDPs) for unincorporated jurisdictions, or census tracts. In addition, the populations of enterprise zone communities ranged from small towns and rural areas (13 had a population of less than 5,000) to urban areas such as Baltimore City (620,200) and Gaithersburg (59,000). Population size influences the accuracy of U.S. Census data as well as the ability to accurately limit census geographies to enterprise zones. For instances in which there was not a clear census geography, DLS calculated multiple geographies to assess accuracy and consistency, and where appropriate, selected the most precise geography. Data were limited for the Rt. 220 enterprise zone in Allegany County, Central Industrial and Keyser's Ridge enterprise zones in Garrett County, Glenmont enterprise zone in Montgomery County, and the Prince George's County enterprise zone.

DBED and the Comptroller's Office Do Not Assess the Effectiveness of the Enterprise Zone Tax Credit

Section 5-709 of the Economic Development Article requires DBED and the Comptroller's Office to annually assess the effectiveness of tax credits provided to businesses in enterprise zones, including the number and amount of credits granted and the success of the tax credits in attracting and retaining businesses within enterprise zones. While DBED tracks the number and amount of credits granted annually, it fails to assess the effectiveness of the tax credits. DBED does not have a framework for measuring success (or failure), and it considers every business that claims an Enterprise Zone credit a success. Various studies, like the GAO study referenced in this report, have shown that many businesses would have increased their economic activity even without the Enterprise Zone incentives.

DBED does not have reliable data on the number of jobs created as a result of the Enterprise Zone program. DBED has produced an estimate in recent annual reports; however, this data is collected from local zone administrators and is based on the companies which choose to report the data. This estimate is not accurate for two reasons: (1) it does not include some of the companies that claim the credit and (2) it does not include businesses that are not claiming the credit. In addition, DBED does not verify that the data provided by local administrators is accurate; it is also not clear the extent to which local administrators verify the company-reported information. DBED acknowledges these shortcomings in the annual report by stating "it is difficult to compare information on the amount of investment or jobs on a year-to-year basis because the information is, in any year, only reflective of the businesses that provided information to the enterprise zone administrators and does not reflect the activity of all of the businesses in the zones."

DLS examined some local administrator reports and found the data problematic. Some of the reports did not accurately measure employment at the business location within a zone and instead included employment by the business at other locations in the State. In addition, businesses appear more likely to report in years in which employment increased. For example, the Baltimore Development Corporation estimated that the number of jobs within the Baltimore City enterprise zone increased by 3,591 in 2010. However, about 880 of those jobs or one-quarter of the total increase was incorrectly attributed to a single dining establishment within the zone. In another instance, within a seven-year period one company reported job increases in five of those years but did not report in the two years in which employment decreased. As a result the reported data shows that the company increased employment by 487 jobs in the seven-year period; however, the company actually decreased employment by 281 jobs. Additionally, some of the new jobs being credited to the Enterprise Zone credit are also being credited to other incentive programs, like the One Maryland and Job Creation tax credits. By not acknowledging how these other programs have influenced job creation within enterprise zones, DBED overstates the impact of the Enterprise Zone credit.

While DBED assumes that all business activity for a business claiming the Enterprise Zone tax credit is a result of the Enterprise Zone incentives, therefore making the credit a success, it does not appear that DBED has carefully examined the data to see what percentage of business activity is actually attributable to the credit. While DBED assumes that 100% of new jobs are attributable to the Enterprise Zone credit, research suggests that a much lower percentage should be attributable to the credit.

There Have Been Recent Errors In the Administration of the Baltimore City Enterprise Zone Property Tax Credit

Local enterprise zone administrators certify eligibility for the Enterprise Zone property and income tax credits. SDAT oversees the administration of property assessments in the State, as well as administering or assisting counties in the calculation of several property tax credits and exemptions. These programs include the Enterprise Zone property tax credit as well as the Homeowners' and Renters' tax credits and the Homestead tax credit; in addition, SDAT

calculates the components of tax credits under local property tax credit programs including the Baltimore City Historic Restoration and Rehabilitation property tax credit and the Brownfields property tax credit.

Recent press reports stated that there have been errors in credits granted under the Baltimore City Historic Restoration and Rehabilitation property tax credit, the Homestead tax credit, and the Enterprise Zone property tax credit. At the request of the General Assembly's Joint Audit Committee, the Office of Legislative Audits (OLA) recently conducted a performance audit of the Homestead property tax credit. One of the audit's findings was that SDAT should improve its processes to ensure that only eligible properties receive the credit, as OLA determined that a significant number of properties were receiving the credit improperly.

Recent press reports documented that \$700,000 in improper Enterprise Zone property tax credits were granted to properties located in Baltimore City. Errors including granting the credit to ineligible properties, using incorrect pre-improvement base year assessments, applying the incorrect credit percentage, and not using the current year assessment in cases where the property owner successfully appealed for a lower assessment.

According to SDAT, its local assessment supervisors calculate the components of the Enterprise Zone property tax credits using one of the agency's systems. This information is sent to SDAT's central office where it is reviewed by the deputy director. In Baltimore City, the final credit component determination in each year is calculated within a spreadsheet where information is manually entered in each year. DLS requested that SDAT provide this data as part of its analysis of the Enterprise Zone program. SDAT was unable to complete the request in a timely manner nor was it able to fully provide all of the requested data. DLS previously requested this data in 2011 and SDAT was able to provide data on fiscal 2012 reimbursements. However, the data was unusable due to discrepancies between the local supervisor data and the final credit determination for Baltimore City – only about one-half of the total eligible assessed values matched in each case. In other instances a business was reflected on one set of data but not the other, or the business was on both but there were discrepancies between the two data sets.

Enterprise Zone Property Tax Credit Data Provided by SDAT Was Inaccurate or Incomplete

SDAT provided DLS a summary report of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone. The summary report lists the account number, owner, beginning date, year number, eligible assessment, base year assessment, credit percentage, and credit amount for a tax credit recipient. The computation worksheet lists the owner, address, property location, type of building, the first taxable year the property will receive the credit, the base year, county, enterprise zone, zone administrator and telephone number, account number, calendar year the property is first qualified, and the last taxable year the property can receive the credit. It also provides the current assessment, the base

year assessment, the percentage of the assessed improvements eligible for the credit, and the assessment subject to the tax credit for the 10 years that the recipient is eligible for the credit.

While this data should be sufficient to evaluate the Enterprise Zone property tax credit, the data that SDAT provided DLS was both incomplete and inaccurate. Additionally, although SDAT has data for the fiscal 2014 assessments, it only provided DLS with fiscal 2013 assessment data.

For fiscal 2013, DLS did not receive an enterprise zone summary report for six of the counties with zones (Calvert, Cecil, Garrett, Prince George's, St. Mary's, and Washington). DLS received a summary report for five of the counties (Allegany, Dorchester, Montgomery, Wicomico, and Worcester), but received no computation worksheets for the businesses receiving credits. Harford County provided an Excel spreadsheet which contained data consisting of the summary report. DLS received both a summary report and computation worksheets on the businesses claiming credits from only three jurisdictions (Baltimore City, Baltimore County, and Somerset County).

Some of the summary reports did not clearly indicate where the property was located. Several of the computation worksheets did not list the enterprise zone, while others incorrectly misclassified the enterprise zones. For instance, the data from Montgomery County erroneously lists Bethesda as an enterprise zone. Similarly, the Worcester County report lists an arts and entertainment district enterprise zone, but there is no enterprise zone in Worcester County designated as such. Additionally, many local assessment supervisors only provided partial addresses for Enterprise Zone properties that were eligible for the credit, or provided no address at all. SDAT uses the account number of a business to identify its address. While SDAT does not have an issue locating a business using account numbers, it creates a huge administrative burden for DLS to look up addresses on SDAT's website using account numbers.

The overall quality of the tax credit data provided ranged from relatively accurate to clearly flawed. Errors included incorrect base year assessments, using the wrong percentage of the eligible assessment to calculate the credit, and basic data entry errors. Despite errors, some counties provided useful information. In Cecil County, for example, the local assessment supervisor made relatively minor errors in calculating the credit over a 9-year instead of a 10-year period. Even with these errors, Cecil County did a good job of providing complete addresses of the Enterprise Zone properties. It also noted why there were changes in some of the base year assessments, such as revisions to reflect acreage changes. Washington County's report was one of the few that provided mailing and physical addresses, and the local zone administrator was thorough in noting six properties that were vacant and therefore ineligible to receive the credit.

The methodology and processes used for reporting data is generally unsophisticated and often necessitates the manual entry of information. Calvert County hand-wrote the assessment and base year assessment values, along with the assessment value subject to the credit. Meanwhile, Wicomico County faxed its summary report to SDAT. Baltimore City uses Excel spreadsheets to determine the assessment eligible for the Enterprise Zone property tax credit.

Using Excel eliminates the manual entry of information, thus making the process faster and more efficient. However, DLS questions whether there is a more sophisticated system that can easily track the Enterprise Zone data.

The summary reports of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone did not match the aggregate data that SDAT provided. With such disparities in the data, it was impossible for DLS to determine if SDAT correctly calculated the State's reimbursement for half of the Enterprise Zone property tax credit costs.

SDAT believes many of the data reporting issues will be resolved through its new assessment administration system, AVS. AVS will modernize the methodology and processes used for reporting data. Through AVS, SDAT can electronically compile standardized spreadsheets with information from summary reports and computation worksheets. AVS will be able to show the physical addresses of businesses. Data will be automatically calculated in AVS so only the base year assessment will need to be entered, thus eliminating the need for most manual entries. By reducing the need for most manual entries, SDAT predicts there will be less errors going forward.

The summary reports of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone did not match the aggregate data that SDAT provided. With such disparities in the data, it was impossible for DLS to determine if SDAT correctly calculated the State's reimbursement for half of the Enterprise Zone property tax credit costs.

Reported Amount of Enterprise Zone Property Investments Is Inaccurate

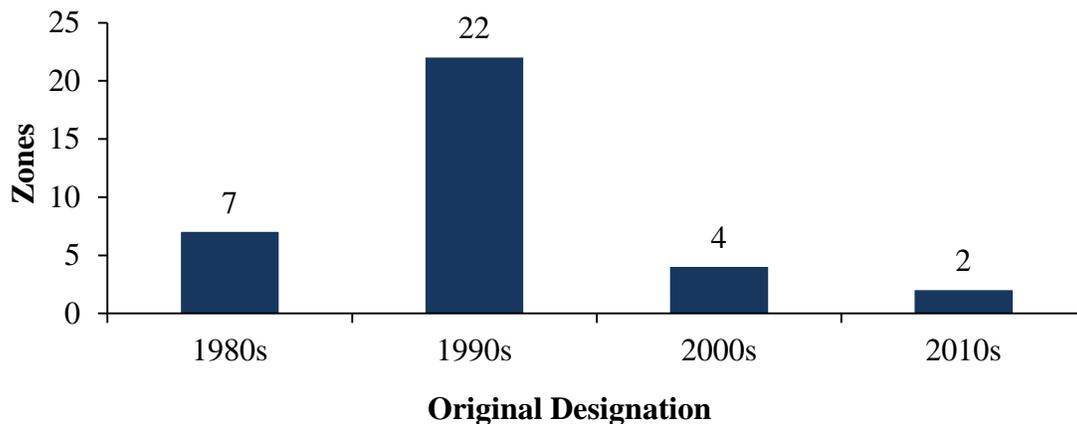
DBED reports the amount of eligible property investments under the program, this data is provided by SDAT. For example, the *2011 Annual Enterprise Zone Report* states that in fiscal 2014 there was a total of \$2.38 billion in eligible property investments and that these investments have increased 22.1% since fiscal 2010. According to SDAT, the investment amount is calculated by comparing the current assessment of an eligible property to the base year assessment (generally the value of the property before the eligible investment). This calculation is not accurate because it includes the change in the assessed value of the building over time. For example, consider the example of a company that makes a \$50.0 million investment in a building that was assessed at \$10.0 million prior to any investment. If the assessed value of the building increases by 4% annually, by the fifth year after the eligible investment the building will be assessed at \$70.7 million (an increase of about \$10.7 million). Under the current method comparing the current year assessment to the base year assessment yields a reported investment of \$60.7 million, thus overstating the investment amount by \$10.7 million or a little more than one-fifth.

Designation of Enterprise Zones

Most Current or Recently Expired Zones Were Designated in the 1990s

As shown in **Exhibit 3.1**, most of the current or recently expired zones were originally designated during the 1990s. Of the zones designated in the 1980s, six zones (Salisbury, Cumberland, Hagerstown, Calvert, Baltimore City, and Washington County Airport) date from the program's inception. Except for the Salisbury zone, the Eastern Shore enterprise zones date from the early- and mid-1990s. Most of the Baltimore area and Western Maryland zones were originally designated in the 1980s and 1990s. Enterprise zones in the Capital region are more recent – one-half of the last eight zone designations are within this area, including Takoma Park, Gaithersburg, Glenmont, and the re-designation of the Prince George's County zone. Other recent designations include Woodlawn in Baltimore County and Keyser's Ridge in Garrett County.

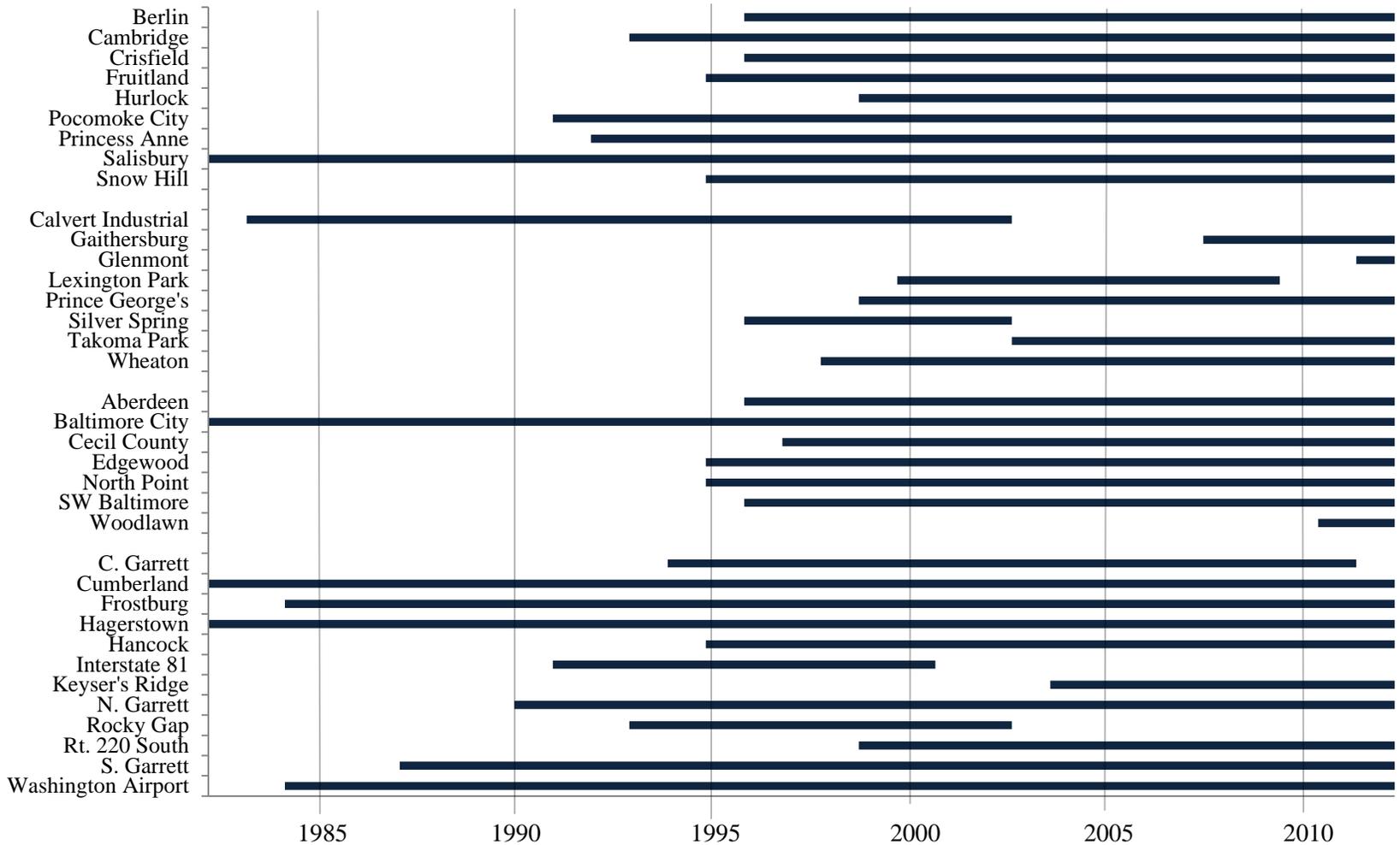
Exhibit 3.1
Enterprise Zone Designations by Date
Current and Recently Expired Zones



Source: Department of Business and Economic Development; Department of Legislative Services

Exhibit 3.2 shows the chronology of recent and expired enterprise zones since the program's beginning. Of the currently designated zones, the typical zone is in its eighteenth year; Western Maryland zones have been designated the longest (23 years), followed by the Eastern Shore (20 years), Greater Baltimore region (15 years), and Capital region (9 years). The Baltimore City enterprise zone is entering its thirty-second year.

Exhibit 3.2
Chronology of Enterprise Zones



Source: Department of Business and Economic Development; Department of Legislative Services

Zone Re-designations and Expirations

All but a few zones are re-designated upon the tenth and final year of the original designation. Upon termination of a zone, a business may continue to claim credits for which it previously qualified when the zone was active. In addition, Chapter 362 of 2006 specified that a business may continue being eligible for additional property tax credits for up to five years after the expiration of the enterprise zone designation. Four zones – Silver Spring, Lexington Park, Rocky Gap, and Interstate 81 in Washington County – were not recently re-designated. The Calvert Industrial Park and Central Garrett County zones each expired after two designations (20 years).

Generally, zones are not re-designated due to changes in the communities over time, and as a result, the area no longer meets one of the credit qualifications related to poverty, low-income households, unemployment, or population loss. St. Mary's County and Calvert County officials chose not to reapply for re-designation because it was estimated that the area could no longer meet one of the four criteria. DBED indicates that both the Silver Spring and I-81 zones are examples of successful zones that no longer qualified for re-designation.

During the 1980s and 1990s, Silver Spring experienced a significant loss of retail establishments and other businesses, a high office vacancy rate, and elevated crime in certain areas. The Silver Spring enterprise zone designation in 1997 was part of a comprehensive and sustained effort by Montgomery County to revitalize the downtown area. These efforts included designation of an arts and entertainment district, several redevelopment committees and boards, purchase and restoration of the Silver Theatre, successfully attracting the Discovery Communications headquarters, and a concerted effort to develop a "town center." According to the Maryland Department of Planning, public investments of about \$450.0 million were accompanied by an additional \$2 billion in private investment. An analysis by the Montgomery County Planning Department concluded that although public investments and incentives were necessary to leverage greater private investments and improve the tax base, there was no "silver bullet" for success but instead a sustained commitment to a comprehensive development plan that was backed by the engagement of both businesses and residents. These comprehensive efforts to improve the community, in conjunction with transportation access and a strong demand for housing in the Washington, DC area, helped positively transform the downtown Silver Spring area.

Washington County determined that the I-81 enterprise zone created in 1991 would not qualify for re-designation in 2001 due to positive economic changes in the zone, which was located in the Hopewell Valley immediately to the west of Hagerstown. However, in July 2012 the county expanded the Hagerstown enterprise zone beyond the city to the predominantly manufacturing and warehousing business area located within the Hopewell Valley. As a result, the Hagerstown enterprise zone has now re-incorporated nearly all of the area which comprised the I-81 zone.

Zone Expansions

Various research studies on Enterprise Zone programs recommend that states target Enterprise Zone programs to economically distressed areas and limit the geographic expansion of zones. Although a limited area of Maryland is currently designated as an enterprise zone, about 1.1% of the State in 2013, the program has increased by 9,700 acres since 2000, representing a 15.8% increase. About one-fifth of all designated acres are within Baltimore City, the largest zone, followed by Harford County (18%) and zones within Allegany County (12%).

Enterprise zones have expanded in 11 of the 13 counties currently housing zones. The Baltimore City enterprise zone expanded the most, from 9,557 acres in 2000 to 13,453 acres in 2013, while Cecil County had the biggest percentage increase in enterprise zone acreage, expanding from 1,989 acres in 2000 to 4,334 acres in 2013. Despite these changes, the overall distribution of enterprise zone acreage by county has remained relatively stable. The amount of acres designated as a zone varies from 18,400 acres in the Greater Baltimore area (about one-quarter of the total) to 8,400 acres in the Capital region (about 12%). The size of the Baltimore City enterprise zone (one-fifth of the total) is similar to the total acres designated within both the Eastern Shore and Western Maryland.

Compared to similar programs in other states, the geographic scope of the Maryland Enterprise Zone program is larger than several states but significantly less than programs in Louisiana, Colorado, and the recently terminated program in California. The amount of acres designated under the Maryland program is 1.5 times larger than the amount of acres designated under the Pennsylvania Keystone Program and 2.5 times larger than the Minnesota JOBZ Program, even though those states are significantly larger than Maryland. About one-fifth of Maryland's population resides within an enterprise zone community, which is similar to New Jersey's Enterprise Zone program.

Baltimore City consolidated from five zones in 2000 to one zone in 2013. By consolidating Baltimore City into one large zone, it makes it easier for city officials to expand the enterprise zone. Zone expansions are also infrequently denied.

