

Getting Our Money's Worth?

Promoting Transparency and Accountability for Corporate Tax Subsidies in Massachusetts

Getting Our Money's Worth?

Promoting Transparency and Accountability for
Corporate Tax Subsidies in Massachusetts

MASSPIRG Education Fund

Tom Van Heeke,
Frontier Group

Phineas Baxandall,
U.S. PIRG Education Fund

Deirdre Cummings,
MASSPIRG Education Fund

February 2013

Acknowledgments

The authors thank Kurt Wise and the research staff at the Massachusetts Budget and Policy Center for sharing their data. The authors also thank Randy Albelda, Professor of Economics at the University of Massachusetts Boston; Noah Berger at the Massachusetts Budget and Policy Center; and Leigh McIlvaine at Good Jobs First for their review of this document. Additional thanks to Tony Dutzik and Elizabeth Ridlington for their editorial assistance.

MASSPIRG Education Fund thanks the Ford Foundation for making this report possible.

The authors bear responsibility for any factual errors. The recommendations are those of MASSPIRG Education Fund. The views expressed in this report are those of the authors and do not necessarily reflect the views of our funders or those who provided review.

© 2013 MASSPIRG Education Fund. Some Rights Reserved. This work is licensed under a Creative Commons Attribution Non-Commercial No Derivatives 3.0 U.S. License. To view the terms of this license, visit <http://creativecommons.org/licenses/by-nc-nd/3.0/us>.

You are free to display, reproduce, and distribute this work in its entirety for non-commercial purposes, with proper attribution. To attribute this work, please credit MASSPIRG Education Fund and provide a link to www.masspirgedfund.org.

With public debate around important issues often dominated by special interests pursuing their own narrow agendas, MASSPIRG Education Fund offers an independent voice that works on behalf of the public interest. MASSPIRG Education Fund, a 501(c)(3) organization, works to protect consumers and promote good government. We investigate problems, craft solutions, educate the public, and offer Bay Staters meaningful opportunities for civic participation. For more information about MASSPIRG Education Fund or for additional copies of this report, please visit www.masspirgedfund.org.

Frontier Group conducts independent research and policy analysis to support a cleaner, healthier and more democratic society. Our mission is to inject accurate information and compelling ideas into public policy debates at the local, state and federal levels. For more information about Frontier Group, please visit www.frontiergroup.org.

Layout & Graphic Design: Harriet Eckstein Graphic Design

Table of Contents

Executive Summary	1
Introduction	5
Special Business Tax Subsidies: \$770 Million and Counting	7
The Cost of Special Business Tax Subsidies Is Surging	8
The Number of Special Business Tax Subsidies Is Growing	9
The Commonwealth’s Special Business Tax Subsidies Lack Full Transparency and Accountability	13
Regular Reviews of Effectiveness	13
Clear Policy Objectives	14
Money-back Guarantees	14
Cost Caps	15
Full Transparency	16
Policy Recommendation: Implement Strong Accountability and Transparency Standards for Tax Subsidies	22
Convert Discretionarily Awarded Transferable and Refundable Tax Subsidies into Grant Programs	23
Articulate Clear Public Policy Goals	24
Establish Expiration Dates	24
Impose Cost Caps	25
Implement Robust “Clawback” Provisions	25
Continue to Improve Public Disclosure	26
Appendix	28
Notes	29

Executive Summary

The people of Massachusetts deserve to know how their tax dollars are spent, including on tax subsidies for businesses. Full transparency allows citizens to hold lawmakers, government contractors, and recipients of public subsidies accountable. It also promotes fiscal responsibility, checks corruption, and bolsters public confidence in government. Currently, Massachusetts offers its citizens the opportunity to scrutinize state spending down to checkbook-level detail thanks to its online portal, *Open Checkbook* on the *Massachusetts Transparency* website. Yet, with the exception of transferable and refundable tax credits, the Commonwealth provides less transparency and accountability for spending conducted through the tax code in the form of “special business tax subsidies.”

This special spending through the tax code merits particular attention because it is not subject to the normal public scrutiny of line-item spending in the state budget. Unlike conventional budget items, the annual cost of such spending may not be known until after the money is spent. And because programs are often automatically

renewed each year, they can continue to impose costs on the Commonwealth without undergoing thorough consideration and annual approval by the Legislature and Governor. To protect the public, Massachusetts should adopt common-sense practices to increase the transparency and accountability of special business tax subsidies.

Massachusetts spends twice as much on special business tax subsidies as it did 16 years ago.

- In fiscal year 2012, Massachusetts spent \$770 million on special business tax subsidies, up from an inflation-adjusted \$342 million in fiscal year 1996, according to research by the Massachusetts Budget and Policy Center. This is more than the \$678 million the Commonwealth spent in fiscal year 2012 on school building construction, or the \$510 million the Commonwealth spent on all public health programs including initiatives to prevent smoking and teenage pregnancy.

- Spending on special business tax breaks as a share of the state economy has increased 60 percent since fiscal year 1996. Every other major area of government spending except health care and education decreased as a share of the state economy during the same period.
- The vast majority of special business tax subsidies—a total of \$626 million in fiscal year 2012—are special deductions or credits that businesses can use to reduce the corporate excise on profits or to collect tax rebates from the Commonwealth. Other subsidies allow companies to avoid sales taxes or permit certain businesses filing taxes through their owners to receive credits or deductions against personal income tax obligations. In fiscal year 2012 these subsidies cost the Commonwealth

\$129 million and \$15 million, respectively.

