THE PEW CHARITABLE TRUSTS

2005 Market Street, Suite 2800
Philadelphia, PA 19103-7077
215.575.9050 Phone

901 E Street NW
Washington, DC 20004
202.552.2000 Phone

www.pewtrusts.org

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The Honorable Anthony Williams
Chairman, District of Columbia Tax Revision Commission
1101 Fourth St. SW
Suite W770
Washington, DC 20024

Dear Chairman Williams,

On behalf of The Pew Charitable Trusts, I would like to thank you for the opportunity to provide information on evaluating tax expenditures, including economic development tax incentives. Our organization has been conducting research and working with state leaders to advance policies that make economic development tax incentive programs effective, accountable, and fiscally sound. We are pleased to support the Tax Revision Commission as it undertakes critical work to modernize the District's tax code and ensure that policymakers have the evidence they need to determine whether tax incentives are working as intended.

In authorizing the Tax Revision Commission last year, the Council of the District of Columbia said, "Present tax policies and laws are in need of evaluation with respect to their equitability, productivity, efficiency and effect on economic growth." It also noted, "The last comprehensive study of District taxes occurred in 1998, and more recent tax changes have been somewhat piecemeal and sometimes made without regard to the system as a whole or knowledge of long-term effects."

The District, like many states, has accumulated a large number of tax expenditures over time; the most recent tax expenditure report included more than 200. These provisions have a substantial effect on its budget. Looking only at tax expenditures intended to spur economic growth, more than $34 million in revenue was forgone in fiscal 2012, according to the Year-End Unified Economic Development Budget Report. However, as Councilmember Mary Cheh stated to the commission Sept. 16, "As it currently stands, we never evaluate the results [of tax expenditures]. We never check to ensure that the policies that we put in place are achieving their intended goals."

Pew's research has shown that the District is far from alone in this area, particularly regarding economic development tax incentives. In 2012, we released "Evidence Counts," a study that assessed whether and how well the 50 states and the District of Columbia evaluate tax incentives and use the resulting evidence to inform policy choices. The study found that the District—along with half the states—was "trailing behind," having not taken key steps to ascertain whether incentive programs deliver a strong return for residents and the local economy.

More positively, our study also identified evaluation policies that have been successful in leading states and offer lessons that others can apply. The District has some elements of an effective evaluation system already in place. The tax expenditure report, for example, documents the purpose, forgone revenue, and beneficiaries for each of the District's tax expenditures. Additionally, under the Tax Abatement and Financial Analysis legislation, projects seeking assistance from the government must report on expected community benefits, undergo financial analyses, and be re-certified on an annual basis. The District also has a long-standing requirement that each piece of legislation include a fiscal impact statement estimating how the proposal will affect the budget.

To build on this foundation, we urge the commission to recommend a process similar to the one set out in the Tax Transparency and Effectiveness Act of 2013, introduced by Councilmember Cheh and co-sponsored by Chairman Phil Mendelson. Implementing such a process would provide policymakers and taxpayers with the information they need to ensure that the District's economic development strategy is effective, accountable, and affordable. Such a system also would position the District as a national leader in tax incentive evaluation.

Specifically, we recommend the following components.

1. **Set clear, measurable program goals.** Council involvement early in the tax incentive evaluation process is vital to ensuring that analysts use goals and metrics that reflect policymakers' current intent for each program. The legislation would establish a process for sharing and gathering feedback on the metrics that will be used in the evaluations.

2. **Undertake thorough evaluations.** We recommend rigorous evaluations that go beyond data on program cost and a collection of numbers reported by those receiving incentives. Economic development tax incentives are designed to change the behavior of businesses—to encourage them to hire, build, and invest more than they would have without these policies. Evaluations should consider whether incentives are in fact having such effects. The proposed act lays out several key considerations to be addressed when evaluating tax incentives for economic development. These include the extent to which an incentive affected choices made by businesses and whether the benefits were offset by harm done to other companies or negative effects from the budget trade-offs needed to pay for the program. Evaluations that examine these questions provide a more accurate and complete picture of an incentive's benefits, costs, and consequences.

3. **Schedule evaluations regularly.** Every tax incentive represents a choice about how to use scarce resources, so policymakers need information about the results of each one. Evaluating all tax incentives on a regular basis (the legislation would set up a five-year cycle) also allows incentive programs to be compared with each other to determine which ones are the most effective use of public dollars. Recurring evaluations are critical, because the District's economic priorities may shift over time, and changes in the economy can affect how well a tax incentive works.

4. **Inform lawmakers' choices.** The best evaluations go beyond rigorous analysis by drawing conclusions that lawmakers can consider and act upon. The proposed act would require recommendations for improvements to existing programs, as well as recommendations for whether to extend, terminate, or modify each program. In addition, the Council would be required to hold public hearings on the evaluations.

5. **Appropriate necessary resources.** Making the Office of the Chief Financial Officer responsible for evaluations would be logical, given the office's existing duties in producing the tax expenditure report and analyzing new incentives. The Cheh legislation takes this approach. Additionally, the commission should recommend sufficient resources to implement this process. Our research shows that a regular evaluation process can be implemented by approximately two full-time equivalents.

We appreciate your consideration of these recommendations as you complete the crucial tasks before the commission. Please feel free to contact me if you have any questions or would like additional information.

Sincerely,

Robert Zahradnik
Director, State Policy
The Pew Charitable Trusts