Characteristics of Maryland's Enterprise Zone Communities

Enterprise Zone Communities Have Higher Unemployment and Poverty Rates

Enterprise zone communities have higher unemployment (12% higher than the State average), lower labor force participation (5% lower), and lower median household incomes (60% of the State average) compared with the rest of the State. About one in seven enterprise zone community residents are employed within the manufacturing or transportation/warehousing industries, which is about 50% more than the State average of 10%.

Many communities experience concentrated areas of joblessness. The Baltimore City unemployment rate is 12.6%; however, 22 census tracts within the city (representing 10% of the adult population) have unemployment rates in excess of 25%, with a peak unemployment rate of 39%. Other areas with high unemployment include Landsdowne within the Southwest enterprise zone in Baltimore County, downtown Hagerstown, and areas within the Frostburg enterprise zone. Concentrated unemployment also exists in communities with smaller populations, albeit on a smaller and more difficult to measure geographic scale.

The incidence of poverty, low-income households, and receipt of public assistance is significantly higher in enterprise zone communities than what the amount of underemployment relative to the rest of the State would suggest. The incidence of receipt of Supplemental Nutrition Assistance Program (SNAP) benefits is about three-quarters higher than the State average and a little more than one-third of all households earn less than \$35,000 – double the State average. Eastern Shore communities had the highest average incidence of poverty – about one-third of Crisfield and Princess Anne residents earn incomes at or below the poverty threshold. Other communities with high levels of poverty include Pocomoke City, Cambridge, Frostburg, Hurlock, and Baltimore City.

Exhibit 3.3 shows the economic and demographic characteristics of enterprise zone communities by region. **Exhibit 3.4** shows the 10 communities with the highest incidence of poverty and unemployment. **Appendix 4** and **5** show detailed economic and demographic information for each enterprise zone community.

Exhibit 3.3
Enterprise Zone Community Economic and Demographic Characteristics by Region
Calendar 2007-2011

	<u>Western Maryland</u>	<u>Eastern Shore</u>	<u>Greater Baltimore</u>	<u>Baltimore City</u>	<u>Capital Region</u>	<u>All Zones</u>	<u>State</u>
Population	100,880	61,840	266,250	620,210	138,210	1,187,390	5,736,550
Unemployment (%)	5.6	9.3	8.5	12.6	7.7	8.2	7.3
Labor Participation (%)	63.9	62.1	69.3	62.3	75.6	65.4	69.0
Median Household Income	\$37,730	\$39,820	\$55,350	\$40,100	\$74,770	\$44,290	\$72,420
Manufacturing/Warehousing (%)	17.1	16.0	14.6	10.9	5.5	14.6	9.7
Poverty (%)	15.4	24.0	11.3	22.4	11.9	15.6	9.0
SNAP Recipients (%)	13.5	16.4	11.4	17.1	7.5	12.7	7.1
Low-income Households (%)	44.2	46.9	27.8	44.8	41.1	37.2	15.6
White (%)	90.6	55.0	68.1	31.6	41.1	68.1	59.2
African American (%)	7.1	38.7	22.8	65.3	20.4	20.7	29.4
Foreign Born (%)	1.5	4.5	7.3	7.2	41.5	5.7	13.5

Notes: Low-income households are the percentage of households earning less than \$35,000. Manufacturing and warehousing equals percentage of residents who are employed within the manufacturing and transportation/warehousing industries. SNAP recipients are the percentage of population receiving Supplemental Nutrition Assistance Program benefits. Poverty rate is for all individuals.

Source: U.S. Census Bureau, 2007-2011 American Community Survey; Department of Legislative Services

Exhibit 3.4
Enterprise Zone Communities with
Highest Unemployment and Poverty Rates

<u>Highest Unemployment</u>	<u>% Rate</u>	<u>Highest Poverty</u>	<u>% Rate</u>
Hurlock	16.4	Crisfield	35.3
Cambridge	15.5	Princess Anne	33.0
Pocomoke City	14.9	Pocomoke City	27.0
Southwest Baltimore Co.	14.2	Frostburg	24.5
Baltimore City	12.6	Cambridge	24.1
Hagerstown	10.5	Hurlock	24.0
Cumberland	10.4	Baltimore City	22.4
Hancock	10.3	Snow Hill	20.9
North Point	10.0	S. Garrett	20.4
Crisfield	9.3	Hagerstown	19.9

Source: U.S. Census Bureau, 2007-2011 American Community Survey; Department of Legislative Services

Enterprise Zone Communities are Diverse

Enterprise zone communities are a diverse mix of small towns, rural areas, and larger urbanized areas. About one-half have a population of less than 5,000, while about one-third have a population of 25,000 or greater including Wheaton (47,300), Gaithersburg (59,000), and North Point (151,200). The Baltimore City enterprise zone is much larger in scope and population (620,200) than other zones. Although several small communities have high rates of unemployment and poverty, in general, larger communities have greater unemployment (one-third more) as well as a 20% higher incidence of poverty and low-income households. Most zones are located within one community or rural area. However, about one-third of all enterprise zones are located in multiple communities – examples of these include Hagerstown, Cumberland, Takoma Park, and zones located in Baltimore, Harford, and Cecil counties.

The Baltimore City, Capital region, and Eastern Shore zones are also racially diverse. Except for the Capital region, significantly fewer community residents are foreign-born. About 10% of community residents are veterans, with residents of the Capital region less likely to have served in the Armed Forces. About one in six residents of the Hurlock, Rt. 220 South, Aberdeen, and Edgewood zones are veterans.

Desired Job Skill Intensity Levels Vary

This report describes research conducted by the International Monetary Fund (IMF) examining the role and sources of structural unemployment, which is unemployment caused primarily by a mismatch between jobs and job seekers. The analysis also focused on the role of the skills mismatch between jobs and job seekers and the extent to which the recent recession increased this mismatch. Although IMF estimated that Maryland had an average skills mismatch compared to other states, the increase caused by the recent recession was higher than that experienced in most states. The research focused on the role of education mismatches and housing market difficulties, which may restrict the ability of individuals to move for employment opportunities.

The IMF research classified industries into three categories based on their skill intensity – low, semi, and high skill – based on the average educational attainment of workers in each industry. This classification, representing the skills demanded by employers, was compared to the supply of education skills provided by Maryland residents. **Exhibit 3.5** shows the classification of industries according to the industry’s skill intensity and need for skilled labor.

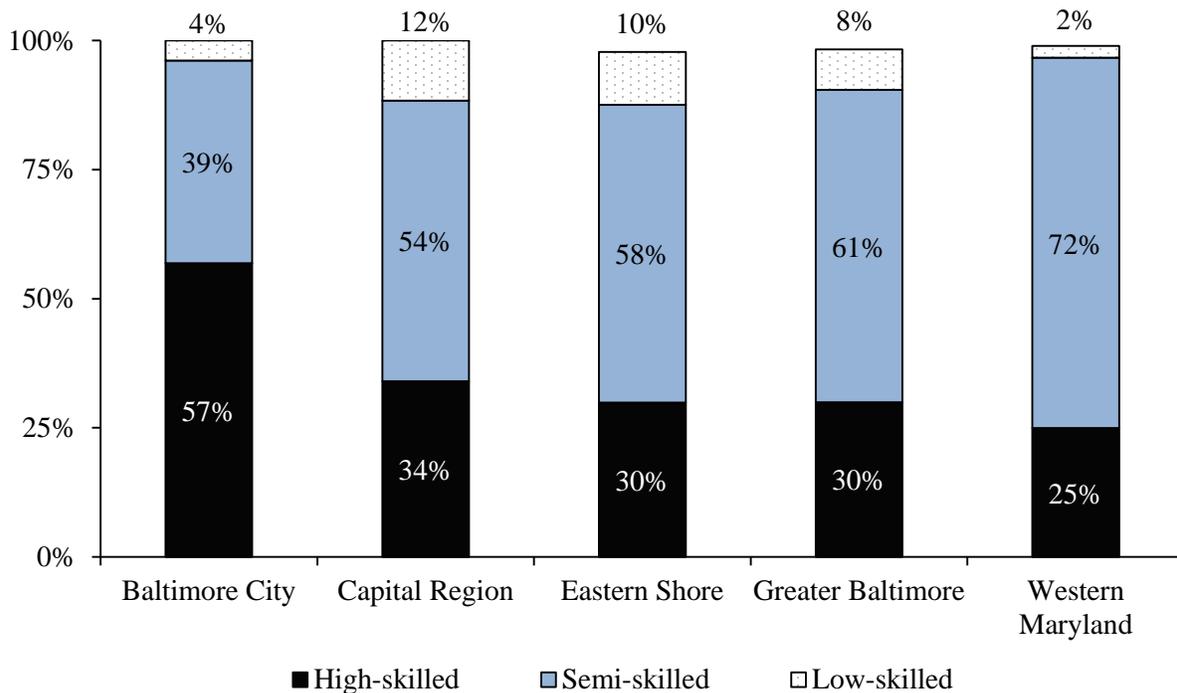
Exhibit 3.5 Skill Level by Industry

<u>Low Skill</u>	<u>Semi Skill</u>	<u>High Skill</u>
Construction	Manufacturing	Information
Mining	Utilities	Financial Activities
Logging	Trade and Transportation	Education
	Leisure/Hospitality	Health Care
	Other Services	Professional/Scientific/Technical
		Business Services

Source: International Monetary Fund – *Has the Great Recession Raised U.S. Structural Unemployment?*

DLS collected data on the total number of private jobs within enterprise zones, including the industry classification and worker demographic information. **Exhibit 3.6** shows by region the percentage of enterprise zone jobs according to skill intensity.

Exhibit 3.6
Percentage of Enterprise Zone Jobs by Skill Intensity
Calendar 2011



Source: National Employment Time-Series Dataset; U.S. Census Bureau – *Longitudinal Employer-Household Dynamics*; Department of Legislative Services

Baltimore City enterprise zone employers had the highest regional demand for high-skill jobs; health care and education industries accounted for about one-half of the demand. Compared with other individual zones, Baltimore City had the third highest skill intensity after zones in Berlin and Salisbury. The health care industry is the dominant employer in Berlin and also has a large presence in Salisbury, which also has a concentration of professional, science, technical services, finance, and information industry jobs. Semi-skilled jobs are prevalent in industrial parks or enterprise zones that target manufacturing and warehousing, including the North Garrett Industrial Park, Hurlock Industrial Park, Hancock enterprise zone, Washington County Airport, Cecil County, North Point and Southwest within Baltimore County, and Edgewood enterprise zone (Harford County). The Capital region's enterprise zones lack dominant industries and have the most job diversity.

Chronically unemployed individuals may live near enterprise zones; however, they must compete against other job seekers. Around 13% of Marylanders have moved within the last year and about one-half of all workers commute 30 minutes or more to work. The efficacy of the Enterprise Zone credit in promoting employment of the chronically unemployed is dependent on

the likelihood of firms hiring these individuals. A large body of research has focused on the link between education levels and employment outcomes. Within the competitive labor market, education acts as a signal to employers about the potential productivity of a job applicant. Research has consistently shown a link between increased education and better job market outcomes. Conversely, a lack of education remains strongly associated with economic and social disadvantage and can reinforce intergenerational cycles of disadvantage.

Enterprise zone businesses may hire community residents, even if less educated, if the skill levels of residents and jobs are aligned. However, as shown in Exhibit 3.6, about one-third of all enterprise zone jobs are within high-skill industries, although these industries employ 6 out of every 10 Baltimore City enterprise zone jobs.

Recent Economic Difficulties Have Intensified Competition for Jobs

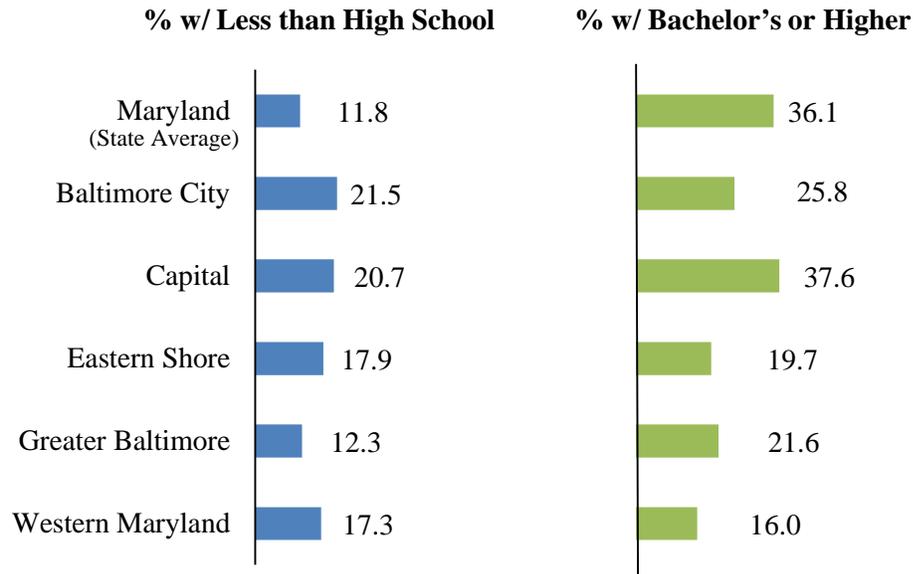
In addition to potential education and skills disadvantages, the recent economic downturn has intensified job competition. Recent research suggests that in the current economy employers are very unlikely to consider hiring individuals who have been unemployed for a long duration. One researcher found that employers would rather call for an interview someone with no relevant experience who has only been out of work for a few months than someone with more relevant experience who has been out of work for longer than six months.

The economy is expected to continue to remain below its potential in the next few years, leading to a lackluster job market in which it is likely that the long-term unemployed will face significant barriers to employment. According to the U.S. Bureau of Labor Statistics (BLS), the long-term unemployed accounted for 4.0% of the total labor force in September 2010, higher than the previous peak of 2.6% in 1983. Although conditions have recently improved, BLS stated that with regard to the labor market, the downturn that began in 2007 is by all indications much worse than those in recent years and can even be considered one of the worst ever.

On Average, Enterprise Zone Community Residents Are Less Educated Than Other Residents

Enterprise zone community residents are on average less educated than the rest of the State. Almost 90% of enterprise zone communities had either a greater percentage of residents without at least a high school diploma or had fewer residents with at least a bachelor's degree or higher. On average, there was a 50% higher prevalence of individuals without a high school diploma (17.9% compared to 11.8%) and 40% fewer individuals with a bachelor's degree or higher (about one-fifth and one-third, respectively). **Exhibit 3.7** shows the education level of enterprise zone community residents by geographic region compared with the State average. Capital region enterprise zone communities had the highest education levels, primarily due to Gaithersburg and Glenmont residents. Enterprise zone communities with the lowest levels of education include Hancock, Hurlock, Hagerstown, and North Point. Baltimore City had an average education level compared to other zones, with a greater number of both less-educated and more-educated individuals.

Exhibit 3.7
Educational Attainment of Enterprise Zone Community Residents by Region
Compared to State Average



Source: U.S. Census Bureau; Department of Legislative Services

Differing Educational Attainment Levels Create Skills Mismatches

DLS compared the educational attainment levels of enterprise zone community residents with the actual education levels of enterprise zone private industry workers. There is a significant mismatch between the skills of those who fill the private jobs within enterprise zones and those who reside in or near the zones. Two measures illustrate this mismatch. The IMF analysis constructs a skills mismatch index (SMI) – the difference in education (whether greater or less) provided by residents and that demanded by employers. The mismatch in resident and worker education levels, as measured by SMI, is two-thirds greater within enterprise zones compared to the entire State. The North Garrett Industrial, Hurlock, Aberdeen, Gaithersburg, and Washington County Airport zones have the lowest mismatch in education levels between residents and enterprise zone workers and are therefore most likely to employ community residents. In four out of the five zones with the greatest mismatch, the mismatch is partially due to a greater supply of residents with at least a bachelor's degree – 30% of Frostburg community residents have at least a bachelor's degree, double the percentage of private wage workers within its enterprise zone.

Given that the intent of the credit is to boost employment of the chronically unemployed and not all area residents, DLS uses a modified skills mismatch index to illustrate the level of educational disadvantage that community residents face when seeking employment within that

community's enterprise zone. This measure shows that 90% of all enterprise zone communities are also undereducated compared to the workers who actually fill the private industry jobs within enterprise zones and thus face significant barriers to employment within the zones. **Exhibit 3.8** shows the zones in which the community residents have the highest and lowest education disadvantages, as measured by the amount by which community residents are undereducated relative to the individuals who fill the jobs within the zone.

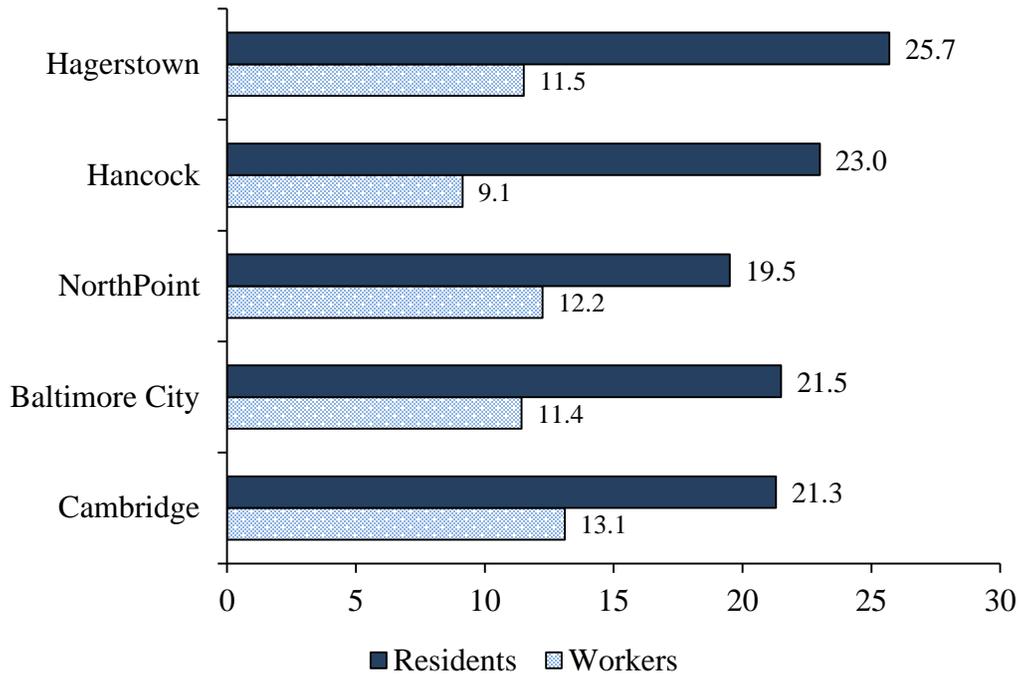
Exhibit 3.8
Ranking of Enterprise Zone Community Education Disadvantages

<u>Highest Disadvantage</u>	<u>Lowest Disadvantage</u>
Hagerstown	Pocomoke City
Hancock	Washington Co. Airport
North Point	Wheaton
Baltimore City	Snow Hill
Cambridge	Aberdeen
Takoma Park	Woodlawn
Fruitland	N. Garrett
Princess Anne	Gaithersburg

Source: U.S. Census Bureau; Department of Legislative Services

For example, about one-quarter of community residents in Hagerstown and Hancock do not have a high school diploma. Businesses within these zones demand higher skills and hire individuals who are better educated – 90% of the jobs within these zones are filled with workers who have at least a high school diploma. **Exhibit 3.9** illustrates the percentage of community residents without a high school diploma within the five zones with the highest education disadvantages.