The Commonwealth does a far better job creating new tax subsidies than ending old ones.

- The number of special business tax subsidies has almost doubled since fiscal year 1996 with the addition of 13 new tax subsidies. At the same time, lawmakers have phased out just two subsidies that were active in fiscal year 1996.
- Two of Massachusetts’ most expensive special business tax subsidies—film production credits and the single sales factor formula, which allows certain companies to avoid taxes based on their property and payroll in Massachusetts—have been created since fiscal year 1996.

Figure ES-1. Cost of Special Business Tax Subsidies, Fiscal Year 1996-Fiscal Year 2012

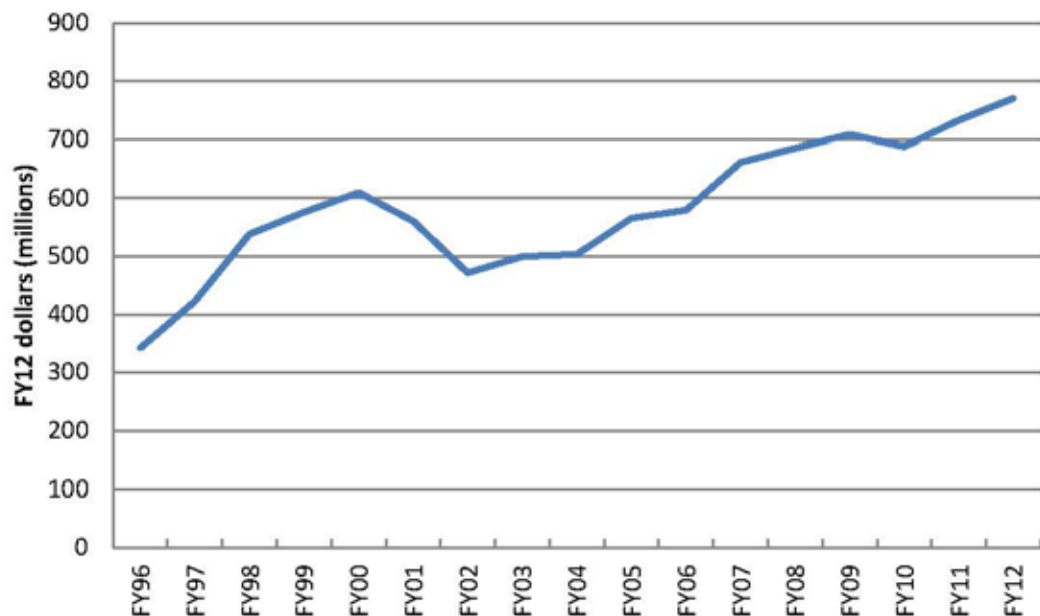
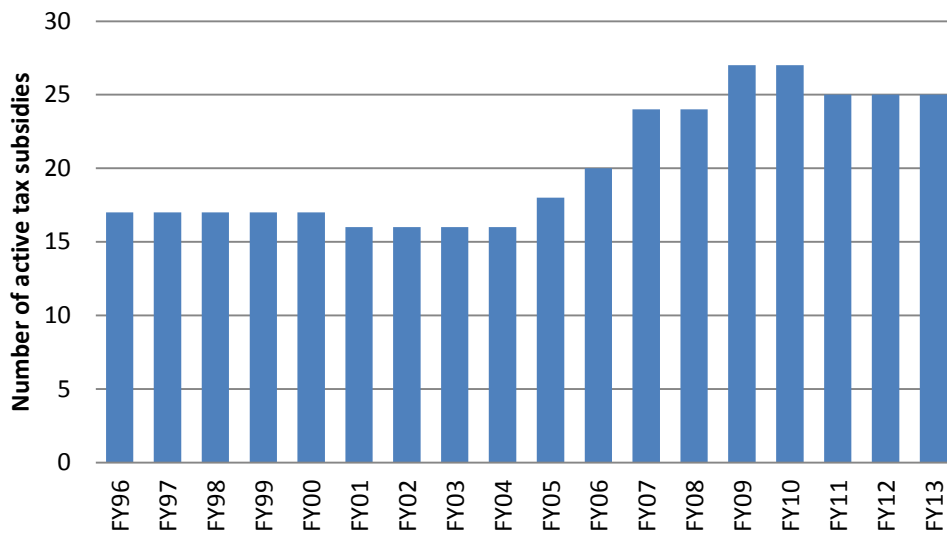


Figure ES-2. Number of Active Special Business Tax Subsidies, Fiscal Year 1996-Fiscal Year 2013



While Massachusetts’ lawmakers have taken steps to make spending through tax expenditures more transparent and accountable, the Commonwealth currently lacks important tools to ensure that citizens get the most bang for their buck.

- Few of the Commonwealth’s special business tax subsidies have well-articulated public policy objectives.
- A lack of clearly defined goals for subsidy programs limits the ability of the Commonwealth to impose money-back guarantees, known as “clawback” provisions. Only nine of the 25 active special business tax breaks currently have such provisions in place. Where clawback provisions do exist, they are not as clear or demanding as they should be.
- Fewer than one-third of the Commonwealth’s special business tax

subsidies (seven of 25) are subject to annual spending limits.