Exhibit 3.9
Percentage of Enterprise Zone Workers and Residents without a High School Diploma
Zones with the Highest Education Disadvantage



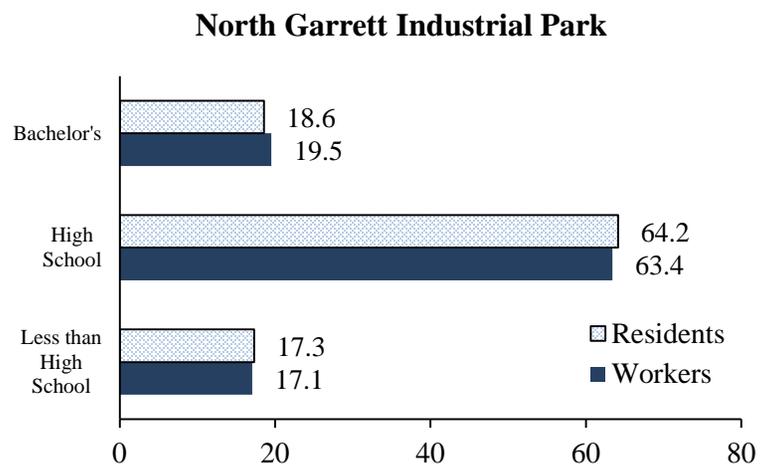
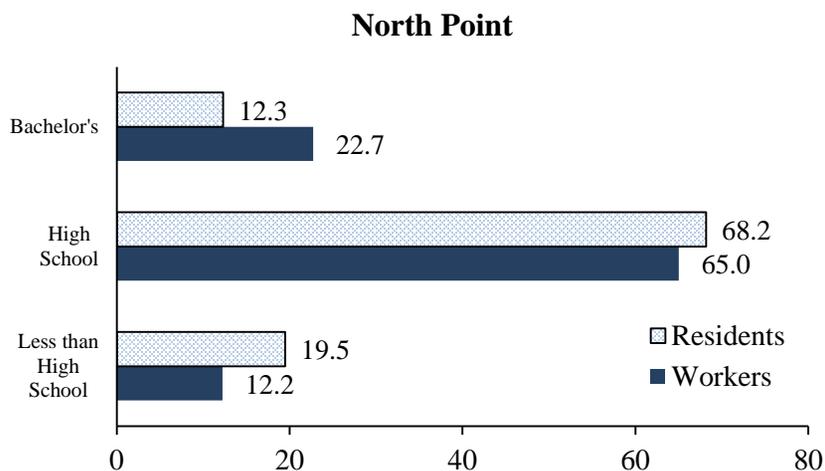
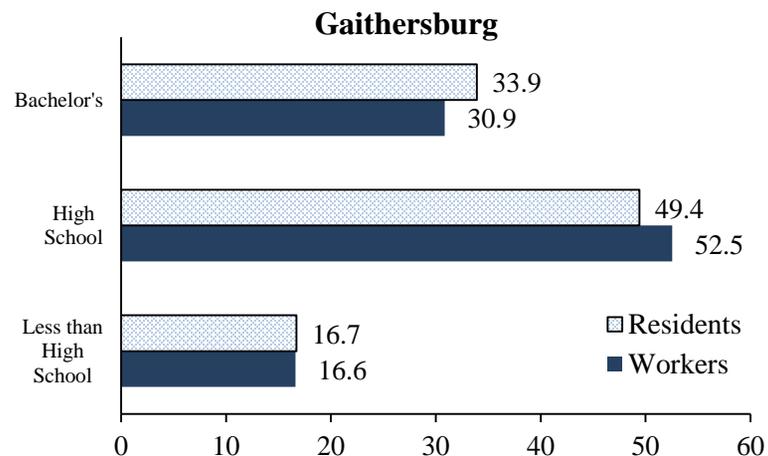
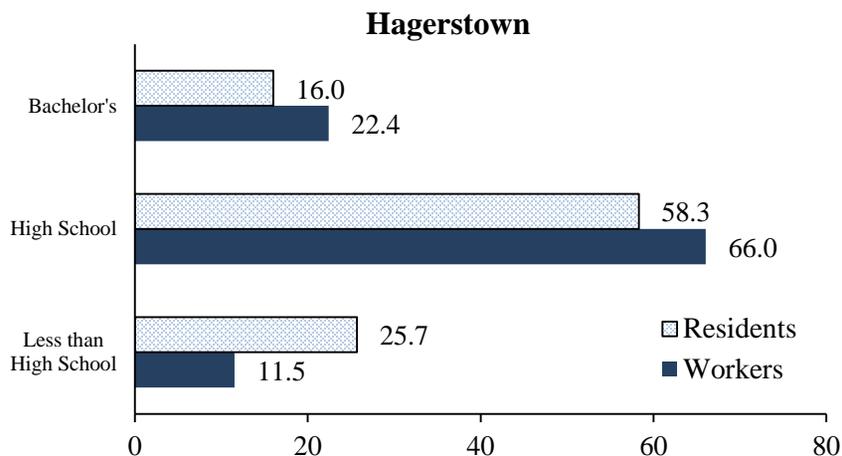
Source: U.S. Census Bureau; Department of Legislative Services

Exhibit 3.10 compares the education levels of residents and workers of two communities with sufficient skills to fill jobs within enterprise zones and two communities that have a large number of individuals who lack the skills demanded by enterprise zone employers. On average, 87% of all jobs within enterprise zones are filled with individuals with at least a high school diploma and almost one-quarter have at least a bachelor's degree. Enterprise zones that focus on semi-skilled industries such as manufacturing and warehousing show mixed results in reducing the education gap between the skills demanded by employers and those possessed by community residents. This gap persists primarily due to the supply of community residents who lack basic education levels. Of the 11 zones with the highest concentration of manufacturing and warehousing jobs, five have an above-average amount of residential under-education including Hagerstown and North Point which have among the highest mismatches.

**Exhibit 3.10
Educational Attainment in Selected Enterprise Zones**

Residents Lack Skills and Face Employment Barriers

Residents are Sufficiently Skilled

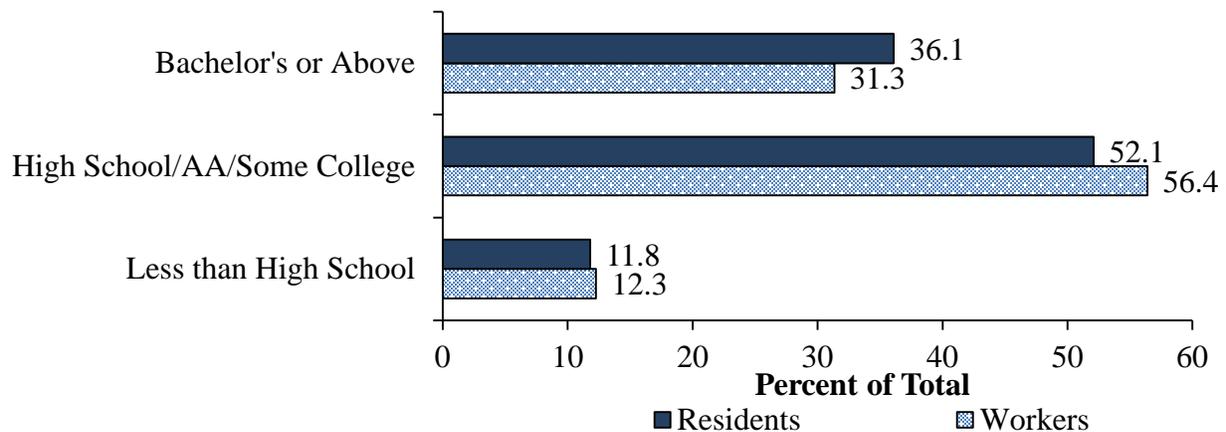


Notes: Bachelor's includes Bachelor's degree or higher; high school includes individuals with high school diploma, some college, or two-year degree.
Source: U.S. Census Bureau, 2007-2011 American Community Survey; Department of Legislative Services

Labor Mobility Hinders the Hiring of Enterprise Zone Community Residents

A significant portion of enterprise zone community residents lack the education skills demanded by enterprise zone employers. Labor supply and demand are mobile across communities – as a result, employers can hire those with the highest skill sets regardless of where the workers live and import skilled workers from other communities. Overall, these workforce trade flows balance out – **Exhibit 3.11** shows that in contrast to enterprise zone communities, the educational level of Maryland residents is sufficient to fill private jobs in the State.

Exhibit 3.11
Percentage of Educational Attainment of Maryland Residents and Private Industry Workers



Source: U.S. Census Bureau – *American Community Survey & Longitudinal Employer-Household Dynamics*; Department of Legislative Services

Due to the lack of skills among enterprise zone community residents and the mobility of labor, only about one in eight enterprise zone jobs are filled by community residents. This includes all community residents and not just the chronically unemployed. **Exhibit 3.12** shows the average percentage of enterprise zone jobs that are filled by residents of the enterprise zone community and county in which the zone is located.

Baltimore City has the highest community job retention compared to other regions. However, the Baltimore City enterprise zone is 13,453 acres, comprises a significant portion of the commercial and industrial areas of the city, and is significantly larger than other zones. About one-half of all zones are less than 1,000 acres and are on average 3% the size of the Baltimore City zone. Given the scope of the Baltimore City zone, a more accurate comparison is at the county level. About two-thirds of Baltimore City enterprise zone workers are not city residents; by comparison, about one-half of all enterprise zone workers do not live in the county in which the zone is located.

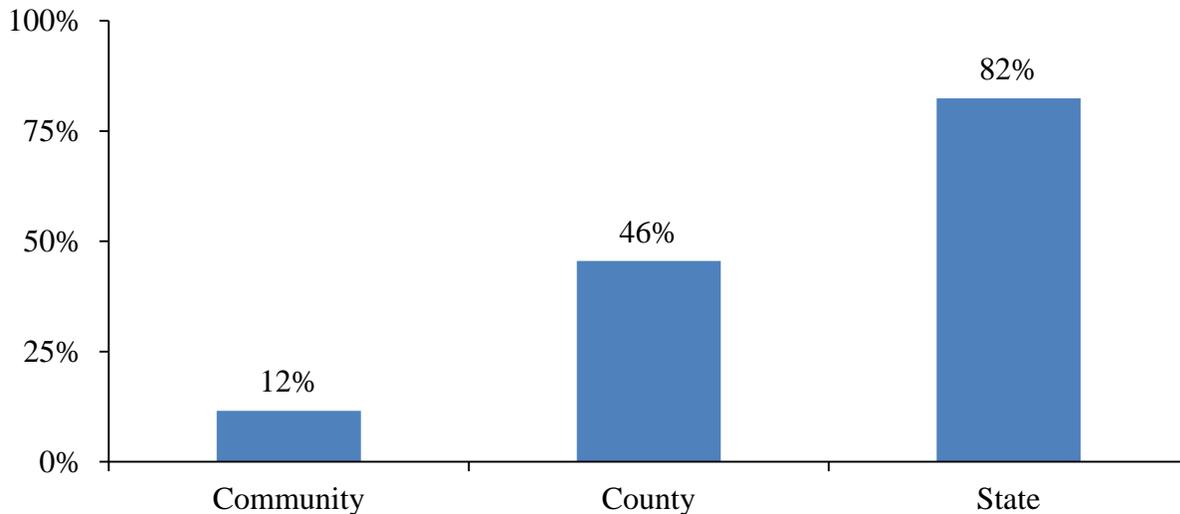
Exhibit 3.12
Percentage of Enterprise Zone Workers by Geography

<u>Region</u>	<u>Community</u>	<u>County</u>	<u>State</u>
Western Maryland	14%	56%	71%
Eastern Shore	8%	39%	86%
Baltimore City	32%	32%	94%
Greater Baltimore Area	13%	46%	93%
Capital Region	6%	39%	83%

Source: Department of Business and Economic Development; U.S. Census Bureau – *Longitudinal Employer-Household Dynamics*; Department of Legislative Services

Exhibit 3.13 shows for all zones the average percentage of enterprise zone jobs that are filled by community, county, and Maryland residents.

Exhibit 3.13
Percentage of Enterprise Zone Jobs Retained by Geography



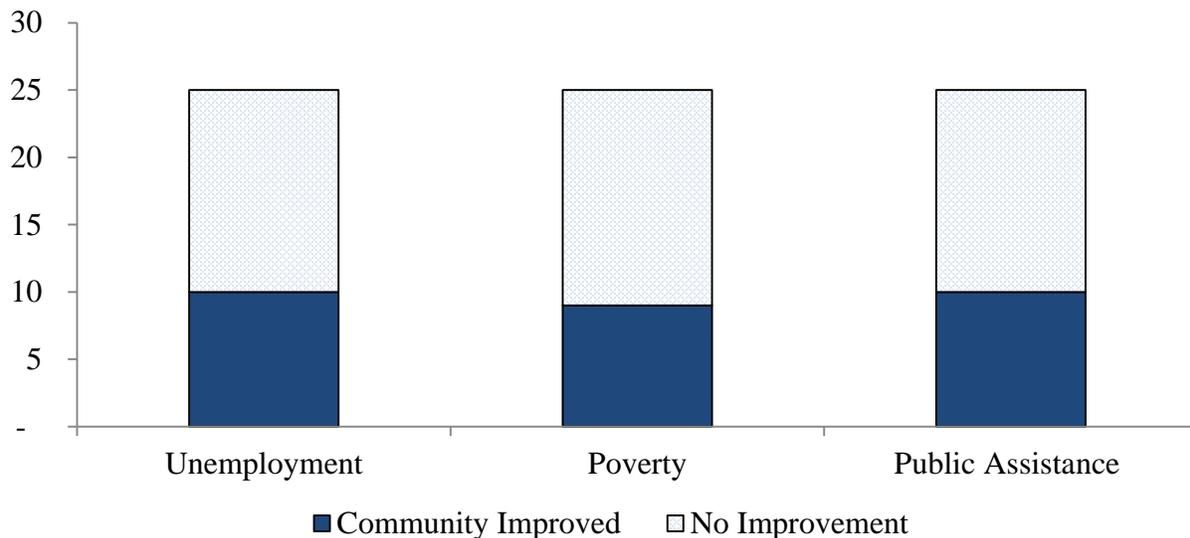
Source: Department of Business and Economic Development; U.S. Census Bureau – *Longitudinal Employer-Household Dynamics*; Department of Legislative Services

Have Enterprise Zone Communities Shown Improvement?

DLS examined changes in communities over time to assess if Enterprise Zone tax credits have benefitted communities through increased employment and reduced poverty. These changes include measuring U.S. Census demographic and economic characteristics of areas that were designated as an enterprise zone from 2000 to the present. Several factors, however, inhibit an accurate assessment including (1) the small population of many zones, which require the use of five-year estimates (2007-2011) with high margins of errors that prevent statistically significant results; (2) the impacts of the recent recession; (3) enterprise zones are economically distressed and should be compared to a similar control group; (4) a limited ability to separate out other influences which might have caused changes within communities; and (5) geographic imprecision. For example, selecting different geographies for several zones that do not have easily identifiable U.S. Census geographies often led to conflicting results.

With these limitations in mind, it appears that median incomes and adult populations increased in most communities. As shown in **Exhibit 3.14**, about one-third of communities had a lower adult poverty rate and 40% had a lower incidence of unemployment and receipt of public assistance.

Exhibit 3.14
Number of Enterprise Zone Communities
that Showed Improvement
2000 to Present



Source: U.S. Census Bureau; Department of Legislative Services

Communities with the largest improvement in poverty and unemployment rates include Central Garrett, Berlin, South Garrett, Snow Hill, and Rt. 220; the Edgewood, Cambridge, Hagerstown, Pocomoke City, and Southwest Baltimore zones experienced the largest increases in poverty and unemployment.

Total private employment of enterprise zone community residents increased by about 27,000, an average annual increase of 0.7%; private employment grew the most within the Capital region and slowest in the greater Baltimore region. The growth in private employment among community residents lagged significantly behind the overall statewide change in private employment. Despite the emphasis of several zones on increasing manufacturing employment, total employment within the manufacturing industry decreased by 13,000 or by 30%, this was greater than the 2010 decrease in the State over the same time, as shown in **Exhibit 3.15**. Significant employment losses also occurred within the wholesale trade, finance, and information industries; the last two industries suffered significant employment losses nationwide due to the recession. Conversely, employment increased most within the education and health care industries, professional, science, and technical services, and arts and entertainment industries. Overall, growth was strongest in high-skilled industries (15.5%) and decreased by 1% within low- and semi-skilled industries.

Exhibit 3.15 also shows for each region the most recent estimate of the total number of unemployed community residents by region. About 90,600 community residents were unemployed, about 40% of the total number of unemployed statewide.

Exhibit 3.15
Change in Employment in Enterprise Zone
Communities by Industry Classification
2000-Present

	<u>Western Maryland</u>	<u>Eastern Shore</u>	<u>Greater Baltimore</u>	<u>Baltimore City</u>	<u>Capital</u>	<u>All Zones</u>	<u>Percent Change</u>	
							<u>Zones</u>	<u>State</u>
Agriculture, Forestry	(150)	0	63	41	29	(17)	-2.3%	-7.5%
Construction	549	(102)	(74)	2,742	340	3,455	13.5%	17.4%
Manufacturing	(1,580)	(1,072)	(5,157)	(5,137)	(26)	(12,972)	-28.8%	-20.0%
Wholesale Trade	(401)	324	(522)	(1,938)	(103)	(2,640)	-20.3%	-13.3%
Retail Trade	501	494	199	904	83	2,181	4.6%	2.8%
Transportation & Warehousing	504	371	(403)	393	(49)	816	2.3%	1.8%
Information	(349)	(41)	22	(2,397)	(53)	(2,818)	-22.3%	-27.9%
Finance	318	(128)	(53)	(494)	(76)	(433)	-2.4%	2.7%
Professional, Science, Technical Services	1,182	626	2,438	3,863	581	8,690	21.4%	31.1%
Education & Healthcare	1,971	1,702	6,170	13,452	358	23,653	23.1%	22.6%
Arts and Entertainment	1,066	1,294	1,038	3,118	771	7,287	21.3%	26.8%
Other Services	(48)	306	(7)	(427)	7	(169)	-1.3%	7.4%
Total Private Employment	3,563	3,774	3,714	14,120	1,862	27,033		
Percent Annual Change	1.0%	1.8%	0.3%	0.7%	2.4%	0.7%	0.7%	1.2%
Current Number of Unemployed*	4,114	3,358	13,794	39,359	29,943	90,598		227,000

Notes: Change in employment within Capital region does not include Prince George's County.

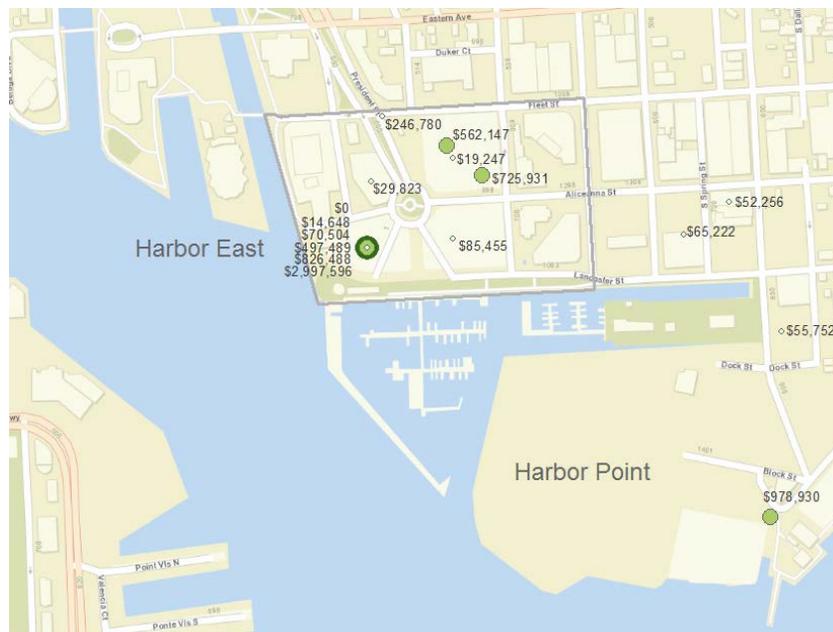
*Current number of unemployed reflects 2007-2011 American Community Survey estimates of the total number of unemployed.

Source: U.S. Census Bureau; Department of Legislative Services

As mentioned previously, Baltimore City has a large enterprise zone encompassing almost 13,500 acres. Baltimore City has used the Enterprise Zone credit, and other State and local incentives, in efforts to build the city's property tax base. Baltimore City's real property tax rate of \$2.248 per \$100 of assessed value in fiscal 2014 is significantly higher than the rate in other jurisdictions in the State, and the city also has a large portion of its property tax base that is exempt from property taxes. For example, if Baltimore City imposed the average property tax rate of \$0.94 per \$100 of assessed value imposed in other enterprise zone counties, State reimbursements to Baltimore City in fiscal 2014 would have totaled \$3.5 million, or about 58% lower than the actual reimbursement of \$8.3 million.

Baltimore City's Harbor East development is a good example of an economic development project in an enterprise zone that has been successful in providing additional employment and property tax revenues, but only with mixed results for the residents of the local community. Harbor East is a mixed-use development on Baltimore's waterfront with more than 5.5 million square feet of office, residential, hotel, retail, entertainment, and parking space. In addition to creating a concentration of retail stores, there is significant employment within the financial, educational, and professional services industries. According to the Baltimore Development Corporation (BDC), Harbor East is a highly successful development which replaced an area that was formally dominated by heavy industry. **Exhibit 3.16** shows in more detail the location of the Harbor East area, which is located next to the future Harbor Point development, and properties receiving a fiscal 2014 property tax credit.

Exhibit 3.16
Enterprise Zone Property Tax Credit
Harbor East Projects
Fiscal 2014



The ongoing benefits of the Harbor East development include:

- the number of businesses increased from 40 in 2000 to 170 in 2011;
- total private employment increased by 2,700 over the same time period according to the U.S. Census Bureau;
- adding residential units and increasing the population of the city;
- increasing the tax base by adding higher-income residents and property taxes; and
- increasing the attractiveness of the area and number and type of amenities available to residents, which can spur additional development and population growth.

Although employment and businesses in the area increased, a significant portion of these businesses and jobs relocated from other parts of the city. In addition to receiving Enterprise Zone credits, several properties received Baltimore City Brownfields tax credits. If a property is receiving the Enterprise Zone credit, the Brownfields tax credit can reduce any remaining amount of property tax in the first 10 qualifying years. As a result, most of the increased property taxes will occur after the expiration of these credits. The Enterprise Zone tax credit reduced the property taxes on the increased assessment of the development; however, the credit does not apply to residential property. Therefore, the credit provided, at best, an indirect incentive for the development of the residential units.

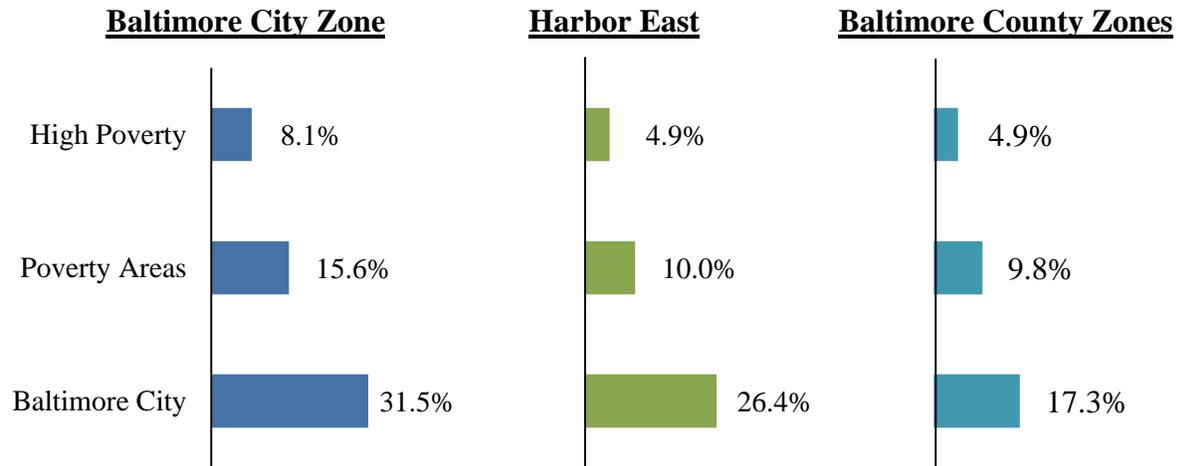
The Harbor East development shifted employment in the area to high-skilled industries which are more likely to increase future employment, thereby increasing economic development within the city. According to BDC, the Baltimore City enterprise zone does not meet statutory criteria related to low-income households, unemployment, or population loss. The high incidence of poverty among residents within the zone; however, is sufficient to meet the statutory requirement.

The Harbor East development has had a limited employment impact on Baltimore City poverty area residents. About three-quarters of all jobs are filled by workers who live outside of the city. About 270 jobs, or only 1 in 10 total jobs, are filled by a Baltimore City resident who lives in a census tract that meets the enterprise zone's poverty requirement. This includes any qualifying census tract, not just the census tracts with high poverty within the enterprise zone. Residents who live in high-income areas are three times more likely than residents of the lowest-income areas of the city to be employed within the Harbor East area.

By comparison, businesses located within a Baltimore County enterprise zone (North Point, Southwest, and Woodlawn) employ 3,100 Baltimore City poverty area residents. These zones are just as efficient as Harbor East in providing employment to Baltimore City residents who live in poverty areas and high-poverty areas within the city. **Exhibit 3.17** compares the percentage of jobs within the Baltimore City enterprise zones, Harbor East, and

Baltimore County enterprise zones that are filled by Baltimore City residents, Baltimore City poverty area residents, and residents of high-poverty areas of the city. Poverty areas are all census tracts within Baltimore City (not just those within the enterprise zone) that currently meet the statutory criterion related to poverty by having a family poverty rate of at least 1.25 times the U.S. average. **Exhibit 3.18** shows the dissimilarity of the demographics of the workers who fill jobs within the Baltimore City enterprise zone and Harbor East and the residents of poverty areas and high-poverty areas within Baltimore City. Baltimore City poverty area residents have significant educational disadvantages relative to the workers who fill jobs within the Baltimore County enterprise zones and Harbor East. For example, as shown in **Exhibit 3.19**, a little less than one-half of all Harbor East workers have at least a bachelor's degree, and less than 10% do not have a high school diploma. A little more than one-quarter of all poverty area residents do not have a high school diploma, and only 10% have at least a bachelor's degree.

Exhibit 3.17
Percentage of Enterprise Zone and Harbor East Jobs Filled by Baltimore City Residents



Notes: Poverty areas are all census tracts within Baltimore City (not just those within the enterprise zone) that currently meet the statutory criterion related to poverty by having a family poverty rate of at least 1.25 times the U.S. average. High-poverty areas are the Baltimore City census tracts with poverty rates in excess of 40%.

Source: U.S. Census Bureau; Department of Legislative Services

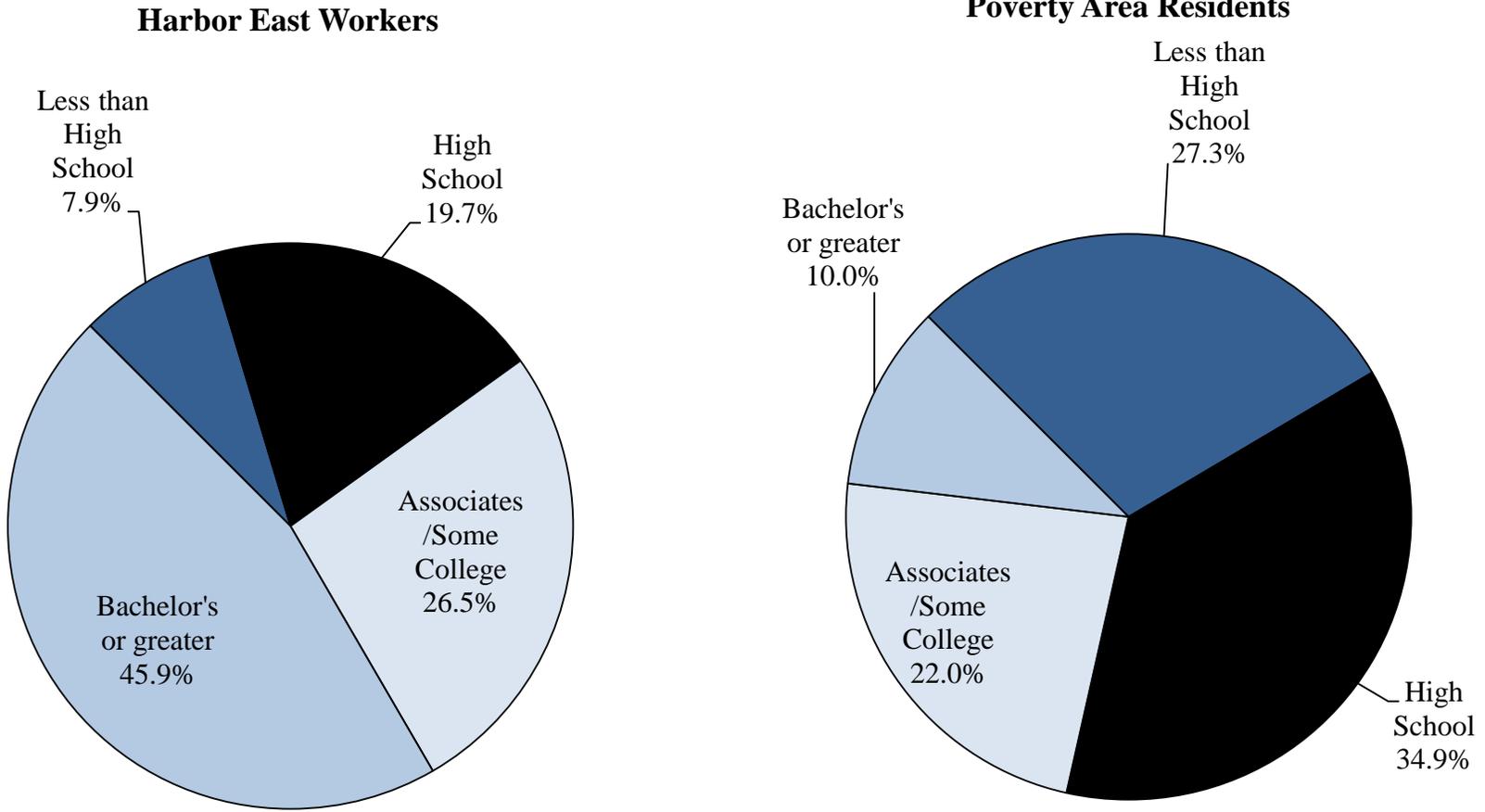
Exhibit 3.18
Demographics of Baltimore City Workers and Poverty Residents

<u>Education Levels</u>	Workers		Baltimore City Residents	
	<u>Enterprise Zone</u>	<u>Harbor East</u>	<u>Poverty Areas</u>	<u>High Poverty</u>
Less than High School	11%	8%	27%	30%
High School	25%	20%	35%	35%
Associates/Some College	30%	27%	22%	22%
Bachelor's or greater	33%	46%	10%	9%
<u>Ethnicity</u>				
Caucasian	62%	73%	19%	4%
African American	31%	20%	76%	92%
Other	7%	7%	5%	3%

Notes: Education levels are for private workers within the Baltimore City enterprise zone and Harbor East. Poverty areas are all census tracts within Baltimore City (not just those within the enterprise zone) that currently meet the statutory criterion related to poverty by having a family poverty rate of at least 1.25 times the U.S. average. High-poverty areas are the Baltimore City census tracts with poverty rates in excess of 40%. Resident data is 2007-2011 American Community Survey. Worker data is calendar 2011.

Source: U.S. Census Bureau; Department of Legislative Services

Exhibit 3.19
Educational Attainment of Harbor East Workers and Baltimore City Poverty Area Residents



Source: U.S. Census Bureau; Department of Legislative Services

Businesses Claiming Enterprise Zone Tax Credits

Variation in Business Activity among Enterprise Zones

The Enterprise Zone program has grown significantly since fiscal 2001 – total State reimbursements to local governments have increased from \$2.4 million to \$13.9 million in fiscal 2014 and the number of businesses eligible to receive property tax credits increased from 352 to 810. However, this growth has not been uniform. Counties and municipalities, with DBED approval and overview, implement the program by (1) establishing and expanding (or not) zones (2) setting any additional standards; (3) certifying businesses; and (4) marketing the program to businesses, which might include additional local incentives. As discussed in this report, local governments take a variety of approaches to the program. Differences in program implementation are in addition to other county and municipal policies which may influence business decisions. Although each enterprise zone has some level of economic distress, zones vary in the amount of distress as well as other factors that influence business decisions such as the zone's proximity to markets; availability, cost, and skill level of the work force; infrastructure; and amenities and attractiveness of the area.

Of the 13 counties which currently have at least 1 enterprise zone, State reimbursements have increased significantly in 8 of these counties – Baltimore, Cecil, Garrett, Harford, Montgomery, Prince George's, and Wicomico counties and Baltimore City. State reimbursements to the other five counties (Allegany, Dorchester, Somerset, Washington, and Worcester) have remained flat or fallen. Total State reimbursements to the eight "growth" counties averaged \$1.9 million from fiscal 2001 through 2003 with reimbursements to the other five counties averaging \$1.1 million over the same time. While total reimbursements to the growth counties grew to an average of \$16.0 million in fiscal 2012 through 2014, total reimbursements to the other five counties decreased to an average of \$830,700. **Exhibit 3.20** shows for each zone the total number of businesses which received a property tax credit in fiscal 2014.

Exhibit 3.20
Number of Businesses Receiving Property Tax Credits by Enterprise Zone
Fiscal 2014

<u>County</u>	<u>Enterprise Zone</u>	<u>Designation Date</u>	<u>Businesses Receiving Property Tax Credit</u>
Allegany	Frostburg	1984	14
	Rt. 220 South	1999	1
	Cumberland/Gateway	1982	11
Baltimore County	North Point	1995	21
	Southwest Baltimore County	1996	23
	Woodlawn	2011	0
Baltimore City	Baltimore City	1983	289
Cecil	Cecil County	1997	23
Dorchester	Hurlock Industrial Park	1999	3
	Cambridge	1993	11
Garrett	Southern Garrett	1987	14
	Northern Garrett	1990	13
	Keyser's Ridge	2004	0
Harford	Edgewood-Joppatowne	1995	33
	Aberdeen-Havre de Grace	1996	75
Montgomery	Gaithersburg	2008	3
	Wheaton	1998	9
	Long Branch/Takoma Park	2003	7
	Glenmont	2013	0
Prince George's	Prince George's	1999	51
Somerset	Crisfield	1996	1
	Princess Anne	1992	2
Washington	Washington County Airport	1984	7
	Town of Hancock	1995	3
	Hagerstown	1982	30
Wicomico	Fruitland	1995	1
	Salisbury	1982	43
Worcester	Snow Hill	1995	1-3*
	Berlin	1996	1-3*
	Pocomoke City	1991	1-3*
Expired Zones			113
Total			810

Note: Individual data were not available for Snow Hill, Berlin, and Pocomoke City. According to SDAT there were a total of three reimbursements to Worcester County.

Source: State Department of Assessments and Taxation; Department of Legislative Services

Enterprise Zones with Limited or Decreased Business Activity

A significant number of enterprise zones have a limited number of businesses claiming property tax credits or have had a decrease in either the number of businesses claiming property tax credits or in the amount of investments. Of the 27 enterprise zones that have been established for at least five years, 10 zones have less than 5 businesses currently claiming the Enterprise Zone property tax credits – an average of less than 1 new business every two years. Not only are these enterprise zones failing to attract many businesses, but many of the businesses that are claiming the Enterprise Zone tax credit are not making significant investments in the zones. Seven of the enterprise zones had State reimbursements of less than \$10,000.

In contrast to the total growth in total investment activity under the property tax credit since fiscal 2001, total investments have fallen in four counties – Dorchester, Somerset, Washington, and Worcester. Investment activity is volatile and can fluctuate from year-to-year, so using an average over several years is a more accurate measure. Investments in Dorchester County averaged \$48.3 million from fiscal 2001 through 2004, but investments decreased to \$8.2 million in fiscal 2011 through 2014 despite a 53% growth in the amount of acres designated as an enterprise zone. Over the same period the average amount of investments decreased from \$225.9 million to \$102.6 million in Washington County. Investments decreased by about one-third in Somerset County and by about three-quarters in Worcester County. Total investments in these four counties decreased by a total of 60% despite a 12.3% growth in the size of zones within the counties. In contrast, total investments increased in enterprise zones in other counties from \$601.9 million to \$2.7 billion; these counties had a similar growth in the size of zones as the four counties which experienced a sharp decrease in investments.

Enterprise zones which had a decrease in the number of businesses claiming the property tax credit include Frostburg (from 25 in fiscal 2001 to 14 in fiscal 2014), Cumberland (34 to 11), Hagerstown (62 to 30), and zones in Worcester County (8 to 3). **Exhibit 3.21** shows the counties which had a decrease in the number of businesses or amount of investments under the property tax credit or have enterprise zones which currently have a limited number of businesses claiming the property tax credit.

Exhibit 3.21
Counties with Limited or Decreased Enterprise Zone Activity

	Fiscal 2001-2014 Decrease in		Enterprise Zones with
	<u>Businesses</u>	<u>Investment</u>	<u>Limited Activity</u>
Allegany	X		Rt. 220 South
Dorchester		X	Hurlock
Montgomery			Gaithersburg
Somerset	X	X	Crisfield Princess Anne
Washington	X	X	Hancock
Wicomico			Fruitland
Worcester		X	Snow Hill Berlin Pocomoke City

Notes: Lack of activity is defined as zones that currently have less than five businesses claiming the property tax credit. A decrease in businesses or investment reflects a significant decrease in the amount of businesses or qualifying investments under the property tax credit.

Source: State Department of Assessments and Taxation; Department of Legislative Services

The geographic size of the enterprise zone does not seem to have much of an impact on the number of businesses claiming the Enterprise Zone tax credit. For example, the Northern Garrett Industrial Park is the smallest zone with only 107 acres and has 13 businesses claiming the credit, while the Princess Anne zone is 1,155 acres with only 2 businesses claiming the credit. The Cambridge zone, with 1,661 acres, has the same number of businesses claiming the credit, 11, as the Gateway zone, which has 7,783 acres. Thus, the zone size does not appear to affect business activity. Additionally, the lack of zone activity is not concentrated in one area. While the majority of businesses are located in the greater Baltimore region, the rest of the businesses are fairly evenly distributed between Western Maryland, the Eastern Shore, and the Capital region. The Capital region, Eastern Shore, and Western Maryland have at least three zones with less than 10 businesses claiming the credit. The lack of activity in enterprise zones is not merely concentrated in rural areas. Gaithersburg, which is a fairly urban area, only has three businesses claiming the credit.

While the geographic size and location of the zones do not appear to explain the lack of activity, there are a number of reasons as to why activity is limited in certain enterprise zones. The lack of activity in certain zones might reflect differences in program implementation such as local governments choosing to limit the scope of the program or poor marketing and targeting of zones. Economic reasons include competition from other nearby zones and barriers such as economic distress and lack of markets and labor force. Seven out of the 10 zones with the highest poverty rates have either a limited number or significant decrease in the number of

businesses claiming the property tax credit. The Enterprise Zone credit might not be effective in promoting economic growth within zones that have a high level of economic distress and/or lack of attractiveness to businesses. Although the value of the credit is constant (except for within focus areas) the variation in economic distress and attractiveness to businesses increases as the amount and sizes of zones increase. As a result, program activity might increase in areas that are attractive to businesses or have less distress at the expense of zones or areas within zones that are more distressed or are less attractive to businesses.

For example, Allegany County has struggled to attract businesses to its Rt. 220 South enterprise zone, with only one business in the zone. Local officials indicate that competition from Hagerstown, an enterprise zone that has a large supply of vacant property, has kept the Rt. 220 zone from attracting businesses. Additionally, economic barriers of the Rt. 220 zone, including a six-mile distance from the nearest interstate, might pose challenges to businesses that the tax credits cannot overcome. In addition local officials indicate that a nearby housing development is also negatively impacting the zone. Despite only one business claiming the credit, local officials consider the Enterprise Zone program a success. The business claiming the credit in the Rt. 220 South zone, American Woodmark Corporation, is the ninth largest employer in Allegany County. While American Woodmark Corporation closed several manufacturing facilities located outside of the State, it has been able to expand its business in Rt. 220 South zone, due to substantial State and local incentives including the Enterprise Zone property tax credit.

Incomplete and Missing Data Hinder Efforts to Identify Businesses Claiming the Credit and to Analyze Economic Impacts

Local enterprise zone administrators submit annual reports to DBED providing information on certified businesses as well as other information about the zone. In general, these reports consist of a narrative that contains general information on the business activity within the reporting year as well as information on marketing, additional incentives offered, and local standards and certification processes. Local governments also submit information listing the businesses which were certified during the year, the change in employment of all certified businesses within the zone, and the total amount of capital investment in that year. While DBED provided local reports from 2006 to 2011, reports were missing for several zones. Only some of the local reports contain information on the industry of the businesses, while others report information for only those certified in the reporting year while others report over multiple years. As is detailed in this report, the local employment data that is reported has proven problematic and likely overstates the change of employment within zones. The employment data is self-reported and does not appear to be verified, and covers only those businesses that actually report the data.

The local reports do not contain information on the amount of credit received by the business; this data is potentially available from SDAT (property tax) or the Comptroller's Office (income tax). In addition, for every zone except Baltimore City there is no indication whether the business received the income tax credit and/or the property tax credit. Although the income tax credit is relatively small compared to the property tax credit, a total of \$9.9 million in income tax credits have been claimed since tax year 2000. Each business claiming the income tax credit submits a limited amount of data to the Comptroller's Office, and the Comptroller's Office

cannot provide information on businesses claiming the credit due to confidentiality requirements. There is no available complete set of data identifying all of the companies that have claimed the credit and the change in employment within these businesses.

The lack of data provided by SDAT as detailed in this report limit the ability to identify the businesses that are claiming the property tax credit and the economic impacts of qualifying investments. Except for Baltimore City, most data provided by SDAT listing each property tax credit does not contain adequate identifying information such as the name of the business or accurate address information. In addition, SDAT did not provide total investment and property tax credits claimed in each zone and year since fiscal 2001.

A Number of Enterprise Zones Focus Incentives to Certain Categories of Businesses

About one-third of all enterprise zones have businesses that are concentrated within manufacturing, fabrication, transportation, warehousing, distribution, and research and development. This concentration typically results from either enterprise zone local standards restricting credit eligibility to these activities and industries or the establishment of the zone within an industrial or business park that has similar requirements. Zones with additional local standards include North Point and Southwest within Baltimore County and zones that are primarily located within a business or industrial park include Garrett County enterprise zones, Rt. 220 South, Cecil County, and Hurlock Industrial Park. Other zones with a high concentration of employment or certified businesses within the manufacturing and transportation/warehousing industries include Washington County Airport and Snow Hill.

Five of these concentrated zones are located in Western Maryland, three are located on the Eastern Shore, and two are in the Greater Baltimore area. No zones in the Capital region are concentrated zones; manufacturing and transportation/warehousing industries employ about 3.5% of all employees within those zones, the lowest amount of any region.

Most of the other enterprise zones are located primarily within one municipality or other urban area. There is variation in the degree to which the zone is located within the “downtown” area and lesser developed areas outside of the urban area. Typical businesses within the downtown area include retail, accommodation and food services, and health care with industry, warehousing, and other lower density development outside of the urban area. For example, the Princess Anne zone comprises part of the downtown area as well as a nearby industrial park. Princess Anne has certified nine companies for tax credits, of which four are manufacturing businesses, one construction, and four are retail. Four of these businesses have closed. Other examples include Hagerstown and Cumberland, which have substantial portions of their zones outside of the urban area and the zones in Cambridge and Salisbury which are mainly urban. Although the Baltimore City zone is entirely within an urban area, there are lower density areas of significant size where industry and warehousing are prevalent.

Montgomery County has established zones that are limited to part of the urban area (Glenmont, Takoma Park and Silver Spring, and Gaithersburg) in which the zone is located. These zones range from 125 to 491 acres, substantially smaller than the typical zone. As a result,

most of these zones have significant numbers of businesses within the retail and accommodation and food services industries.

Several zones encompass more than one urban area and/or municipality. Several urban areas, municipalities, and lesser developed areas along the Rt. 40 corridor in Harford and Cecil counties are located within the Aberdeen and Edgewood enterprise zones. At least 30 municipalities and urban areas are within the Prince George's County zone.

Exhibit 3.22 shows the industries which have the greatest share of employment within enterprise zones that have a mixture of businesses. This includes all businesses and can differ from the businesses that actually claim credits, as described below for Baltimore City.