- Only eight of Massachusetts’ 25 special business tax subsidies require the Legislature to actively renew the program, meaning that the other 17 continue regardless of their merit.
- Important information is scattered across different reports and online databases.
- Nearly half of all special business tax subsidy programs fail to publicly disclose one or more of the following pieces of information: recipients, subsidized projects, project-by-project or program-wide cost to the state budget, or results generated by the program.
- With the exception of the film industry and life sciences industry tax credits, no publicly available evaluations of after-the-fact cost-effectiveness

exist for special business tax subsidies. Bay Staters lack tools to easily discern when the state has recaptured subsidies from companies that fail to deliver on promises. A dearth of information on costs and benefits means that Bay Staters cannot weigh in on the merits of particular subsidy programs before they are renewed.

To increase the transparency and accountability of special business tax subsidies, the Commonwealth should adopt the recommendations of the state’s bipartisan Tax Expenditure Commission as a starting point. Building on these, ultimately the system should:

- Transition away from discretionarily awarded tax subsidies to a system of direct grants, improving the transparency, accountability and efficiency of economic development subsidies.
- Articulate clear and measurable public policy goals for each subsidy program, and require that proposals for new breaks include a clear policy purpose. Businesses that receive a tax subsidy should report measurable, company-level targets that fit with the subsidy’s overarching policy objective.
- Mandate periodic review of all tax subsidies and require them to expire in the absence of active decisions to renew based on the review.
- Cap the cost of each subsidy program, protecting the Commonwealth and its citizens from runaway costs.
- Define strong and clear clawback provisions to recoup tax subsidies from companies that fail to meet their programmatic goals wherever practical.
- Continue to improve public disclosure of information—including information on each subsidy program’s purpose, progress toward the policy’s goal, total annual cost, expiration date, clawback statistics and names of beneficiaries—on the state’s transparency website. Users should have the ability to “drill down” to see details about the monetary value of each business’ tax subsidy, the intended benefit for the state (number and quality of jobs, volume of sales and so on), the recipients’ performance relative to targets, and any instance in which the state gets its money back due to a recipient’s failure to deliver on promises.

Introduction

In March 2011, financial services giant Fidelity Investments announced that it was closing its Marlboro, Massachusetts, facility and moving 1,100 jobs out of the Commonwealth. After a half-decade job-cutting spree, the firm's consolidation had claimed 5,000 jobs leading up to the announcement.¹

Especially surprising and disappointing is the fact that Fidelity enjoys the benefits of unequal weighting of sales, payroll and property in the apportionment formula, the Commonwealth's costliest special business tax subsidy. In particular, Fidelity benefits from the single sales factor formula, a type of unequal weighting rule passed into law in "An Act Relative to Job Retention and Economic Expansion in the Commonwealth."² The single sales factor rule allows eligible companies in the defense, mutual fund and manufacturing industries to avoid some in-state tax obligations in the interest of creating a favorable tax climate and bolstering Massachusetts' economy.

Fidelity's closure of the Marlboro campus ran counter to the spirit in which the Commonwealth offered the single sales factor apportionment rule, leaving Bay

Staters to wonder if their tax dollars are put to good use funding tax subsidies for corporations.

Fidelity is not the only high-profile firm in Massachusetts to take large subsidies from taxpayers before falling short of its promises, cutting jobs, or relocating. A 2010 report in *The Boston Globe* called attention to rampant waste in Massachusetts' Economic Development Incentive Program (EDIP)—one of the key programs through which state and local governments use tax policy to provide special business subsidies—finding hundreds of instances over a 16-year period in which the beneficiaries of subsidies failed to deliver what they promised, or took taxpayer dollars in return for only a handful of jobs.³

Nor is Massachusetts alone. The much-publicized collapse of former Red Sox star Curt Schilling's video game firm, 38 Studios—which was located in Massachusetts and offered some state support before moving to neighboring Rhode Island in exchange for \$75 million in guaranteed loans—drew attention to the common pitfalls that affect special business tax subsidies in all states, as well as the emerging

competition between states keen to create and sustain local jobs.⁴

With companies of all stripes promising new job creation in exchange for a subsidy—or threatening to leave and take their existing jobs with them if they do not receive one—state governments find themselves in what *The New York Times* recently called a “high-stakes bazaar,” a race to the bottom to offer the most lucrative deal to a corporation and beat out their neighbors.⁵ The challenge for states like Massachusetts lies in knowing when the public is getting “bang for their buck” from tax subsidies.

Fortunately, the Commonwealth is learning from its own experiences and those of other states. In late 2010, the Legislature passed, and Governor Deval Patrick signed, legislation creating stronger money-back guarantees and reporting requirements for EDIP credits. Another reform required more transparency for 12 other refundable and transferable tax credit programs.⁶ As part of that reform effort, in June 2012 the Department of Revenue produced its first *Tax Credit Transparency Report* for credits issued in 2011.⁷

The Commonwealth took a further step by creating a Tax Expenditure Commission as part of its fiscal year 2012 budget. The Commission conducted the first careful study of Massachusetts’ tax exemptions, deductions and credits. After

public meetings and deliberations, the Commission produced a report that made a number of strong policy recommendations to improve the transparency and accountability of all tax expenditures, including those we categorize in this report as special business tax subsidies.