Exhibit 3.22
Industries with the Highest Employment
within Enterprise Zones by Region

<u>Region</u>	<u>Top Five Industries</u>
Capital Region	Retail Construction Accommodation/Food Services Administration/Support Services Professional/Science/Technical
Baltimore City	Health Care Education Administration/Support Services Accommodation/Food Services Professional/Science/Technical
Greater Baltimore	Manufacturing Retail Professional/Science/Technical Health Care Accommodation/Food Services
Eastern Shore	Health Care Manufacturing Retail Accommodation/Food Services Professional/Science/Technical
Western Maryland	Health Care Retail Warehousing/Transportation Accommodation/Food Services Finance

Source: U.S. Census Bureau; Department of Legislative Services

Employment Data for Businesses Claiming the Enterprise Zone Credit in Baltimore City

The Baltimore Development Corporation provided data on the 152 companies which submitted enterprise zone employment data in 2011. These companies reported employment of a little more than 13,000, which is about 7% of the total private employment within the zone. According to SDAT, about 300 Baltimore City properties were eligible for a property tax credit at this time in 2011; an unknown number of Baltimore City businesses were awarded income tax credits. Baltimore City does not impose any additional eligibility standards; as such, businesses that reported employment data within 16 different industries. The industries most represented in the reported data are manufacturing; retail; professional, science, and technical services; and accommodations and food services. Finance and insurance and manufacturing reported about one-half of the total employment whereas these industries comprise 12% of total private employment within the zone. Most of the reported net increase in employment resulted from businesses within the manufacturing, retail, health care, and accommodations and food services industries, as shown in **Exhibit 3.23**.

Exhibit 3.23
Baltimore City Business and Employment Data by Industry
Enterprise Zone Tax Credit

<u>Industry</u>	<u>Companies</u>	<u>Percent Total</u>	<u>Employment</u>	<u>Percent Total</u>	<u>2010-2011 Employment Change</u>
Agriculture & Forestry	1	0.7%	181	1.4%	-2
Construction	13	8.6%	821	6.3%	238
Manufacturing	23	15.1%	2856	21.8%	666
Wholesale Trade	13	8.6%	627	4.8%	237
Retail	15	9.9%	595	4.5%	472
Transportation/Warehousing	9	5.9%	522	4.0%	218
Information	2	1.3%	30	0.2%	-5
Finance and Insurance	4	2.6%	3,380	25.8%	73
Real Estate, Rental, and Leasing	6	3.9%	119	0.9%	24
Professional, Scientific, and Technical Services	15	9.9%	667	5.1%	215
Management of Companies	1	0.7%	23	0.2%	2
Administrative and Support Services	10	6.6%	658	5.0%	130
Educational Services	2	1.3%	95	0.7%	8
Health Care and Social Assistance	10	6.6%	858	6.6%	692
Accommodation and Food Services	18	11.8%	735	5.6%	225
Other Services (except Public Administration)	10	6.6%	932	7.1%	-25
Total	152		13,099		3,168

Source: Baltimore Development Corporation; Dun & Bradstreet; National Employment Time-Series Dataset; Department of Legislative Services

Tax Credits for Businesses that Depend on Local Demand May Have a Limited Economic Impact

Research indicates that many industries are dependent on local demand and/or have high substitution effects – gains in employment at one business might be at the expense of other businesses given a finite local demand. This can include businesses within the hotel, restaurant, retail, and health care industries. For example, the demand for restaurants is mostly dependent on the number of nearby residents and the disposable income of the residents.

The Louisiana Economic Development agency recently analyzed its Enterprise Zone program and estimated that 90% of enterprise zone jobs within industries dependent on local demand merely replaced existing jobs and limited the overall effectiveness of the program relative to nearby states, most of which limited credits to these industries. In response to the report's findings Louisiana enacted restrictions on the ability of retail businesses to claim the credit.

As shown in Exhibit 3.23 above, about 28% of the Baltimore City businesses that reported employment data in 2011 were within the health care, retail, and accommodations and food services industries. These businesses accounted for 44% of the reported 3,168 increase in employment, suggesting that a significant portion of the reported employment change was the result of increased demand within Baltimore City and not due to receipt of the Enterprise Zone credit. Supermarkets, convenience stores, pharmacies, and chain stores comprised most of the retail businesses. The accommodation and food services industry was comprised of 3 bars, 11 restaurants, and 4 hotels.

Local demand dependent industries comprise a significant portion of certified businesses within the Prince George's, Hagerstown, Takoma Park, Gaithersburg, and Wheaton enterprise zones. Chain restaurants and hotels comprised most of the Prince George's certified businesses in 2010 and a significant portion of certified businesses in Hagerstown. Virtually all of the certified businesses in the Wheaton zone are retail businesses or developers of retail property. However, Montgomery County appears to be adopting a comprehensive development plan for Wheaton and its other zones, similar to the development plan that was implemented for Silver Spring. For example, the county has designated the Wheaton area as a priority for development, offers additional incentives, and plans a number of initiatives to boost revitalization, including a transit-oriented development to attract businesses and residents and the development of a town center. The success of these other county initiatives in increasing local population and revitalizing the area will be a key determinant in the effectiveness in providing Enterprise Zone credits to these retail businesses.

Economic Impacts of Credit Can Differ Based on Property Ownership

A significant portion of businesses that claim the property tax credit in several zones are developers or real estate management companies. About one-third of the total businesses that have been certified in Baltimore City from 2001 to 2010 and have identifying information are developers or real estate companies. The economic impact of a credit provided to a real estate developer differs from a credit provided to a business that is also the owner of the property. The most important distinction is within the direct impacts – tax credits to businesses may increase

investment and jobs at the business whereas the impact of tax credits to developers is mainly through additional investment in nonresidential property. This will typically result in additional commercial property in nonindustrial zones which can increase the likelihood that a business locates within the zone by increasing the quantity or quality of commercial property. In these instances the investment did not necessarily “create” the jobs located at businesses within the property but could have increased the likelihood that a business located within the zone rather than a location outside the zone.

In both instances, however, the most important determinant of the credit’s effectiveness is the extent to which the development or business expansion/establishment was due to the credit and would not have happened in the absence of the credit. If the activity would have occurred in the absence of the credit, which research has typically shown is a majority of activity, the impact is more muted and comprised of the economic impacts from increasing the cash flow of the business or property developer’s return on investment, minus the offsetting cost of reducing State spending or increasing revenues to cover the net State cost of the credit.

Enterprise zones can have difficulties attracting businesses and residents due to poverty, unemployment, and other economic barriers present within the zone. Given the limited geography of zones, most of the indirect impacts of credits (additional construction spending and income) will not be recycled within the zone but will be realized in areas beyond the zone. Increased investment and business expansions and establishments may increase the assessable property tax base of the area, can revitalize areas which suffer from vacant buildings and a lack of property maintenance, and increase the attractiveness of the zone to businesses by increasing the supply or quality of office space. If investment is sufficient, it may re-invigorate the local property market and spur additional investment and businesses thereby increasing the attractiveness of the area. To date, the only clear evidence of this occurring is within the Silver Spring enterprise zone, which was part of a comprehensive effort by Montgomery County to revitalize that area.

Research indicates, however, that enterprise zone benefits may instead be capitalized into property values, therefore transferring resources from businesses to property owners. This shift in resources may reduce the amounts the businesses within zones would otherwise spend on capital assets or labor. A recent analysis of the Ohio Enterprise Zone program concluded that this impact was not likely in zones that were truly economically distressed but likely to occur in zones that were marginally distressed or not distressed at all. The analysis concluded that if an Enterprise Zone program expands, in particular to areas that are not truly distressed, it will dilute the effectiveness of incentives offered in areas that are actually distressed.

About 150 census tracts are located either fully or partially within the current Baltimore City enterprise zone. The Baltimore Develop Corporation and DBED calculate that the average poverty rate of all of these census tracts is higher than 125% of the U.S. family poverty rate, thereby qualifying the area for designation as an enterprise zone. However, there is considerable variation within the zone, about one-quarter of the census tracts do not meet any of the statutory requirements to be designated as an enterprise zone, and about 50 census tracts or one-third, do not qualify based on poverty rate. There is also significant variation in the amount of business activity within the zone.

A total of \$12.4 million or three-quarters of the total property tax credits claimed within Baltimore City in fiscal 2014 were awarded to businesses located within six census tracts. Five of these zones do not have a poverty rate that would qualify the tract for the program, while the sixth census tract qualifies but is no longer part of the enterprise zone. In addition, these census tracts are higher-income communities, have increased employment, and lower incidence of public assistance. In contrast, there have been no property tax investments in more than one-half of the census tracts located within the zone, these census tracts are lower-income communities, as shown in **Exhibit 3.24**.

Exhibit 3.24
Baltimore City Property Tax Credits by Census Tract
Fiscal 2014

<u>Area</u>	<u>Census Tracts</u>	<u>Credits (\$ in Millions)</u>	<u>Unemployment Rate</u>	<u>Mean Income</u>	<u>SNAP</u>	<u>Labor Force Participation</u>
<u>Enterprise Zone:</u>						
Top 6 Census Tracts	6	\$12.8	5.7%	\$50,702	8%	68.1%
No Projects	80	0	15.6%	38,399	22%	62.1%
Baltimore City	200	17.1	14.0%	41,085	20%	63.6%

Note: SNAP is receipt of Supplemental Nutrition Assistance Program.

Source: State Department of Assessments and Taxation; Department of Legislative Services

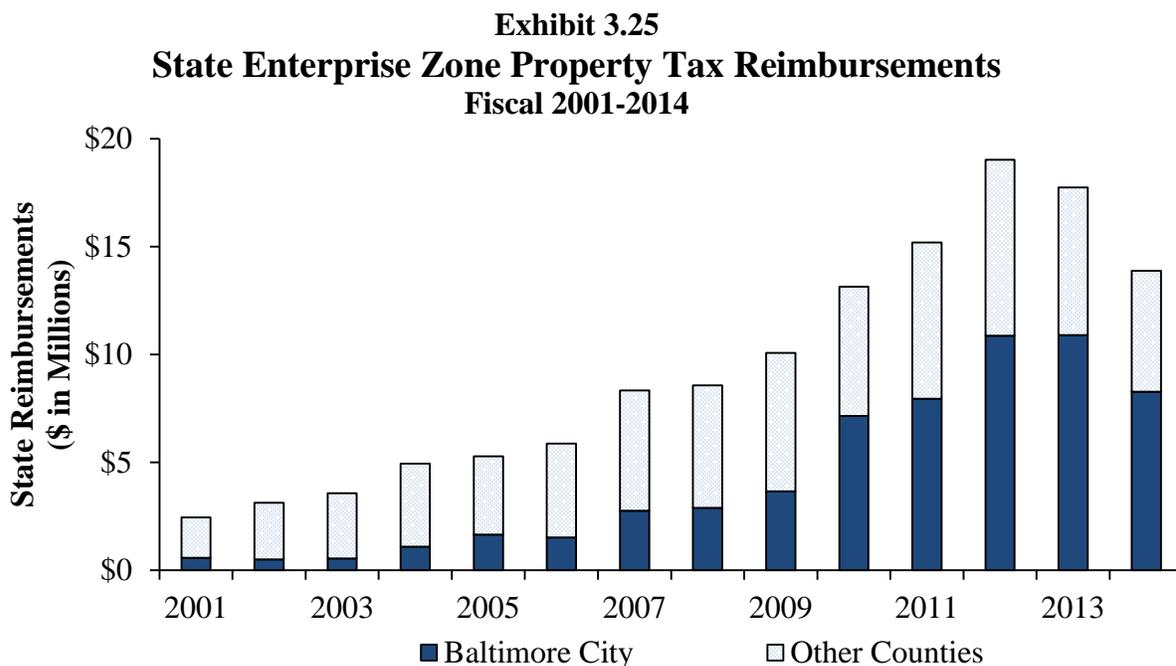
The federal New Markets Tax Credit is a similar tax credit program that aims to increase investment in lower-income communities. In contrast to the State Enterprise Zone program, the census tract in which a proposed project is located must meet program requirements, not just the entire zone spread out over many census tracts. The Baltimore City zone has expanded significantly within the last several years. As the zone has expanded it has increased the likelihood that the program focuses development within lesser distressed areas of the city at the expense of more distressed areas.

State and Local Revenue Impacts

State Reimbursements to Local Governments Have Increased Significantly Since Fiscal 2001, Although Reimbursements Have Decreased in the Last Two Fiscal Years

The State reimburses local governments for one-half of the cost of the Enterprise Zone property tax credit. The State budget includes this reimbursement as an appropriation within SDAT. From fiscal 2001 to 2014, State reimbursements to local governments totaled \$131.2 million.

State Enterprise Zone credit reimbursements have significantly increased since fiscal 2001. State reimbursements increased from \$2.5 million in fiscal 2001 to \$13.9 million in fiscal 2014, an average annual increase of 14%. SDAT reimbursements to Baltimore City totaled \$8.3 million or about 60% of the total amount reimbursed in fiscal 2014, as illustrated in **Exhibit 3.25**.



Source: State Department of Assessments and Taxation; Department of Legislative Services

The increase in reimbursements to Baltimore City accounts for about two-thirds of the net increase in State reimbursements over this period. Baltimore City reimbursements spiked three times – tripling from fiscal 2003 to 2005 and doubling in both fiscal 2007 and 2010. The remaining net increase in State reimbursements resulted mainly from growth in Baltimore, Cecil, Harford, Montgomery, and Prince George’s counties. Since 2001, reimbursements have increased by 23% annually in Baltimore City and 32% in both Montgomery County and Prince George’s County.

The largest percentage increase in total reimbursements occurred in fiscal 2007 when State reimbursements increased by 42%; this growth was driven by a \$1.2 million increase in reimbursements to Montgomery County. In contrast to this growth, reimbursements to Somerset County remained constant and decreased in Dorchester, Washington, and Worcester counties. **Exhibit 3.26** shows the State reimbursements and local property tax loss in each county for fiscal 2014.

Exhibit 3.26
State and Local Property Tax Credit Costs
Fiscal 2014

<u>County</u>	<u>State Cost</u>	<u>Local Cost</u>	<u>Total</u>
Allegany	\$259,900	\$259,900	\$519,800
Anne Arundel	0	0	0
Baltimore City	8,276,500	8,276,500	16,553,000
Baltimore	662,500	662,500	1,325,000
Calvert	33,300	33,300	66,600
Caroline	0	0	0
Carroll	0	0	0
Cecil	761,300	761,300	1,522,600
Charles	0	0	0
Dorchester	15,300	15,300	30,600
Frederick	0	0	0
Garrett	137,700	137,700	275,400
Harford	1,540,900	1,540,900	3,081,800
Howard	0	0	0
Kent	0	0	0
Montgomery	493,700	493,700	987,400
Prince George's	1,006,300	1,006,300	2,012,600
Queen Anne's	0	0	0
St. Mary's	41,600	41,600	83,200
Somerset	10,100	10,100	20,200
Talbot	0	0	0
Washington	485,800	485,800	971,600
Wicomico	151,700	151,700	303,400
Worcester	1,000	1,000	2,000
Total	\$13,877,500	\$13,877,500	\$27,755,000

Source: State Department of Assessments and Taxation; Department of Legislative Services

Despite the overall growth, State reimbursements have decreased by about one-quarter in the last two fiscal years. According to SDAT and DBED, the recent recession coupled with the phase in of lower property assessments has contributed to this decrease. Overall changes in the number of participating businesses appear to have a larger impact on reimbursements than changes in property tax values. A total of 352 businesses were eligible to receive a property tax credit in fiscal 2001; that number had tripled to 1,027 by fiscal 2012. Within the last two fiscal years the number of participating businesses fell by slightly less than total reimbursements (one-fifth).

Baltimore City Projects Receive Almost One-half of Overall State Tax Credit Reimbursements

The Baltimore City enterprise zone is the largest zone in the State, consisting of about 13,500 acres, and contains about one-half of the total population that lives within an enterprise zone community. From fiscal 2001 through 2014, State property tax credit reimbursements to Baltimore City totaled \$60.3 million, which was a little less than one-half of the total reimbursements over this time. Baltimore City reimbursements over this period increased by 23% annually. About 266 properties and \$1.1 billion in assessed property were eligible to receive a property tax credit during fiscal 2014.

About Two-thirds of the Fiscal 2014 Property Tax Credits for Baltimore City are from a Small Number of Projects

About 20 eligible properties in the city did not receive a credit because the current assessment does not exceed the base assessment. A little more than one-half of all city property credits were for less than \$10,000; these properties comprised about 2% of the total credits. Conversely, credits to the 15 city properties that received the largest property tax credits totaled \$11.1 million, about two-thirds of the total amount of credits. **Exhibit 3.27** shows the number of properties and credits by the amount of credit in fiscal 2014.

Exhibit 3.27 Baltimore City Enterprise Zone Property Tax Credits Fiscal 2014

<u>Credit Amount</u>	<u>Number</u>	<u>% Total</u>	<u>Total</u>	<u>% Total</u>
No Credit	20	7.5%	\$0	0.0%
\$10,000 or less	145	54.5%	350,900	2.1%
\$10,000 to \$50,000	61	22.9%	1,389,400	8.1%
\$50,000 to \$100,000	30	11.3%	1,969,000	11.5%
\$100,000 to \$500,000	22	8.3%	4,857,900	28.5%
\$500,000 to \$1.0 million	7	2.6%	5,502,900	32.2%
Over \$1.0 million	1	0.4%	2,997,600	17.6%
Total	266		\$17,067,700	

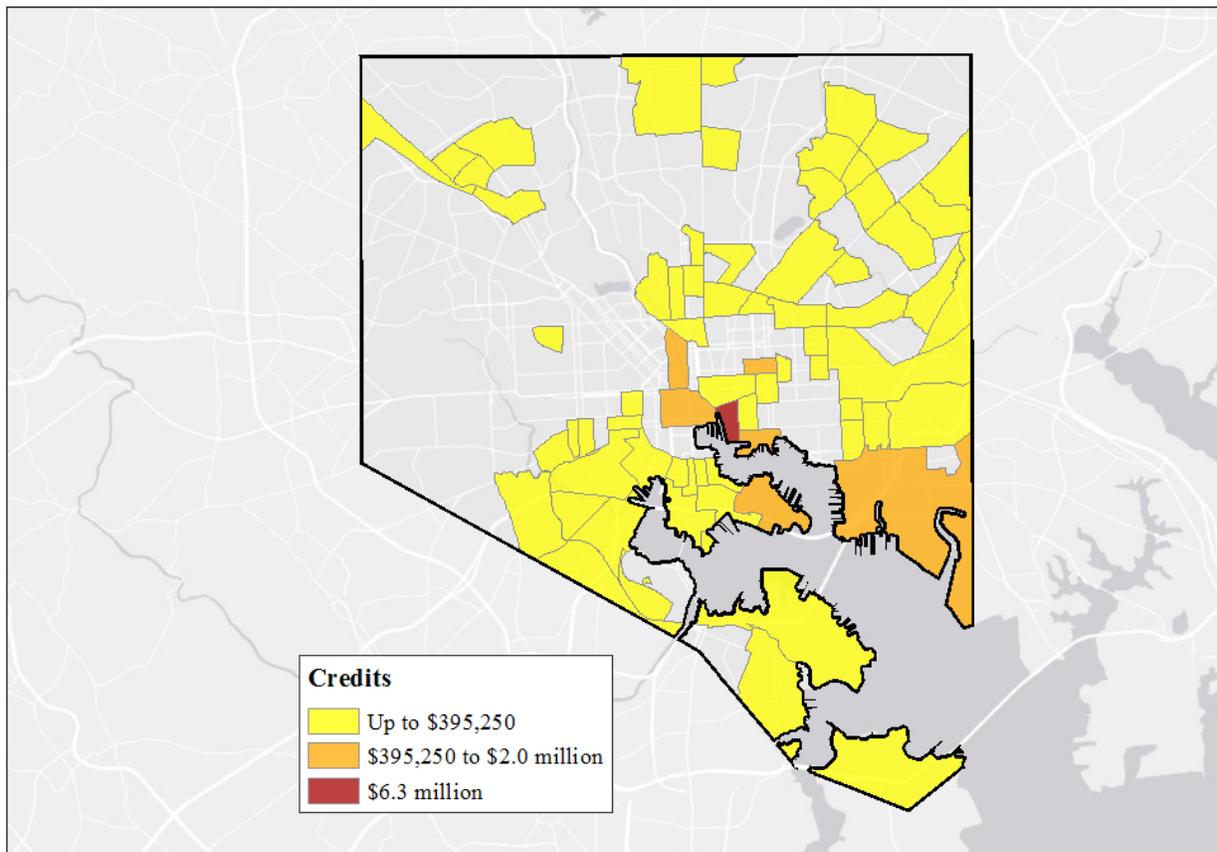
Note: Data is based on analysis of individual projects, the amount of credits shown here differ than that reported for Baltimore City by SDAT.

Source: State Department of Assessments and Taxation; Department of Legislative Services

Most Baltimore City Tax Credits Are For Inner Harbor Projects

Although the properties receiving Enterprise Zone property tax credits are dispersed throughout the city, most of the property tax credits are concentrated in the Inner Harbor area. The highest concentration of fiscal 2014 credits, about \$6.3 million or a little more than one-third of the total fiscal 2014 credits, is for properties located in the area to the east of Harborplace or the central Inner Harbor. **Exhibit 3.28** shows the amount of fiscal 2014 property tax credits by Baltimore City census tract.