Massachusetts stands poised to be a national leader in establishing the rules and mechanisms needed to identify and pursue cost-effective economic development strategies. The report of the Tax Expenditure Commission gives the Commonwealth momentum and a blueprint for progress. Massachusetts should seize this opportunity.

Spending on special business tax subsidies—like spending on anything else—involves trade-offs. More money spent through the tax code results in less money for schools, roads and other public programs, or alternately in higher tax rates to make up for budget shortfalls. To make informed decisions about when those trade-offs are acceptable, taxpayers need information about the scope and impact of these subsidies. This report describes common-sense policy reforms that would not only enable full accountability and transparency, but also turn Massachusetts into a national leader in its stewardship of public subsidies.

Special Business Tax Subsidies: \$770 Million and Counting

“In fiscal year 2012...the Commonwealth distributed \$770 million in special business tax subsidies, an all-time high and more than double what was distributed 16 years ago.”

Like all states, Massachusetts wants to foster a vibrant state economy providing jobs, services and opportunity for its citizens. Historically, the Commonwealth has fulfilled this function through public investments in areas such as schools and infrastructure. In recent years, however, Massachusetts and other states have intensified the provision of direct subsidies to businesses and industries with the stated intention of sparking economic growth.

These subsidies can take many forms, including taxpayer-backed loan guarantees and lines of credit provided by the Massachusetts Growth Capital Corporation.⁸ The Commonwealth also uses tax policy to subsidize businesses through *tax expenditures*.⁹ These expenditures impact Massachusetts’ bottom line just as any item of the appropriated state budget: every dollar

of tax subsidies must be offset through program cuts or higher taxes elsewhere.

Tax expenditures take the form of tax deductions, exemptions, credits and other special rules like double-weighted sales or single sales factor apportionment. Many of these tax subsidies behave much like cash. Refundable tax credits can be redeemed for rebate payments from the state. Transferable tax credits can also be sold by companies that do not have tax liability to other companies that want to purchase a lower tax bill. All of these provisions reduce annual revenues for the state.

Since fiscal year 1996, Massachusetts has used a total of 58 different tax expenditures for businesses and corporations. In fiscal year 2012, 52 of these expenditures were still in existence and cost the Commonwealth \$2.44 billion in forgone revenue.¹⁰ This amount is more than the entire sum that the Commonwealth collected in corporate and business taxes in the same year.¹¹

According to a recent report by the Massachusetts Budget and Policy Center,¹² the Commonwealth’s business tax expenditures fall into three categories:

- “Piggybacks”: Massachusetts implements 19 business tax expenditures by “piggybacking” on the federal tax code, allowing some federal tax expenditures to operate through the state tax code as well. Legislators could expressly “decouple” from Washington’s tax rules, but Bay State decision-makers have instead allowed 19 federal tax expenditures for businesses to operate as part of the state code, too. This report does not study these expenditures.
- Pyramiding and double taxation: Eight business tax expenditures are intended to avoid “pyramiding” or double taxation. Double taxation occurs when, for instance, a business’ property is taxed both at the local and state level. The most common example of tax pyramiding occurs when a company pays sales tax on components of a larger product which will ultimately be sold and subject to the sales tax itself. These expenditures fall outside the concern of this study.
- Special business tax breaks: According to the Massachusetts Budget and Policy Center, the remaining 31 expenditures are “best described as being part of the Commonwealth’s actual economic development *strategy*” (emphasis in original text).¹³ These 31 expenditures form the core of this report’s analysis and are termed “special business tax subsidies” throughout this study. These tax subsidies have been specifically designed and enacted by Massachusetts’ policy makers in an effort to spark economic growth.

These 31 special business tax subsidies come in three forms, as defined by the Massachusetts Budget and Policy Center:

- General: Available to any business engaged in qualifying business activities

(for example, the corporate research credit is available to any corporation incurring qualified research costs or making research payments in Massachusetts in a given tax year).

- Sector-specific: Automatically available to businesses in certain industries (such as the film production credit).
- Discretionary: Taxpayers must apply for these subsidies and receive approval from an administering agency (for instance, credits for life sciences companies seeking to develop their businesses in the state).¹⁴

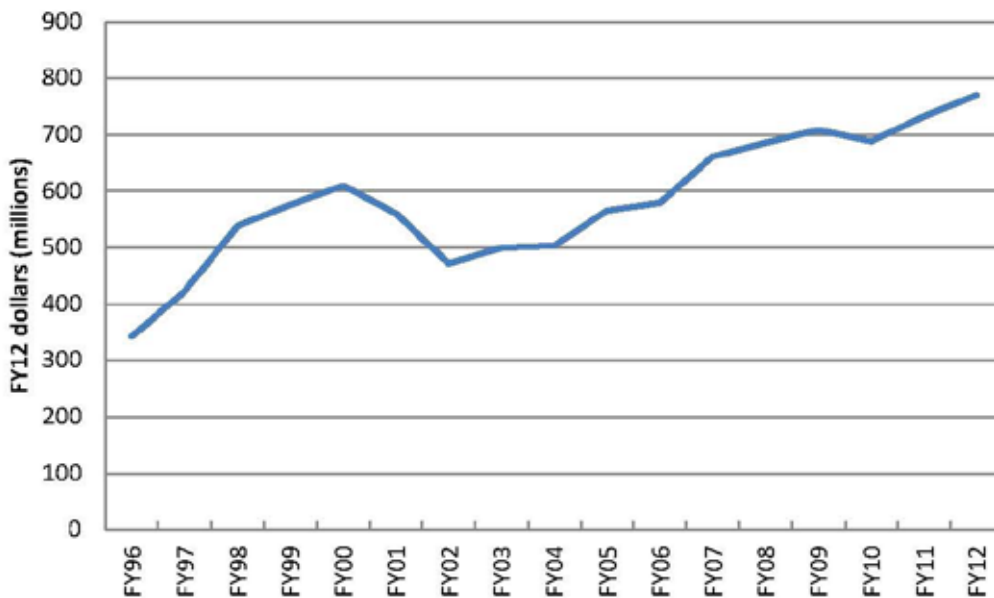
In fiscal year 2012 Massachusetts offered six general, 14 sector-specific, and five discretionary subsidies.