Exhibit 3.28
Enterprise Zone Property Tax Credit
By Baltimore City Census Tract
Fiscal 2014

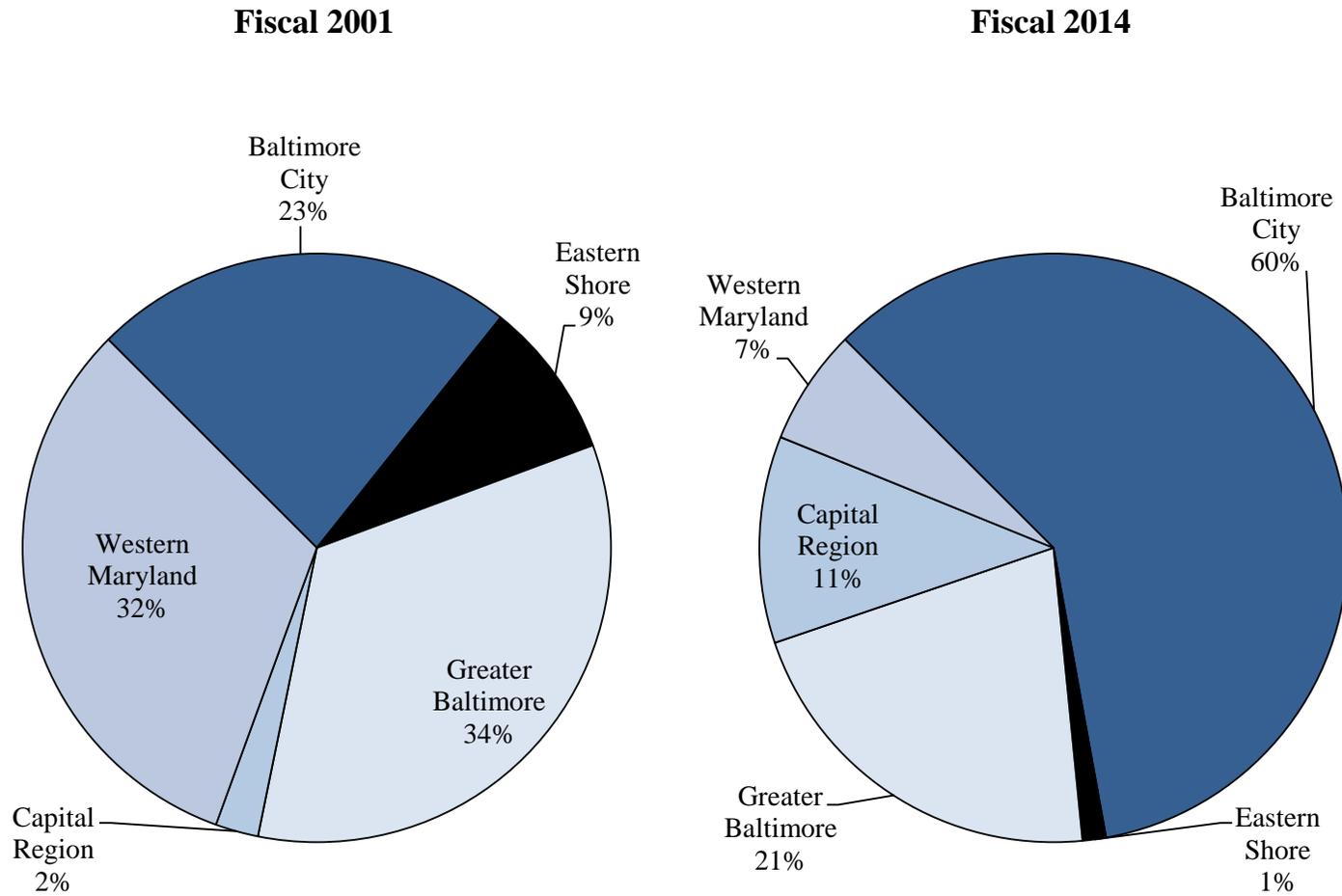


Source: U.S. Census Bureau; Department of Legislative Services

The Bulk of Property Tax Credits and Reimbursements Has Shifted to Enterprise Zones in Baltimore City and the Capital Region

Since fiscal 2001, Enterprise Zone property tax credits have reduced local property tax revenues by \$131.2 million. Property tax credits in Western Maryland and the Eastern Shore comprised 40% of all reimbursements in fiscal 2001 but decreased to 9% of all reimbursements in fiscal 2014. Conversely, property tax credits increased in Baltimore City and the Capital region from one-quarter of all reimbursements in fiscal 2001 to almost three-quarters in fiscal 2014. Anne Arundel, Caroline, Carroll, Charles, Frederick, Howard, Kent, Queen Anne's, and Talbot counties have no enterprise zones so they did not incur any costs associated with the Enterprise Zone program. **Exhibit 3.29** illustrates the shift in the distribution of property tax credits since 2001.

Exhibit 3.29
Enterprise Zone Property Tax Credits by Region



Source: State Department of Assessment and Taxation; Department of Legislative Services

Baltimore City's Planned Harbor Point Development and Amazon.com Facility Could Significantly Increase State and City Property Tax Credit Costs

The Harbor Point development is an approximately 3-million square-foot master-planned mixed-use community being built on a 27-acre waterfront site in Baltimore City. Harbor Point will include retail and office space, a hotel, apartments, and a number of public infrastructure projects, including parks and community open space, a promenade, and roads and utilities to complement privately financed buildings and privately financed public parking.

The project will be built in three phases over approximately 12 years and consists of nine planned buildings and related public infrastructure. The project represents an investment of just over \$1 billion in Baltimore City, consisting of \$921 million of private development costs that will be supplemented by approximately \$107 million of public infrastructure costs.

The project developer is eligible to take advantage of Enterprise Zone tax credits for each of the commercial buildings. The pre-development assessed value of the property is estimated at \$10.8 million and Baltimore City is collecting pre-development property taxes of approximately \$244,000 annually. At completion, the property is expected to be assessed at over \$1.8 billion and Baltimore City anticipates collecting an average of \$19.6 million in annual property taxes at full build-out.

The Enterprise Zone tax credits will be recognized over a 19-year period. If the project proceeds as planned, the last year of the Enterprise Zone tax credit will be the tax year starting July 1, 2032 (fiscal 2033). It is estimated that the project developer will be entitled to Enterprise Zone tax credits valued at \$88.4 million over the life of the project. The State will reimburse Baltimore City 50% of the total amount of the credits for a total reimbursement of \$44.2 million.

Amazon.com recently announced plans to open a 1 million square foot distribution center in Baltimore City. The company stated that it selected the site because of its proximity to a large customer base. According to published reports, DBED and BDC offered incentives totaling \$43 million, including Enterprise Zone tax credits (\$35.5 million), One Maryland credits (\$5.5 million), Brownfield and Job Creation credits (\$1.7 million), and a conditional loan of \$1.25 million which will be forgiven if certain conditions are met.

Annual Income Tax Credit Claims Have Been Relatively Modest

Since tax year 2000, an average of \$900,000 in Enterprise Zone income tax credits have been claimed. In tax year 2010 about 100 tax returns claimed \$634,900 in income tax credits, as shown in **Exhibit 3.30**. By comparison, 850 properties claimed \$30.4 million in property tax credits. In contrast to the rapid growth of the property tax credit, the total amount of income tax credits has grown by less than 1% annually. While income tax credits consisted of almost 20% of the enterprise zone total costs for the State in tax year 2000, income tax credits now make up only 4% of the enterprise zone total costs in tax year 2010. In fiscal 2011, businesses averaged \$6,478 in Enterprise Zone income tax credits and \$17,791 in Enterprise Zone property tax credits.

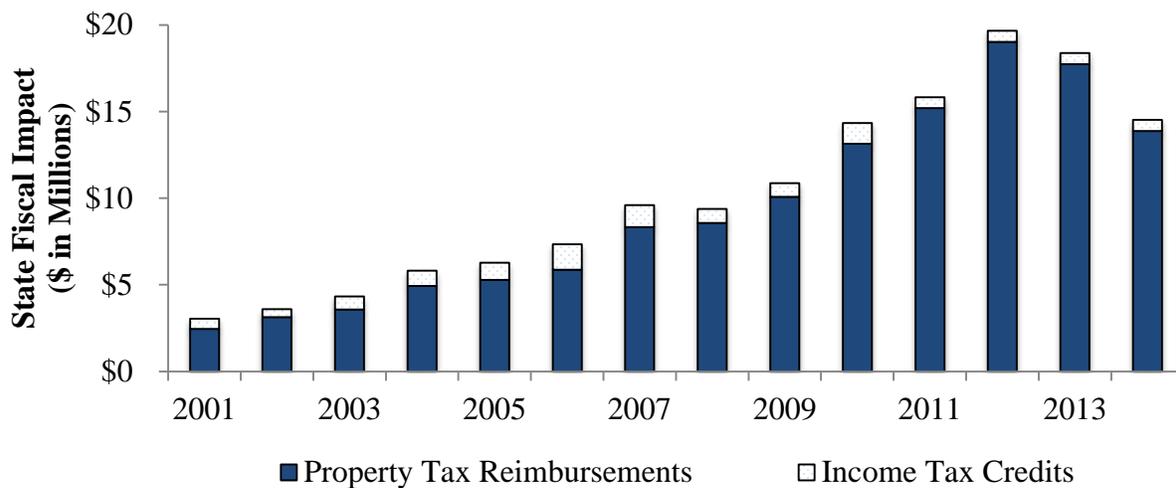
Exhibit 3.30
Enterprise Zone Income Tax Credits
Tax Years 2000-2010

<u>Tax Year</u>	<u>Tax Returns</u>	<u>Credit</u>	<u>Average</u>
2000	125	\$587,356	\$4,699
2001	83	463,483	5,584
2002	86	768,042	8,931
2003	110	881,044	8,009
2004	117	1,006,097	8,599
2005	111	1,464,866	13,197
2006	81	1,256,951	15,518
2007	101	809,834	8,018
2008	130	788,575	6,113
2009	93	1,197,890	12,881
2010	98	634,892	6,478

Source: Comptroller's Office; Department of Legislative Services

Exhibit 3.31 shows in each fiscal year the total State income tax credits claimed and State property tax reimbursements.

Exhibit 3.31
Total State Income Tax Credits and Property Tax Reimbursements
Fiscal 2001-2014



Note: Fiscal 2012-2014 assume a constant amount of income tax credit claims.

Source: State Department of Assessments and Taxation; Comptroller's Office; Department of Legislative Services

According to DBED and local governments, many businesses are eligible to claim the income tax credit but fail to do so because the credit value does not justify the perceived amount of time necessary to claim the credit. In addition, DBED indicates that businesses have indicated that the income tax credit that may be claimed for economically disadvantaged workers is also underutilized due to the perceived difficulty in receiving certification for those workers from DLLR. In order to claim the credit, the business must be aware that a potential hire is a member of an economically disadvantaged household. According to DBED, potential hires are hesitant to self-identify as economically disadvantaged during the interview process either due to a lack of knowledge about the program or the potential stigma of doing so.

Chapter 4. Findings and Recommendations

Based on the information and analysis provided in this report, the Department of Legislative Services (DLS) recommends that changes to the Enterprise Zone tax credit be made to improve the credit's effectiveness as discussed below.

Enterprise Zone Tax Credits Are Not Effective in Creating Employment Opportunities for Enterprise Zone Residents

While Enterprise Zone tax credits may incentivize some businesses to create additional jobs within enterprise zones, the tax credit is not effective in providing employment to zone residents that are chronically unemployed and/or live in poverty. A number of factors contribute to this problem, including skills mismatches for new jobs created, lower than average educational attainment levels of zone residents, and labor mobility. As such, improved educational opportunities and/or additional job training programs for residents may be more effective in enabling those residents to better compete for jobs created in enterprise zones.

In addition, annual claims for the Enterprise Zone income tax credit have been modest, particularly when compared to the property tax credit. The Department of Business and Economic Development (DBED) indicates that this could be in part due to administrative burdens that contribute to low utilization rates of the enhanced income tax credit that can be claimed for hiring members of an economically disadvantaged household.

Recommendation: DBED and the Department of Labor, Licensing, and Regulation (DLLR) should propose statutory changes that will improve the likelihood that residents in enterprise zones and enterprise zone communities, particularly those that are in poverty and/or chronically unemployed, can gain employment within enterprise zones. DBED and DLLR should also propose methods by which other State and local programs that seek to improve job skills and educational attainment levels, such as job training programs, can be better coordinated with the Enterprise Zone tax credit.

Recommendation: DBED, in consultation with the Comptroller's Office, should propose statutory changes to the Enterprise Zone income tax credit that will help increase net employment, including reducing administrative burdens and a mechanism that incorporates job reductions at similar sites or other locations in the State.

In a Significant Number of Enterprise Zones, Few Businesses Are Claiming the Property Tax Credit

Of the 30 current enterprise zones, 13 zones have less than 10 businesses claiming Enterprise Zone property tax credits. Not only are these enterprise zones failing to attract many businesses, but a number of the businesses claiming the tax credit are not making significant investments in those zones. While the geographic size and location of the zones do not appear to

explain the lack of activity in some zones, other reasons may contribute to the lack of activity. Possibilities for why zones have failed to attract businesses are poor marketing and targeting of zones, competition from other nearby zones, and that the credits are simply not enough of an incentive to overcome economic barriers. Each political subdivision is authorized to establish additional local standards to govern access to the program. Many local jurisdictions generally require a minimum capital investment or a minimum number of jobs created, or both. A few enterprise zones also have additional standards limiting the type or category of business entity that is eligible to participate.

Recommendation: DBED should comment on the potential reasons for the lack of activity in some enterprise zones, the variation in program effectiveness across zones, and the role of local standards in attracting businesses to enterprise zones, specifically as whether those local standards are beneficial or a detriment to encouraging businesses to locate in enterprise zones.

DBED and the Comptroller's Office Do Not Assess the Effectiveness of the Enterprise Zone Tax Credit

DBED and the Comptroller's Office are required by law to annually assess the effectiveness of tax credits provided to businesses in enterprise zones, including the number and amount of credits granted and the success of the tax credits in attracting and retaining businesses within enterprise zones. While DBED tracks the number and amount of credits granted annually, it does not have a framework or metrics in place for measuring the actual effectiveness of the credit. There is also a lack of accurate data on the change in employment and number of businesses within enterprise zones, which makes assessing the impacts of the credit very difficult.

Recommendation: DBED, in consultation with the Comptroller's Office and the State Department of Assessments and Taxation (SDAT), should adopt formal metrics and a framework for analyzing the cost-effectiveness of each enterprise zone and the effectiveness of each zone in attracting businesses and increasing employment. DBED should identify clear outcomes and determine quantifiable measures, which could include project evaluation, employment trends, impacts on poverty and population, private-sector investment in communities, and overall community revitalization.

In addition, DBED, in consultation with SDAT and local jurisdictions, should adopt procedures that will facilitate more accurate collection of enterprise zone data to enable evaluation of the program.

Enterprise Zone Expansions Have Become More Prevalent in Recent Years, Diluting the Impacts of Zones and Increasing State and Local Credit Costs

State reimbursements to local jurisdictions for 50% of Enterprise Zone tax credit costs are subject to an annual appropriation in the State budget. However, there is no limit on the maximum amount of reimbursements. State reimbursements have greatly increased in recent years, from \$2.5 million in fiscal 2001 to \$13.9 million in fiscal 2014, an average annual increase of 14%. There are few limitations on zone expansions and no specific criteria related to zone expansion requirements. In addition, a handful of enterprise zones are large enough to have one or more focus areas within the zone. State reimbursement costs may also increase significantly as credits are granted for new development projects, particularly for the Harbor Point and Amazon.com developments in Baltimore City.

Recommendation: DBED should propose statutory changes that will provide for evaluation criteria that must be considered before an enterprise zone may be expanded. These criteria could include restrictions on the size of any expansion, whether businesses have expressed interest in locating within the potential area of expansion, and whether basic infrastructure is in place in order to facilitate business development within the proposed expansion area.

Recommendation: DBED should comment on whether focus areas within enterprise zones have actually increased employment and economic development in those areas above and beyond what would have otherwise occurred within the zone with the general Enterprise Zone credit.

Recommendation: DBED should comment on whether a cap on the maximum amount of State reimbursements that may be granted each year should be imposed.

Some Baltimore City Enterprise Zone Property Tax Credits Have Been Erroneously Calculated

Recent press reports and a performance audit conducted by the Office of Legislative Audits determined that there were errors in several property tax credit programs including the Enterprise Zone, Homestead, and Baltimore City Historic tax credits. The press reports also documented that \$700,000 in improper Enterprise Zone property tax credits were granted to properties located in Baltimore City. Potential errors including granting the credit to ineligible properties, using the incorrect pre-improvement base year assessments, applying the incorrect credit percentage, and not using the correct assessment when the property owner successfully appealed for a lower assessment. For this report, DLS requested that SDAT provide Enterprise Zone property tax credit data – SDAT was only able to partially fulfill the request and only after a significant delay. This delay prevented DLS from fully analyzing the data and assessing whether tax credits have been accurately calculated.

Recommendation: DLS recommends that SDAT comment on:

- Whether SDAT, DBED, and local zone administrators' current tax credit calculation procedures are sufficient to properly (1) calculate the current credit assessment if a property owner successfully appeals an assessment; (2) value the pre-improvement base year property assessment of the property; (3) assign the correct percentage of the credit based on which year the property is claiming the credit; and (4) exclude the value of residential property from the credit.
- The lack of standardization of the administration of the credit across counties, including (1) the reasons for differences in SDAT procedures used in counties; (2) the sources of discrepancies between initial and final credit determinations; and (3) how tax credit calculations for properties will be handled going forward through a new assessment administration system, AVS.

In addition, the evaluation committee may wish to consider asking the Office of Legislative Audits to conduct a performance audit of the Enterprise Zone property tax credit program.

Collection of Enterprise Zone Property Tax Credit Data Is Not Standardized

SDAT provided DLS a summary report of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone. While the data contained in the summary report and computation worksheets should have been sufficient to evaluate the Enterprise Zone property tax credit, some of the data that SDAT provided DLS was incomplete and/or inaccurate.

There is a lack of standardization in the data that each county assessment office provides about properties claiming the Enterprise Zone property tax credit. Many counties do not provide information such as the prior credit year, the credit recipient's address, or other basic identifying information such as the zone in which the property is located. Data errors included incorrect base year assessments, using the wrong percentage of the eligible assessment to calculate the credit, and basic data entry errors. The methodology and processes used for reporting data is generally unsophisticated and often necessitates the manual entry of information. In addition, the summary reports of the individual enterprise zones and computation worksheets for companies claiming the credit in each zone did not match the aggregate data that SDAT provided. With such disparities in the data, it was impossible for DLS to determine if SDAT correctly calculated the State's reimbursement for half of the Enterprise Zone property tax credit.

Many of these issues will likely be resolved with SDAT implementing AVS. AVS will standardize the data so information, like a business's physical address, will be reported. Additionally, the system will automate the calculation of the credit so only the base year assessment will be entered manually, thereby reducing the chance of data entry errors. Through

AVS, a spreadsheet can be compiled using the summary report and the computation worksheets, thus eliminating disparities in the data.

Recommendation: Procedures should be adopted that provide for uniform Enterprise Zone tax credit data collection procedures in each county. Ideally, the data collected for each credit recipient would contain the following information for all years that the business is eligible to receive the credit:

- company name and employer identification number;
- address of the company and address of the enterprise zone property;
- type of company;
- county and enterprise zone;
- current assessment and base assessment of the property;
- assessment subject to the credit;
- year the property began receiving the credit; and
- the number of years it has been receiving the credit.

SDAT should also continue to work with local assessment offices to reduce the amount of data that is manually entered and improve its ability to provide data in an accurate and timely fashion through AVS. SDAT should comment as to whether additional resources would be required to implement these changes.

Appendix 1
Local Enterprise Zone Capital Investment
And Job Creation Requirements

Enterprise Zone	Capital Investment Requirements	Job Creation Requirements
Baltimore City	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
North Point	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Southwest Baltimore County	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Woodlawn	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Edgewood	<ul style="list-style-type: none"> • At least \$50,000 	<ul style="list-style-type: none"> • At least 5 jobs
Aberdeen/Havre de Grace	<ul style="list-style-type: none"> • At least \$75,000 for a business with 10 or less employees • At least \$125,000 for a business with 11 or more employees 	<ul style="list-style-type: none"> • At least 2 jobs for a business with 10 or less employees • At least 5 jobs for a business with 11 or more employees
Long Branch/Takoma Park ¹	<ul style="list-style-type: none"> • The minimum qualifying capital investment is \$10 per sq. ft. of building floor area improved • At least 20% of the total building floor area must be improved 	<ul style="list-style-type: none"> • A business must show a net increase of at least 35 work hours per week for each employment tax credit • A business must show an increase in employees of 5% to a minimum of 1 employee
Wheaton ¹	<ul style="list-style-type: none"> • The minimum qualifying capital investment is \$10 per sq. ft. of building floor area improved • At least 20% of the total building floor area must be improved 	<ul style="list-style-type: none"> • A business must show a net increase of at least 35 work hours per week for each employment tax credit • A business must show an increase in employees of 5% to a minimum of 1 employee
Olde Towne ¹	<ul style="list-style-type: none"> • A minimum qualifying capital investment of \$250,000 is required for new construction and additions 	<ul style="list-style-type: none"> • None

Enterprise Zone	Capital Investment Requirements	Job Creation Requirements
	<ul style="list-style-type: none"> • Renovations with no expansion of floor area require a minimum qualifying capital investment of at least \$10 per sq. ft., and at least 50% of the total building floor area must be improved 	
Glenmont	<ul style="list-style-type: none"> • The minimum qualifying capital investment is \$10 per sq. ft. of building floor area improved • At least 20% of the total building floor area must be improved 	<ul style="list-style-type: none"> • A business must show a net increase of at least 35 work hours per week for each employment tax credit • A business must show an increase in employees of 5% to a minimum of 1 employee
Prince George's County	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Cecil County	<ul style="list-style-type: none"> • A business presently located and operating in Cecil County that relocates from outside the zone to within a zone may be eligible for incentives if the assessable value of the land and building located in the zone exceeds the assessed value of the land and building located outside the zone by 50% or more 	<ul style="list-style-type: none"> • A business presently located and operating in Cecil County that relocates from outside the zone to within a zone may be eligible for incentives if total employment of the business increases by a minimum of 50% during a 12-month period
Cambridge	<ul style="list-style-type: none"> • New and existing companies in the Central Business District must either meet the job creation requirement or make a capital investment of at least \$5,000 • New and existing companies within areas zoned as industrial must either meet the job creation 	<ul style="list-style-type: none"> • New and existing companies in the Central Business District must either meet the capital investment requirement or create 1 new job above a base employment level • New and existing companies within areas zoned as industrial must either meet the capital

Enterprise Zone	Capital Investment Requirements	Job Creation Requirements
	requirement or make a capital investment of at least \$50,000	investment requirement or create 5 new jobs above a base employment level
Hurlock	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Crisfield	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Princess Anne	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Fruitland	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Salisbury	<ul style="list-style-type: none"> • A business must invest at least \$50,000 	<ul style="list-style-type: none"> • A business must create at least 2 jobs
Berlin	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Pocomoke City	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Snow Hill	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Gateway	<ul style="list-style-type: none"> • Existing businesses in the zone must make an unspecified investment or demonstrate the required job creation • A business existing in the zone, which has been previously certified, may make a capital investment of \$200,000 and be exempt from all employment standards 	<ul style="list-style-type: none"> • An existing business that does not make an capital investment must demonstrate a 5% increase in employment to a minimum of 1 new job above a base employment level within a reasonable time period as determined by the Enterprise Zone Advisory Committee • A business relocating in the zone must (1) demonstrate a 10% increase in employment over its previous high level for the preceding 5 years; (2) the increase in employment must have occurred within the first year of operation in the zone; and (3) the Enterprise Zone Advisory Committee must agree by majority opinion that it was impossible for the business to have expanded at its previous location • Businesses that are

Enterprise Zone	Capital Investment Requirements	Job Creation Requirements
		<p>certified as eligible for Enterprise Zone program participation must be recertified annually. Businesses previously certified as eligible, who have been in the program for 10 years, will be given an adjusted employment base determined by the average number of employees that company had for years 6 through 10 of its original certification</p>
Frostburg/Allegany County	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Rt. 220 South/Allegany County	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Existing businesses in the zone must demonstrate a 5% increase in employment to a minimum of 1 new job above a base employment level within a reasonable time period as determined by the Enterprise Zone Advisory Committee • A business relocating in the zone must (1) demonstrate a 10% increase in employment over its previous high level for the preceding 5 years; (2) the increase in employment must have occurred within the first year of operation in the zone; and (3) the Enterprise Zone Advisory Committee must agree by majority opinion that it was impossible for the business to have expanded at its previous location

Enterprise Zone	Capital Investment Requirements	Job Creation Requirements
Keyser's Ridge	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Northern Garrett Industrial Park	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Southern Garrett Industrial Park	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Hagerstown	<ul style="list-style-type: none"> • In the Central Business District a minimum \$5,000 capital investment is required • Outside the Central Business District a minimum \$50,000 capital investment is required 	<ul style="list-style-type: none"> • Job creation requirements are for the State Income Tax Credits • In the Central Business District a minimum of 1 new job must be created • Outside the Central Business District a minimum of 5 new jobs must be created
Town of Hancock	<ul style="list-style-type: none"> • In the Central Business District a minimum of \$5,000 capital investment is required 	<ul style="list-style-type: none"> • Job creation requirements are for the State Income Tax Credits • In the Central Business District a minimum of 1 new job must be created
Washington County Airport	<ul style="list-style-type: none"> • In the Central Business District a minimum of \$5,000 capital investment is required 	<ul style="list-style-type: none"> • Job creation requirements are for the State Income Tax Credits • In the Central Business District a minimum of 1 new job must be created

¹Construction of new parking facilities, or improvements to existing parking facilities, are not eligible for tax credits.

Appendix 2
Local Enterprise Zone Industry Requirements

Industry	Enterprise Zone								
	Woodlawn	Edgewood	Aberdeen/ Havre de Grace	Cambridge	Gateway EZ	Rt. 220 South	Hagerstown	Hancock	Washington County Airport
Manufacturing	✓	✓	✓	✓	✓				
Fabrication	✓	✓	✓						
Assembly	✓	✓	✓						
Warehousing	✓	✓	✓	✓	✓	✓	✓	✓	✓
Distribution	✓	✓	✓		✓				
Offices	✓	✓	✓	✓	✓	✓	✓	✓	✓
Research and Development	✓	✓	✓	✓	✓	✓	✓	✓	✓
Community Facilities	✓				✓	✓			
Retail		✓	✓	✓	✓		✓	✓	✓
Services		✓	✓	✓	✓		✓	✓	✓
Tourism Activities			✓	✓	✓	✓			
Hospitality Services			✓						
Professional or Personal Commercial Services			✓	✓		✓			
Residential Services					✓				

Appendix 3. Studies of Enterprise Zone Programs

The concept of enterprise zones began in 1978 in Great Britain as a means to encourage local economic development in distressed communities. The Enterprise Zone program was established in Maryland in 1982 with two enterprise zones in two jurisdictions as an economic development tool to stimulate business investment and job creation through the use of real property and employment tax credits. It has since grown to include 30 enterprise zones throughout the State.

The federal government passed the Empowerment Zone and Enterprise Community Act in 1993. By 1995 over half of the states had Enterprise Zone programs, and as of 2008, 43 states had programs. While most states have Enterprise Zone programs, the programs differ vastly. The prevalence of enterprise zones varies from only 1 zone in New Mexico to more than 1,700 zones in Louisiana. Goals of the program vary from curbing population flight in Michigan's inner city neighborhoods to improving community infrastructure in New Jersey. Additionally, the programs have different requirements and incentives.

This section provides an overview of various academic studies that have attempted to determine whether enterprise zones have been effective in achieving their objectives of promoting business development and job creation in economically distressed areas.

Challenges of Evaluating Enterprise Zones

Despite the increased popularity of enterprise zones over the last 30 years, academic studies have not provided definitive evidence that enterprise zones have achieved their goals. Much of the variation in enterprise zone studies stems from the challenges of evaluating the effectiveness of enterprise zones. Neumark and Kolko (2010) summarize those challenges as (1) precisely identifying the targeted areas; (2) selecting appropriate control groups; (3) differentiating the effects of enterprise zone policies from other policies; and (4) measuring outcomes in line with program goals. Additionally, variations in program characteristics make it difficult to come to broad generalizations of the effectiveness of Enterprise Zone programs.

Most enterprise zones do not perfectly coincide with zip codes or census tracts. Thus studies that use zip codes or census tracts likely have measurement errors because they incorrectly assign areas as inside or outside of enterprise zones. This measurement error leads toward a bias of finding enterprise zones ineffective. Bondonio and Greenbaum investigated state-specific policy features across 10 states and the District of Columbia by assigning a zip code as an enterprise zone if any portion of an enterprise zone was within the zip code. Bondonio and Greenbaum admit this method is not ideal since it might lead to underestimating the enterprise zones' levels of distress, and they found enterprise zones did not have a statistically significant net impact on economic growth outcomes. O'Keefe examined the impact of California's Enterprise Zone program on employment growth at the census tract level by

comparing census tracts that received the enterprise zone designation to similar census tracts that did not receive the designation. She found that the enterprise zone designation raises employment growth approximately 3% each year for the first six years after designation, but then the effect disappears in later years. The bias that stems from measurement error is mitigated by employing geographic mapping methods, which constructs precise boundaries of enterprise zones using GIS maps.

Another issue that researchers face is selecting appropriate control groups for comparison. Comparing an enterprise zone to a control group is a way to estimate how much economic growth would have occurred without the program. The ideal control group would be identical to the enterprise zone except that it is not designated as an enterprise zone. Some studies use broad control groups such as all areas within a state that are not in an enterprise zone. Peters and Fisher looked at 13 states as a whole and compared them to the enterprise zones within those states and found that enterprise zone incentives had no significant impact on local establishment growth. Another approach is to select control groups based on characteristics of the enterprise zones or proximity to the enterprise zones. However, propensity score matching, which bases control groups on characteristics, fails to account for unobservable differences, which could cause an enterprise zone to be predisposed to grow faster than areas not in the enterprise zone. O'Keefe uses a propensity score matching model to match enterprise zone census tracts to nonenterprise zone census tracts and finds no long-term effect on employment growth. Boarnet and Bogart concluded that the Enterprise Zone program in New Jersey had no significant impact on employment or property values by comparing enterprise zones to municipalities that qualified but were not designated as enterprise zones. Some studies compare enterprise zones to areas right outside of the enterprise zone in a methodology known as the border effect. The border effects methodology assumes that unobservable characteristics are unlikely to differ between businesses in a small geographical area.

Areas within enterprise zones usually qualify for other geographically targeted policies, so it is hard to distinguish the effects of the Enterprise Zone program from other programs. In Maryland, a business can qualify for the Enterprise Zone income tax credit and various other State tax credits, along with the federal Work Opportunity Tax Credit (WOTC) and the federal Empowerment Zone Tax Credit. Approximately 5% of enterprise zones are also federal empowerment zones or federal enterprise communities, and approximately 10% of federal empowerment zones and 20% of federal enterprise communities are also state enterprise zones. Ham, *et al.*, measures the impact of state enterprise zones, federal empowerment zones, and federal enterprise community programs using census tract data. The authors found that all three programs have a positive impact on local labor markets but that federal empowerment zones and federal enterprise community programs have a much greater effect than state enterprise zones in terms of the unemployment rate, poverty rate, wage and salary income, and employment.

The challenges of evaluating enterprise zones have led researchers to approach the methodology of enterprise zones differently. One must account for all of the other factors that affect local growth before the impact of enterprise zones alone can be measured, so researchers

have gone about this in different ways. There are three basic methodologies for evaluating enterprise zones, which are through surveys, case-study analysis, and regression analysis. Survey studies are biased toward showing larger increases in employment or income because they rely on representations made by businesses and other respondents who tend to benefit from the existence of enterprise zones. Also, response rates for surveys tend to be low and those directly involved in the issues may not be the ones completing the surveys. A case-study approach compares economic growth levels before and after the implementation of an Enterprise Zone program, but this approach fails to consider other factors that may have caused growth. Shift-share analysis, a more sophisticated case-study method, tries to isolate job growth within the enterprise zone from job growth related to a larger geographic region. While this method is preferable over the survey method, it still fails to control for all other factors that could account for growth in the enterprise zone, it can only compare two time periods, and it assumes that growth within the enterprise zone is proportionate to growth within the larger geographic region. Regression analysis avoids the limitations of surveys and shift-share analysis by statistically measuring the extent to which various factors impact the desired variable. A difference-in-difference methodology compares an enterprise zone to a nonenterprise zone over time, but it assumes that unobservable factors do not vary over time. This methodology assumes that enterprise zones do not have fundamentally different growth trends.

Given all of the challenges of evaluating enterprise zones, it is not surprising that researchers have not been able to agree on the effectiveness of enterprise zones in spurring economic growth. Up to the 1990s, most academics thought economic development incentives had only a marginal impact on business location decisions, and thus on the creation of new investment and jobs. However, in the 1990s opinion changed to thinking lower taxes or more incentives would cause greater economic growth. The consensus changed due to improvements in econometric modeling and increased tax and incentive differentials across states and cities. More recent studies have found ambiguous effects of enterprise zones on economic growth.

Economic Theory Behind Enterprise Zone Programs

An Enterprise Zone program is a tool that many state governments use to encourage economic development in designated locations, which are often economically distressed areas. An Enterprise Zone program tends to be different from other economic development programs in that the program is geographically targeted for investment in economically depressed areas. Supporters of Enterprise Zone programs believe enterprise zones are needed to overcome economic barriers of businesses, the decentralization of cities, and poor labor markets.

Economically distressed areas typically experience high economic costs to do business, such as poor access to transportation, labor, and capital. These areas may also have high crime and environmental compliance issues. Thus, compared to the rest of the state, economically distressed areas tend to have higher levels of unemployment, lower incomes, less jobs or well-paying jobs, and more unused land or blighted structures. These economic barriers, which include transportation problems, lack of financial capital, few skilled workers, high crime rates,

and land requiring environmental cleanup expenses, presumably raise the cost of doing business and impede economic activity in the area. Economic principles suggest that lower taxes and less regulation can increase jobs and incomes by reducing the cost of doing business. By reducing economic burdens, the government attracts capital, labor, and economic activity in those targeted areas. Greenstone and Looney claim, “attracting new businesses to distressed areas would provide new jobs, raise wages, and provide local services.”

Besides overcoming economic barriers, another economic argument for Enterprise Zone programs is the spatial mismatch hypothesis. The spatial mismatch hypothesis claims that businesses have been moving from the cities to the suburbs as a result of various developments, like trucks and the interstate highway system. This decentralization led to inner cities losing employment opportunities and the middle class moving out of the city. Public transit was built, but on the basis of moving workers downtown, not to low-density suburban work sites. High costs and racial discrimination in the suburban housing market have prevented the economically disadvantaged inner-city residents from moving easily to the suburbs. Consequentially, there is a concentrated population of economically disadvantaged people in the inner cities who find working in the suburbs difficult. Enterprise Zone programs are used as a way to bring jobs to those in the inner cities who are unable to commute.

Lastly, Enterprise Zone programs can shift employment from tight labor markets to labor surplus markets (high unemployment areas), thus raising overall employment. A decrease in the unemployment rate from 15% to 14% may have a larger positive impact on a community than a decrease in the unemployment rate from 5% to 4%. Additionally, it can offset program costs from increases in workers’ tax liability and a decrease in transfer payments to those on welfare. Employment demand shocks, like those created by Enterprise Zone programs, have positive long-term employment, labor force participation, and income effects.

Enterprise zone theory assumes that state officials can identify Enterprise Zone tax incentives that can overcome economic barriers and that conditions in the enterprise zone will allow for businesses to be profitable in the long run. Tax incentives should be set so that an enterprise zone can offer equal or higher returns to businesses than in other areas. Some businesses may require additional incentives to compensate for the political risk of legislative changes or repealing the enterprise zone. The tax incentives need to be large enough to entice businesses to invest in the enterprise zone, but not too large so that the program merely raises the public cost without adding benefits. It is possible that tax incentives at the cost of local public services may reduce, rather than increase economic activity. Ideally, the Enterprise Zone’s tax incentives would be set so that the marginal social benefits caused by the Enterprise Zone program would equal the marginal social costs of the program. However, valuing the social costs and benefits is a difficult task because it involves assigning a monetary value to nonmonetary items, such as crime, blight, and other social issues.

Additionally, enterprise zone theory assumes that the enterprise zones increase overall growth, and it is not merely speeding up when the growth occurs or shifting the growth from a nearby location. Enterprise Zone programs should not merely induce an investor to locate in the

enterprise zone instead of right outside of the enterprise zone, but rather the enterprise zones should bring new businesses to the region. The program should also bring sustained growth, so that a business does not end operations when the tax incentives expire.

Do Enterprise Zone Incentives Factor into Business Location Decisions?

Researchers have argued that enterprise zones are ineffective at influencing business location choices. Most experts agree that businesses tend to be reluctant to move long distances in response to state and local tax breaks. However, some believe that enterprise zones can play a role on location choices on the local level.

State and local business taxes do not account for a large share of a business's activity so taxes should not be a big influencing factor on location decisions. State and local business taxes make up only 4% of Maryland's private-sector gross State product in 2012 so taxes are only a small share of a business's activity. Other considerations play a larger role in determining where a business will locate, such as being strategically located near suppliers and customers. In reviewing enterprise zone studies, Wilder and Rubin stated, "traditionally recognized location factors such as proximity to markets and transportation access were consistently acknowledged as more critical than development incentives in site selections." The U.S. Government Accountability Office's (GAO) 1988 study concurred with this assessment by surveying select Maryland employers on location decision factors. GAO determined financial incentives were relatively unimportant factors while market access was of great or very great importance to most respondents. Community and site characteristics also ranked high in importance on location decision factors. Only 14% of respondents cited financial inducements of great or very great importance to their location decision, while 60% of respondents rated financial inducements of little or no importance. This is consistent with survey findings of other states. Lister found 55% of firms surveyed in California ranked enterprise zone designation of little or no importance to their location decision.

Tax differences become more important in determining location when other factors, such as wage rates, and access to markets and inputs are similar across localities, as they are likely to be within a metropolitan area. By reviewing literature on enterprise zones, Wilder and Rubin claim enterprise zones incentives became important when the more central factors for competing locations were equal.

However, Billings finds that enterprise zones have no effect on where new establishments locate in Colorado by comparing mean values of the number of new establishments and the number of establishments lost in an enterprise zone to a nonenterprise zone border area. He bases his analysis on the assumption that location characteristics drive a business's location decision, but for establishments located in an enterprise zone border neighborhood, enterprise zones may impact a business's location decision. While Billings found no significant impact on location decisions of new establishments overall, he found significant positive impacts for manufacturing and retail establishments. Conversely, he found negative results for mining and

construction, which he speculates is from tax credits being capitalized in land rents, which negates the benefit of the tax credits. Additionally, there may be a lack of acceptable locations on both sides of the enterprise zone border since mining and construction have specific site requirements.

Enterprise Zones and Job Creation

An important goal of Maryland's enterprise zones, like most enterprise zones, is to create and retain jobs. However, academics have criticized an enterprise zone's ability to create jobs and many studies of Enterprise Zone programs have not found employment effects of enterprise zones. Some researchers assert that Enterprise Zone programs are a zero-sum game where instead of generating new investments, it merely moves investments to different locations. New investment and job creation within enterprise zones come at the expense of other urban areas. This spatial equilibrium theory suggests mobile workers and firms will arbitrage the benefits associated with Enterprise Zone programs by relocating into the enterprise zones. This will in turn increase land prices and offset any welfare gains to the original enterprise zone residents. Other critics claim the program has a negative net impact on the national economy because it induces businesses to make inefficient location decisions, while others argue the program is ineffective because the incentives are too small to sway investment decisions.

GAO used interrupted time series analyses of employment levels of enterprise zone participants in Hagerstown, Cumberland, and Salisbury, along with data from select employers, and determined that while there was employment growth in the enterprise zones between 1980 and 1987, it could not be linked to the Enterprise Zone program. When GAO interviewed participants who experienced employment growth, the majority of them said it was due to increased demand, not the enterprise zone incentives.

Boarnet and Bogart concluded that New Jersey's Enterprise Zone program had no significant impact on employment by using econometric analysis. Bondonio and Engberg and Greenbaum and Engberg did not find that employment growth in enterprise zones was significantly greater than in comparable nonenterprise zone areas. Using establishment-level data and geographic mapping methods, Neumark and Kolko find that enterprise zones do not increase employment in California.

Bondonio and Greenbaum investigate state-specific policy features across 10 states and the District of Columbia by looking at employment; sales (shipments); capital expenditures; and payroll per employee growth outcomes for new, existing, and vanishing establishments using establishment-level data. They found positive enterprise zone-induced increases in employment, sales, and capital expenditures in new and existing establishments, but they were offset by enterprise zone-induced losses among firms that close or leave the enterprise zone areas. Bondonio and Greenbaum speculate that new economic activity is more visible than retention of existing economic activity so political pressure puts more emphasis on attracting new jobs at the

expense of existing establishments, which must compete in the same markets without any subsidies. Their findings support the theory that enterprise zones are a zero-sum game.

Additionally, Peters and Fisher found no evidence that enterprise zones created economic growth by examining births, moves-in, deaths, and expansions of businesses. They suggest tax incentives are not enough to overcome the economic barriers in the area, such as high crime, poor infrastructure, and lack of skilled workers.

There are several reasons why enterprise zones would not create jobs. For states that offer an incentive for hiring disadvantaged workers, like California, one might expect to see higher-skilled labor being substituted for low-skilled labor. However, since Neumark and Kolko found no evidence of a shift toward low-wage industries in California, they dismiss this theory.

An economic theory suggests geographically targeted economic development policies, like the Enterprise Zone program, are ineffective because the benefits of the enterprise zone are capitalized into higher property values. The capitalization theory rationalizes that property values increase within jurisdictions that have expectations of lower property taxes. However, if land values rise, employers will substitute toward labor, especially since the employment credits make labor cheaper. Lack of a significant effect on employment from Enterprise Zone programs may suggest enterprise zone benefits targeting property could lead to businesses substituting away from labor and toward property inputs. Lynch and Zax's believe that this is happening in Colorado's urban enterprise zones because the investment tax credit for machinery and equipment accounts for approximately 70% of total subsidies claimed by enterprise zone participants in Colorado. Lynch and Zax found that urban enterprise zones had no positive effects on employment while rural enterprise zones had a small positive employment effect. They believe there is a positive effect on employment in rural enterprise zones because capital is a less suitable substitution for labor in agricultural processing. Neumark and Kolko do not believe this substitution away from labor is what is happening in California since California's hiring credits are generous and are the largest of the enterprise zone tax incentives in California. Peters and Fisher found the maximum price reduction of labor never exceeded 3% when they examined 16 sectors in 13 states, so it is likely that most states have a capital bias that will lead firms to more capital-intensive methods of production over labor. In Maryland, property tax credits are much larger than employment tax credits, so it is likely that Maryland behaves similarly to Colorado by favoring capital over labor in urban enterprise zones.

Enterprise zones may have positive spillover effects, in which areas just outside of the enterprise zone boundaries experience employment growth due to increased retail traffic, increased income of local residents, and improvements in infrastructure. Thus, it is not surprising that studies that compare enterprise zones to neighboring areas might find no effect of enterprise zones on employment. However, Neumark and Kolko did not find any positive spillover effects of employment growth just outside of enterprise zone boundaries.