The Cost of Special Business Tax Subsidies Is Surging

Massachusetts is dedicating an increasing amount of its fiscal resources to special business tax subsidies. In fiscal year 2012, according to an analysis by the Massachusetts Budget and Policy Center, the Commonwealth distributed \$770 million in special business tax subsidies, an all-time high and more than double what was distributed 16 years ago. Adjusted for inflation, the cost of special business tax subsidies has increased from a total of \$342 million in fiscal year 1996 to \$770 million in fiscal year 2012.¹⁵

This is a huge sum. By comparison, this is more than the \$678 million the Commonwealth spent in fiscal year 2012 on school building construction, or the \$510 million the Commonwealth spent on all public health programs such as those aimed at preventing smoking and teenage pregnancy.¹⁶ It is eleven times what the state spent on environmental programs,¹⁷

Figure 1. Cost of Special Business Tax Subsidies, Fiscal Year 1996-Fiscal Year 2012



and represents more than nine times the amount the state spends directly through the budget on economic development, community development, workforce development, culture and arts combined.¹⁸

Business tax subsidies can occur in all three tax categories: corporate, sales and personal income. In addition to the credits and deductions applicable to the corporate excise on profits, other tax subsidies reduce sales tax obligations for companies. And some businesses, particularly smaller ones, pay business-related taxes through the owner’s personal income taxes. They make use of special subsidies to reduce personal income taxes for owners. The largest category of business tax subsidies accounts for special deductions or credits that businesses can use to reduce the corporate excise on profits, or to collect tax rebates from the Commonwealth. These subsidies totaled \$626 million in fiscal year 2012. In the same fiscal year, some businesses in Massachusetts also received \$15 million in personal income tax subsidies, and avoided \$129 million in sales taxes.

Spending on special business tax

subsidies is also squeezing out other forms of public investment because it is growing faster than other forms of state spending. In fact, the Massachusetts Budget and Policy Center highlights that spending on special business tax breaks as a share of the state economy has grown 60 percent since fiscal year 1996. At the same time, in every other major area of government expenditure except education and healthcare, government outlays as a share of the state economy have declined.¹⁹ As Massachusetts spends more and more on special business tax subsidies, it becomes increasingly pressing that Bay Staters have the information and tools they need to evaluate them.

The Number of Special Business Tax Subsidies Is Growing

It is not just the cost of special business tax subsidies that is on the rise. Though the number of subsidies has held steady

for the past three fiscal years, today there are almost 50 percent more active special business tax subsidy programs in Massachusetts than there were in fiscal year 1996 (25 versus 17). Just two tax subsidies that were active in fiscal year 1996 have been phased out, while 13 new ones were created. (One tax subsidy both came onto the books and expired over the same time period.) (See Table 1 for details.)²⁰

Of the 13 tax subsidies active in fiscal year 2012 that were created since fiscal year 1996, two are exemptions from sales tax and 11 are credits against income and corporate excise taxes. Some of the better known additions are tax credits for film production and those awarded through the Life Sciences Tax Incentive Program signed into law by Governor Deval Patrick in 2008. These subsidies aim to encourage film production in the state and the creation of long-term jobs in the life sciences industry, respectively. These new tax breaks are responsible for much of the cost increase detailed above. For example, while the Life Sciences Tax Incentive Program did not exist in fiscal year 1996,

it cost Massachusetts \$20 million in fiscal year 2012.

The unequal weighting of sales, payroll and property in the apportionment formula has added more to special business tax subsidy costs than anything else. Traditionally, when a corporation produces or sells goods and services around the country, a given state will tax the corporation's nationwide profit in relation to the share of total corporate property, payroll and sales located in that state. But with unequal weighting of sales, payroll and property, some corporations can greatly diminish or even eliminate their in-state tax liability. Unequal weighting can occur in two ways: through double-weighting of sales or use of the single sales factor (SSF) formula. The latter—allowed only for particular defense contractors, mutual fund corporations, and eligible manufacturers—lets beneficiaries calculate their tax liability based solely on in-state sales, with no influence from property and payroll. So a business with its only factory and all of its employees located in Boston, but all of its sales outside of Massachusetts, would owe no corporate

Figure 2: Number of Special Business Tax Subsidies, Fiscal Year 1996-Fiscal Year 2013

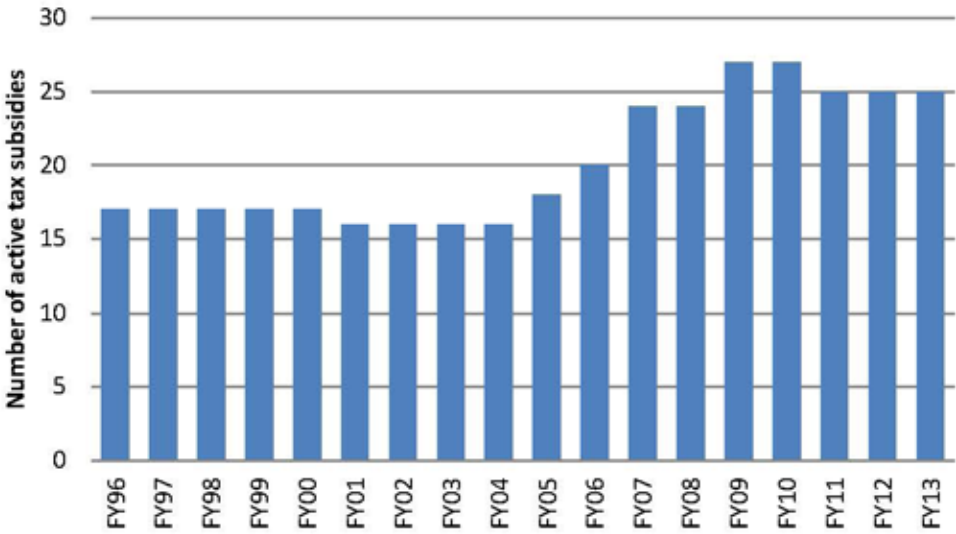


Table 1. Special Business Tax Subsidies since Fiscal Year 1996²¹

Subsidy	Tax Category	Cost in FY12 (millions)
Active since FY96 or earlier		
Abandoned Building Renovation Deduction	Income	\$4.0
Economic Development Incentive Program Credit	Income	\$2.9
Abandoned Building Renovation Deduction	Corporate	Negligible
Unequal Weighting of Sales, Payroll and Property in Apportionment Formula (Double-Weighting of Sales and Single Sales Factor)	Corporate	\$247.6
Investment Credit	Corporate	\$57.9
Research Credit	Corporate	\$113.5
Economic Development Incentive Program Credit	Corporate	\$21.7
Credit for Harbor Maintenance Taxes Paid	Corporate	\$1.0
Exemption for Materials, Tools, Fuels and Machinery Used in Furnishing Power to an Industrial Manufacturing Plant	Sales	\$0.0
Exemption for Materials, Tools, Fuels and Machinery Used in Newspaper Printing	Sales	\$60.4
Exemption for Fuels, Supplies and Repairs for Vessels Engaged in Interstate or Foreign Commerce	Sales	\$0.7
Exemption for Fuel Used in Operating Aircraft and Railroads	Sales	\$56.0
New since FY96		
Brownfields Credit	Income	\$3.2
Historic Buildings Rehabilitation Credit	Income	\$2.5
Film Credit, Payroll and Production	Income	\$1.5
Medical Device Credit	Income	\$0.4
Dairy Farmer Credit	Income	\$0.7
Brownfields Credit	Corporate	\$24.6
Historic Buildings Rehabilitation Credit	Corporate	\$47.5
Film Credit, Payroll and Non-Wage Production	Corporate	\$82.6
Medical Device-User Fee Credit	Corporate	\$3.6
Life Sciences Tax Incentive Program	Corporate	\$20.0
Dairy Farmer Credit	Corporate	\$6.3
Exemption for Sales to Motion Picture Production Companies	Sales	\$0.5
Exemption for Aircraft and Aircraft Parts	Sales	\$11.2
Expired since FY96		
Credit for Employing Former Full-Employment Program Participants	Income	Expired
Additional Deduction for Certain Businesses in a Poverty Area	Corporate	Expired
Created and expired since FY96		
Jobs Incentive Payment for Biotechnology and Medical Device Companies	Corporate	Expired
Included in a single subsidy since FY01²²		
Exemption for Plant and Seed	Sales	N/A
Exemption of Feed	Sales	N/A
Exemption for Commercial Fishing Vessels	Sales	N/A

taxes whatsoever to the Commonwealth. Double-weighting in-state sales allows other companies to make in-state sales twice as important as the other factors in calculating tax, so a hypothetical business with all of its property and employees in Boston but all of its sales outside of the Commonwealth could use this rule to diminish its tax obligation. Though double-weighting of sales existed in Massachusetts prior to fiscal year 1996, the SSF formula

came into force for eligible defense contractors in fiscal year 1996, mutual funds in fiscal year 1997, and phased in for qualified manufacturing concerns between fiscal year 1996 and fiscal year 2000. In fiscal year 2012 alone, the unequal weighting of sales, payroll, and property cost the Commonwealth \$247.6 million making it the single costliest special business tax subsidy (the SSF formula in particular cost \$160 million).²³

The Commonwealth's Special Business Tax Subsidies Lack Full Transparency and Accountability

Lawmakers have added new tax subsidies without necessarily reviewing and analyzing the success or failure of older ones. This speaks to the underlying challenge of spending through the tax code. Once a subsidy is passed into law, it will not necessarily face formal reviews in the future, despite its lack of a clear policy objective or annual spending allocation, unlike budget line-items which legislators must approve, oppose or modify on an annual basis. Thus, for Bay Staters to be sure the programs funded through the tax code are worthwhile investments, it is critical that they have the ability to evaluate the programs' achievements and cost-effectiveness. This information is critical in determining which tax breaks to keep, eliminate, create or modify.