Enterprise zone incentives may not be large enough to affect behavior. Peters and Fisher found the effects of labor incentives on the price of labor to be small. The maximum price

reduction never exceeded 3% when Peters and Fisher examined 16 sectors in 13 states, so one would not expect a firm to hire more workers because labor became 3% cheaper. However, Peters and Fisher caution against increasing the incentives. Assuming the elasticity of economic activity with respect to taxes is less than one, enterprise zones will generate fiscal losses, so the larger the incentives, the larger the fiscal losses will become. Bondonio and Engberg agree with Peters and Fisher's warnings since they found that the success of Enterprise Zone programs is not dependent on the monetary amount of the enterprise zone incentives. If that is the case, the enterprise zone's costs are not justified.

Although most studies have found that enterprise zones do not create jobs, some studies have found that enterprise zones do positively affect employment, or at least in the short term. O'Keefe found the enterprise zone designation in California raises employment growth in enterprise zones approximately 3% each year for the first six years after designation, but then the effect disappears in later years. O'Keefe suggests the employment growth disappears in later years due to businesses seizing the most attractive vacant properties in the early years, so that in later years there are fewer opportunities for businesses, and the time horizon left for receiving enterprise zone benefits shrinks as years pass, making it less profitable for a business to begin or expand in later years. Additionally, O'Keefe found that enterprise zone status does not significantly affect earnings or number of firms in the first six years, but it has a significant negative effect on number of firms after seven years.

Billings examined Enterprise Zones credits in Colorado by using establishment-level data and a border effects methodology. He found the credit increased the number of employees hired by between 1.5 and 1.8 more employees for new establishments and 0.0 to 0.3 more employees for existing establishments located within an enterprise zone. Given that existing establishments in Colorado must increase employment by at least 10% or investment by at least \$1 million, it is not surprising that existing establishments have a smaller impact on employment than new establishments.

Papke found that Indiana enterprise zones reduced unemployment claims by about 19% in cities that had enterprise zones. Indiana's Enterprise Zone program, which includes an incentive for stock of inventory, differs greatly from other states, so Papke's conflicting results could merely reflect differences in programs.

Using a two-way fixed effects model and census data, Moore finds some firms (finance, insurance, and real estate, along with wholesale and retail) have produced some positive employment effects for enterprise zones. Couch *et al.*, find a positive effect from qualifying as an enterprise zone in Mississippi on a county's rate of job creation using ordinary least squares and data from the Mississippi Statistical Abstract.

Bartik examined how taxes affect business activity and concluded that if a small suburban jurisdiction within a metropolitan area raised its taxes 10%, there would be a 10% to 30% reduction in its business activity in the long run. However, if an entire state or metropolitan area raised taxes by 10%, it would only see between a 1% and 6% reduction of business activity.

Bartik's findings suggest that if taxes decreased through the Enterprise Zone program, business activity would increase.

Busso, Gregory, and Kline found that the federal Urban Empowerment Zone program increased employment in zone neighborhoods by 12% to 21% compared to equivalent neighborhoods in rejected and future empowerment zones. Busso, Gregory, and Kline disagree by finding that the federal urban empowerment zone program increased employment in zone neighborhoods and raised wages for local workers, but it did not significantly increase population or the local cost of living. They used rejected and future applicants to the empowerment zone program as controls.

Negative spillover effects may cause Enterprise Zone programs to look successful. Enterprise zones may steal jobs and businesses away from neighboring areas causing a negative spillover effect. However, Neumark and Kolko did not find any negative spillover effects of employment growth just outside of enterprise zone boundaries in California. Maryland tries to prevent negative spillover effects from happening by stipulating the credits are only for new hires or those that move businesses from outside of the State to a Maryland enterprise zone.

Impact of Enterprise Zones on Enterprise Zone Residents and Economically Disadvantaged Workers

Many enterprise programs have goals of improving the employment opportunities for people living in the enterprise zones since people, especially those with less skills, do not readily move to find work (Bartik, 1991). However, the vast majority of workers in enterprise zones do not live in an enterprise zone and those who lived in enterprise zones do not work in the enterprise zones. Thus, it is not surprising that many academic studies have found enterprise zone residents are not directly benefiting from Enterprise Zone programs.

Elvery expected that if any Enterprise Zone program would have a positive impact on resident employment, it would be in California and Florida because they provided large incentives for hiring enterprise zone residents and people with a history of unemployment. By examining California and Florida Enterprise Zone programs, Elvery finds that the programs had no significant effects on the employment of enterprise zone residents. Additionally, Elvery did not find support for the belief that enterprise zones create negative spillovers for residents of nearby areas. Reasons for enterprise zones to be ineffective in improving employment for enterprise zone residents or disadvantaged workers include: (1) enterprise zone residents do not possess the skills required by businesses that are attracted by the Enterprise Zone program; (2) the Enterprise Zone program causes businesses to substitute labor for capital; (3) capital-intensive establishments do not value labor incentives; and (4) enterprise zones incentives are poorly targeted or insufficiently large to induce businesses to increase enterprise zone resident employment.

The enterprise zone studies that Wilder and Rubin reviewed averaged about 20% to 30% of new jobs going to enterprise zone residents while nonzone residents received many of the new jobs created by enterprise zones. They noted many state Enterprise Zone programs provide such modest tax credits for employing enterprise zone residents or disadvantaged persons that businesses view them as “not worth the trouble.” DBED officials believe businesses in the State share this viewpoint because it takes a lot of effort to claim the Enterprise Zone employment tax credits in Maryland.

Using establishment-level data and geographic mapping methods, Neumark and Kolko find that enterprise zones do not increase employment or shift employment toward targeted low-wage workers in the enterprise zone in California.

Bondonio and Greenbaum stated enterprise zones reduce the payroll per employee because jobs created by new establishments in enterprise zones are likely low-paying and low-skill jobs. So even if an enterprise zone resident or disadvantaged worker is hired, he or she will be paid low wages. This is consistent with Lynch and Zax’s findings that enterprise zones have no effect on payroll per worker.

Lynch finds that urban zones increase the unemployment rate of zone residents while reducing per capita income in urban and rural zones. This finding suggests enterprise zone incentives led businesses to the substitution of capital for labor. Additionally, the study finds the enterprise zones have no significant effect on poverty rates.

While most studies have found that enterprise zone residents do not benefit from enterprise zones, a few studies have contradicted these results. Papke found that Indiana enterprise zones increased employment for enterprise zone residents by about 1.5 percentage points. However, by utilizing unemployment claims, Papke does not include those who are unemployed but are not claiming unemployment benefits, so the impact may be overstated.

Busso, Gregory, and Kline found that the largest employment increases in the federal Urban Empowerment Zone were from zone residents. Additionally, they found that the federal urban empowerment zone program raised weekly wages for zone residents working inside the zone by approximately 8% to 13% compared to workers in equivalent neighborhoods in rejected and future zones, but when examining overall wage effects for zone workers as a whole, there was no significant wage effect. The Empowerment Zone tax credit program creates an incentive to hire zone residents over commuters with all else being equal, so zone firms are likely to pay different wages to residents and commuters. For enterprise zones that do not link employment tax credits to an employee’s residence, there is no cost differential for employers to hire enterprise zone residents or nonresidents so higher wages for enterprise zone residents is unlikely. Maryland does not link employment tax credits to an employee’s residence.

Ham *et al.*, measure the impact of State enterprise zones, federal empowerment zones, and federal enterprise community programs through a double difference estimation approach using census tract data. The authors found that all three programs have a positive impact on

local labor markets, but that federal empowerment zones and federal enterprise community programs have a much greater effect than state enterprise zones.

Types of Firms Utilizing Incentives

Previous studies on Enterprise Zone programs have found that larger firms utilize enterprise zone incentives more than small businesses. Wilder and Rubin found larger firms with over 50 employees favored incentives more, since they tend to have more capital assets and want to take advantage of inventory-related and capital investment credits. O’Keefe suggests enterprise zones attract larger firms than nonenterprise zones since she found overall employment grew more quickly in enterprise zones. Busso, Gregory, and Kline found that employment increased for establishments that were already large when studying the federal urban empowerment zone, which is consistent with prior findings that large firms are more likely to use tax credits.

GAO found that large urban businesses and rural businesses were more likely than small urban businesses to use federal empowerment zone tax incentives. Nonrefundable tax credits are only useful for businesses that generate profits. Generally small businesses have limited tax liability during the first few years of operation. Another reason why businesses do not claim the federal empowerment zone credits is that businesses are not aware of the credit. Small family-run businesses are less likely to be aware of the empowerment zone program than large establishments (Busso, Gregory, and Kline). Additionally, larger firms have the economies of scale advantage when it comes to the process of claiming the credit. Neumark and Kolko state, “smaller businesses find it less worthwhile than larger businesses do to claim enterprise zone benefits because of the administrative burden.”

By reviewing enterprise zone studies, Wilder and Rubin concluded new employment created through enterprise zones was heavily concentrated in manufacturing and wholesale/retail trade, and most new jobs are within firms with fewer than 50 employees. However, Neumark and Kolko found that the enterprise zone incentives favor the creation of jobs outside the manufacturing sector instead of within it in California. Economic developers use additional incentives to lure manufacturing firms so enterprise zone incentives are small comparatively to other economic development tools. Additionally, manufacturing firms that Neumark and Kolko studied may have shifted from labor to capital as a result of the manufacturing firms valuing enterprise zone benefits focused on property and machinery more than those focused on labor.

Existing firms and/or new business start-ups generated most new jobs, while relocating firms and new branch expansions of outside firms made up only a small proportion of new jobs. Wilder and Rubin summarized that existing firms were more likely to utilize enterprise zone incentives than new firms by expanding facilities through tax breaks.

Impact on Property Values

Critics of Enterprise Zone programs suggest geographically targeted economic development policies are ineffective because the benefits of the enterprise zone are capitalized into higher property values. The capitalization theory rationalizes that property values increase within jurisdictions that have expectations of lower property taxes. Offering enterprise zone incentives increases demand for enterprise zone property, which is immobile. Since the supply of enterprise zone sites is fixed, researchers expect enterprise zones to raise property values in the enterprise zone. However, when Boarnet and Bogart studied the Urban Enterprise Zone program in New Jersey, they found that the enterprise zones did not increase property values.

Using a hedonic price model and parcel-level property sales data from Cleveland, Ohio, Landers concludes that having an enterprise zone status may have a positive impact on enterprise zone property values in some instances, but the potential price effects diminish as enterprise zones are designated in other nearby locations. Additionally, Landers notes in depressed areas, there is an overabundance of idle resources. Thus, the supply of commercial and industrial property is elastic while the demand for business sites is inelastic. As a result, Landers found some evidence that suggests enterprise zone premiums are not present in economically distressed areas, but may be present in nondistressed areas. Longo and Alberini found that the Maryland Enterprise Zone program increased property values of contaminated industrial sites in Baltimore by 25%, but there was a negative significant effect on property values of commercial properties.

It is unlikely that capitalization is occurring in Maryland's Enterprise Zone program. Since enterprise zones expire within 10 years (unless they are renewed), the expectations of lower property taxes becomes unstable, thus diminishing the likelihood of enterprise zones raising property values.

Enterprise Zone Program Costs

Enterprise Zone program costs have not been scrutinized as closely as other economic development programs. Few studies have calculated cost/benefit ratios or cost-per-job figures of Enterprise Zone programs, and those that have done so have not measured indirect impacts or costs. Indirect benefits include increased personal taxes paid by in-migrants or those who were previously unemployed and increased taxes paid by other businesses that may see increased economic activity as a result of a new firm opening. Indirect costs may consist of increased state and local public service costs that would follow from a new firm opening. Also, researchers are unable to obtain data on state revenues foregone due to the confidential nature of tax returns, and often states do not provide detailed annual reports of the program costs. Studies that have calculated the cost-per-job have ranged greatly.

Enterprise Zone programs generally cost states and local governments more money than they receive in revenue from increased economic activity because it is extremely difficult for

governments to target tax reductions at firms who would have otherwise not made an investment without the enterprise zone incentives.

Peters and Fisher found that governments lost more revenue the more they front-loaded their incentives. When incentives are front-loaded, localities need a larger response of investments to tax reductions in order to break even because businesses tend not to live forever. Establishments could have ceased operations or moved before the incentives are phased out so they never pay additional taxes. Peter and Fisher found that enterprise zones experience a large amount of establishment turnover. Peters and Fisher also found that constant, permanent tax cuts produce more positive revenues than a larger initial tax cut that is phased out over several years. However, GAO claims that new businesses are in need of help the most during their earlier years.

Enterprise zone studies vary widely on the cost-benefit analysis of enterprise zones. Wilder and Rubin note the aggregate costs of states and localities for enterprise zone incentives range from less than \$400,000 to over \$50 million. The Enterprise Zone program cost Colorado on average \$30 million annually of forgone tax revenue between 1986 and 1996, with the amount increasing to over \$60 million annually between 2000 and 2005. Papke found the cost-per-job of enterprise zones in Indiana was \$4,100 in forgone tax revenue by using data from official firm-level tax records, while Rubin and Wilder found the annual cost-per-job to be \$1,045 in one specific enterprise zone in Indiana.

Peters and Fisher find the cost-per-job of Enterprise Zone tax credits to be approximately \$5,000 for the 20 most industrialized states during the 1990s. They believe the value-to-firm/cost-to-government ratio is less than one, which means enterprise zone incentives cost states and cities more than they benefit firms. By examining 20 states, Peters and Fisher found enterprise zone incentives reduced state and local taxes on new investments by approximately 19%.

Research Recommendations

As a result of studies on the enterprise zone, researchers have made suggestions to make enterprise zones more successful. The number of enterprise zones should be targeted and restricted. Enterprise Zone programs should develop specific employment goals. By reviewing enterprise zone studies, Wilder and Rubin found that the most successful state programs (1) restricted the number of enterprise zones, (2) used a competitive designation process, and (3) provided a wide array of development incentives.

Enterprise zones should be targeted to distressed areas. Bartik found economic development policy was more cost effective and efficient when it was targeted in economically depressed areas because the reservation wage (the lowest wage at which a person is willing to work) is lower in depressed areas compared to less depressed areas. Additionally, Landers suggest that enterprise zone premiums are not prevalent in economically distressed zones, but may be present in more prosperous areas. Peters and Fisher warns against designating zones in

nondistressed areas, saying “in growing places enterprise zones may do little more than reinforce growth trends.”

Enterprise Zone program officials should limit the geographic expansion of enterprise zones. Bondonio and Greenbaum state, “the baseline employment and sales growth among new establishments increases when the geographic extent of the zones decreases.” Bondonio and Greenbaum tout the advantages of limiting geographic expansion of enterprise zones by arguing the following: (1) it enables program officials to intensify marketing efforts for each enterprise zone; (2) officials are better able to evaluate the comparative advantage of different eligible areas; (3) it allows for close program monitoring and evaluation; and (4) it prevents the dilution of enterprise zone incentives. Landers agrees that creating more enterprise zones dilutes the effectiveness of incentive packages offered in distressed zones.

Bondonio and Greenbaum recommend that Enterprise Zone program officials should incorporate a strategic planning portion into the application process. Developing an Enterprise Zone strategic plan would facilitate communication on business needs between business leaders and administrative officials. Additionally, it would help business owners become more aware of the opportunities offered by enterprise zone incentives.

Bondonio and Greenbaum think incentives should be tied to job creation since they found that it is the only enterprise zone feature that marginally increases employment growth of existing enterprise zone firms. However, they found that tying incentives to new jobs does not impact employment for new firms.

Appendix 4
Enterprise Zone Community Demographics
Percent of Population

<u>Zone</u>	<u>Poverty</u>	<u>SNAP Recipient</u>	<u>Low Income</u>	<u>White</u>	<u>African American</u>	<u>Foreign Born</u>	<u>Other Language</u>
Hagerstown	19.9	20.8	46.3	77.9	19.1	6.0	
Wash. Co. Airport	8.6	6.4	21.9	87.2	9.6	5.3	
Hancock	11.7	6.0	47.6	87.6	10.4	1.3	
Cumberland	16.8	18.0	52.5	86.8	8.9	1.7	
Rt. 220 South	11.2	26.8	42.1	93.5	5.3	1.7	
Frostburg	24.5	16.3	52.4	86.2	9.0	2.3	
N. Garrett	16.4	10.8	37.2	97.8	0.1	0.2	
Keyser's Ridge	14.3	9.9	36.3	98.4	0.1	0.3	
C. Garrett	7.2	9.6	39.8	99.3	0.2	0.7	
S. Garrett	20.4	16.7	47.6	96.5	2.3	1.2	
Western Maryland	15.4	13.5	44.2	90.6	7.1	1.5	
Berlin	10.0	12.7	34.9	72.3	22.9	11.0	15.6
Cambridge	24.1	29.6	49.2	47.1	46.7	4.5	5.7
Crisfield	35.3	27.5	51.7	59.7	34.4	2.6	5.6
Fruitland	17.3	14.6	28.2	55.0	38.9	8.3	9.9
Hurlock	24.0	15.9	46.9	49.6	38.7	6.2	10.7
Pocomoke City	27.0	24.6	60.4	49.1	47.8	2.0	3.7
Princess Anne	33.0	16.4	52.6	34.3	54.7	8.4	11.0
Snow Hill	20.9	17.6	45.7	64.1	35.4	2.5	3.5
Cecil County	12.4	10.9	31.5	85.1	11.3	3.8	10.2
Eastern Shore	24.0	16.4	46.9	55.0	38.7	4.5	9.9
Aberdeen	11.1	8.8	26.9	68.1	22.8	5.7	9.3
Edgewood	13.1	11.4	26.9	59.7	33.9	6.5	11.1
North Point	11.3	11.8	32.9	74.4	18.7	7.3	9.3
Southwest	19	15	33.8	69.6	20.7	9.1	11.6
Woodlawn	10.4	8.1	27.8	14.9	70.4	16.6	18.2
Greater Baltimore	11.3	11.4	27.8	68.1	22.8	7.3	11.1
Baltimore City	22.4	17.1	44.8	31.6	65.3	7.2	8.9
Gaithersburg	8.3	7.3	17.7	53.3	15.6	38.1	46.0
Glenmont	10.7	5.9	15.6	39.0	26.1	42.0	58.1
Takoma Park	13.1	7.7	22.6	38.6	25.1	48.0	56.6
Wheaton	15.6	8.5	21.3	43.2	15.1	41.0	53.5
Capital Region	11.9	7.5	19.5	41.1	20.4	41.5	55.1
All Regions	15.6	12.7	37.2	68.1	20.7	5.7	10.7
Maryland	9.0	7.1	15.6	59.2	29.4	13.5	16.2

Note: Other Language is percent of households where a language other than English is spoken at home.
Source: U.S. Census Bureau – 2007-2011 American Community Survey; Department of Legislative Services

Appendix 5 Enterprise Zone Community Economic Conditions

<u>Zone</u>	<u>Population</u>	<u>Unemployment</u>	<u>Labor Participation</u>	<u>Median Household Income</u>	<u>MFG/Warehousing</u>
Hagerstown	36,140	10.5%	64.1%	\$38,231	15.4%
Wash. Co. Airport	8,512	5.3%	65.3%	58,347	14.6%
Hancock	1,490	10.3%	66.2%	37,222	18.6%
Cumberland	26,388	10.4%	53.4%	34,058	16.1%
Rt. 220 South	4,097	2.2%	66.0%	40,674	34.3%
Frostburg	10,400	8.1%	56.0%	32,890	7.2%
N. Garrett	2,566	5.5%	65.3%	32,890	18.3%
Keyser's Ridge	4,187	5.2%	63.7%	48,912	21.0%
C. Garrett	2,162	3.7%	61.4%	44,288	18.1%
S. Garrett	4,938	5.8%	57.7%	37,066	11.9%
Western Maryland	100,879	5.6%	63.9%	\$37,727	17.1%
Berlin	4,415	3.9%	71.6%	\$58,000	6.2%
Cambridge	12,226	15.5%	62.1%	35,599	19.7%
Crisfield	2,741	9.3%	58.2%	34,074	18.0%
Fruitland	4,781	3.9%	72.0%	52,871	16.0%
Hurlock	1,979	16.4%	71.6%	39,821	32.4%
Pocomoke City	4,217	14.9%	61.2%	30,909	11.8%
Princess Anne	3,199	6.2%	59.8%	32,159	7.2%
Snow Hill	2,530	5.9%	54.5%	40,515	12.9%
Cecil County	25,750	9.3%	65.9%	58,440	16.4%
Eastern Shore	61,838	9.3%	62.1%	\$39,821	16.0%
Aberdeen	37,195	8.2%	69.3%	\$63,311	12.2%
Edgewood	39,288	8.5%	72.3%	62,281	15.5%
North Point	151,174	10.0%	65.4%	50,665	16.0%
Southwest	23,496	14.2%	68.0%	52,888	14.6%
Woodlawn	15,094	7.4%	71.9%	55,345	12.6%
Greater Baltimore	266,247	8.5%	69.3%	\$55,345	14.6%
Baltimore City	620,210	12.6%	62.3%	\$40,100	10.9%
Gaithersburg	59,037	5.5%	76.5%	\$81,118	6.2%
Glenmont	12,657	7.0%	74.7%	82,338	6.4%
Takoma Park	19,239	8.4%	81.5%	68,426	4.1%
Wheaton	47,279	8.5%	74.1%	66,395	4.8%
Capital Region	138,212	7.7%	75.6%	\$74,772	5.5%
All Zones	1,187,386	8.2%	65.4%	\$44,288	14.6%
Maryland	5,736,545	7.3%	69.0%	\$72,419	9.7%

Note: MFG/Warehousing is percent of residents employed within the manufacturing and transportation and warehousing industries.

Source: U.S. Census Bureau – 2007-2011 American Community Survey; Department of Legislative Services