Despite taking steps in the right direction, the Commonwealth does not yet meet the best practices of accountability and transparency for \$770 million in state spending through the tax code. To make special business tax subsidies fully accountable, programs should include the following characteristics.²⁴

Regular Reviews of Effectiveness

Legislation authorizing each subsidy should periodically expire to bring the credits, deductions and exemptions under regular public scrutiny.

Unlike items in the state budget, which are subject to annual review and appropriation by the Legislature, tax subsidies do not necessarily face further scrutiny. State Auditor Suzanne Bump has expressed concern that after a tax break passes the Legislature, it falls into a "black box and seldom, if ever, does anyone look back and determine whether it is working as intended or whether there is continued public benefit."²⁵

Of the Commonwealth's 25 special business tax subsidies that were active in fiscal year 2012, only eight (32 percent) include an expiration date. As a result, \$587.7 million in annual special business tax subsidies are currently on the books indefinitely, and will potentially cost Bay State taxpayers even more in the future without facing further scrutiny from decision-makers or the public.²⁶

Clear Policy Objectives

Tax subsidies, like other government spending, should be clearly justified on measurable public policy grounds. With a clear purpose articulated in law, citizens and their representatives in government can make informed assessments about their value relative to other uses of the Commonwealth's financial resources.

Many special business tax subsidies are like discretionary grants. A well-run grant program establishes clear objectives for the program and, to meet those objectives, expects recipients to make progress toward measurable goals in exchange for receiving an award. Grant-like, discretionarily awarded subsidies should be no different. Such subsidy awards should come with project-specific economic development goals attached. These goals should include measurements like targets for job creation, wages and profitability.

Massachusetts does a poor job of establishing clear policy objectives for its special business tax subsidies. In fact, until the Tax Expenditure Commission in 2012, no uniform effort had been made to identify and publish the various subsidies' policy objectives in a single place. According to Department of Revenue research reported to the Tax Expenditure Commission in one of its public meetings, "few [tax subsidy] statutes actually include specifically identified goals" beyond vague descriptions of intent in the title.²⁷ For example the single sales factor apportionment formula—a type of unequal weighting of sales, payroll and property in the apportionment formula—was enacted in "An Act Relative to Job Retention and Economic Expansion in the Commonwealth."²⁸ Despite describing what the tax subsidy relates to, and initially incorporating job retention and job creation requirements in its first few years as law, the statute today offers no specific job retention or creation targets.²⁹ The legislation authorizing film production credits is

equally unclear. Though defenders of the law have touted its alleged economic benefits,³⁰ the 2005 statute provides no measurable economic goals, leaving its value a controversial matter of opinion.³¹

Even where a policy goal can be interpreted through some element of the statute, statements of goals are not available in any of the most accessible public resources describing the Commonwealth's tax subsidies. The annual Tax Expenditure Budget—the most accessible, centralized resource available—does not include a description of any of the expenditures' policy aims, despite detailing the nature and fiscal impact of every tax expenditure item on the books. Not even the annual *Tax Credit Transparency Report*, the document intended to shine a brighter light on at least some of these subsidies, which was released for the first time in June 2012, includes such information.

Money-back Guarantees

Another mechanism to improve the overall effectiveness of tax subsidies is to make recipients agree to a subsidy program's clear objectives and commit to returning the money if the recipient fails to meet those objectives. These tax credit recapture provisions are money-back guarantees for taxpayers and are often referred to as "clawbacks."

Massachusetts cannot always implement this common-sense safeguard for lack of clearly defined and measurable policy goals. In all, just nine of the Commonwealth's 25 active special business tax subsidies contain clawback provisions.³² One of the costliest tax subsidies missing a clawback provision is the corporate income tax credit for film production companies. The program cost the Commonwealth \$82.6 million in fiscal year 2012, all of which was unprotected by

a money-back guarantee. The underlying cause is the absence of well-defined objectives for the program as a whole and for individual subsidy beneficiaries. Though legislators have touted the film tax credit as an economic boon for the Commonwealth and a driver of tourism,³³ no specific job creation or tourism targets have been established, making it impossible to hold the overall tax credit initiative or individual beneficiaries to account. But without clear economic development goals attached to each subsidy program, and thus yardsticks against which to measure performance, more clawbacks are presently impractical to implement.³⁴

Even where clawback provisions are in place, they can be inadequate and unclear. In 2011, Evergreen Solar’s manufacturing plant in Devens, Massachusetts, closed, despite having received approximately \$58 million in state aid, some of which was tied to job creation goals. In the wake of the closure, state legislators and Evergreen Solar executives publicly disagreed on what the company owed the Commonwealth, exposing a lack of clarity in the rules for the program.³⁵ And while the Economic Development Incentive Program contains detailed rules on when and how a tax credit

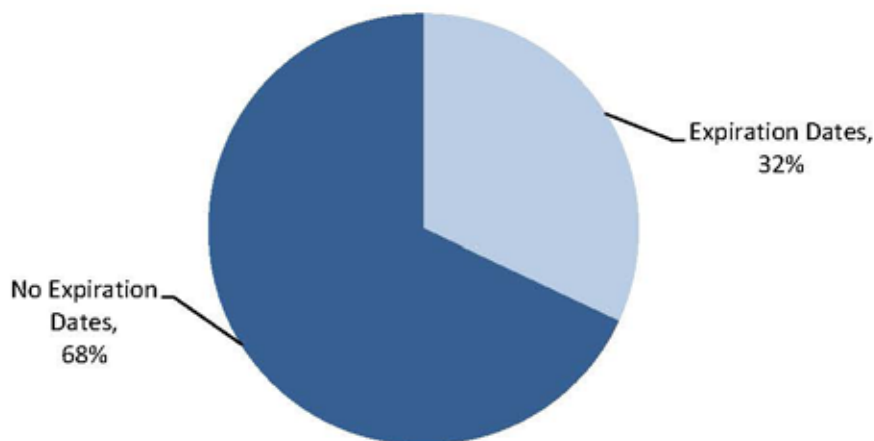
may be clawed back, the provision itself is not sufficiently demanding: the clawback process is only triggered when a company fails to meet at least 50 percent of its job creation target. Put another way, this allows companies to keep their subsidy even when they fall up to 50 percent short of meeting their goal.³⁶

Cost Caps

Tax subsidy spending generally does not come with a set price tag. For instance, when the Legislature agrees to fund tax credits for film production companies equal to a certain percentage of their in-state expenses, it essentially signs off on spending an unspecified sum of money to be determined after the fact. This makes it difficult to plan within the larger state budget, and it makes it impossible to weigh these costs against other budget alternatives. It is like setting up a special credit card to be spent on a particular purpose, but with no limits.

In Massachusetts, just seven of the 25 special business tax subsidies active in fiscal

Figure 3. Most Special Business Tax Subsidies Lack Expiration Dates



year 2012 (28 percent) were subject to a cost cap, with limits ranging from \$4 million to \$50 million per subsidy program, per year. In all, that means just \$104 million of the \$770 million spent on special business tax subsidies in fiscal year 2012 was known to legislators ahead of time.³⁷ So while the Commonwealth knows with certainty that these seven subsidies will cost no more than \$104 million in fiscal year 2013, no such certainty exists around the remaining 18 special business tax subsidies.³⁸ Under current law, the state is committed to absorb those costs regardless of the final bill.

disclosure of information and provide access to that information that is:

- Online,
- Comprehensive,
- Timely,
- Evaluative,
- One-stop, and
- Searchable

Online

Information is not practically accessible in the public domain unless it is on the Internet.

To its credit, Massachusetts recognizes this and has made a number of moves to increase the online availability of its government data, including those related to special business tax subsidies.

- Since 2008 the Governor of Massachusetts has released the details of the tax expenditure budget for the

Full Transparency

To make special business tax breaks fully transparent, states should require public

Tax Subsidies Require Regular Review

Without expiration dates ensuring regular review, tax subsidies can turn into costly corporate giveaways of questionable value to the broader public. In March 2011, Marlboro, Massachusetts, lost 1,100 jobs when financial services giant Fidelity Investments closed its office in town as part of a five-year-long consolidation effort. All told, Fidelity cut 5,000 jobs statewide in the run-up to the Marlboro closure.³⁹ But Fidelity benefits from the unequal weighting of sales, property and payroll in the apportionment formula, a special business tax subsidy intended to benefit the economy by creating a favorable tax climate for businesses. In particular, Fidelity benefits from the single sales factor (SSF) formula, an apportionment rule available only to eligible defense contractors, mutual funds and manufacturing concerns. The legislation promulgating the SSF formula for defense and manufacturing companies and, separately a year later, for mutual funds, originally contained job retention and creation requirements: mutual funds were required to increase their employment by 25 percent in the first five years the law was in effect. But these requirements ended more than a decade ago, enabling mutual funds alone to receive more than \$1.5 billion in SSF formula subsidies since then without necessarily keeping jobs in the state.⁴⁰ Without the Legislature checking in, the SSF's job creation requirement phased out while the subsidy itself remained. Ensuring that the Legislature reviews each subsidy on a regular basis would give Massachusetts the chance to renew the subsidies that work and end those that no longer serve a meaningful public purpose.

upcoming fiscal year online. This web-based resource is clickable and allows users to “drill down” to a brief description of every expenditure, its statutory origin and its estimated cost.⁴¹ This resource covers the same ground as the annual tax expenditure report, but does so in a more user-friendly manner.

- Massachusetts posts its annual tax expenditure budget online as a printable document. Budgets dating back to 2000 are available, allowing both citizens and decision-makers to follow tax expenditures through recent history.⁴²
- The recently inaugurated *Tax Credit Transparency Report* is available through the Department of Revenue website,⁴³ as is the annual *Report on the Massachusetts Film Industry Tax Incentives*.⁴⁴ To the benefit of the public and decision-makers interested in patterns

and trends over time, the Massachusetts Department of Revenue archives reports from years past on its website.

- The data included in the *Tax Credit Transparency Report* are also available in a clickable online database via a link on the *Open Checkbook* website. This database shows the recipient and value of each individual subsidy awarded through 13 of the Commonwealth’s tax subsidy programs.

There is much room, however, to improve the accessibility of these resources. Massachusetts presently posts its formal annual reports in different subsections of the “Tax Professionals” link on the Department of Revenue website (making it unlikely that interested citizens who are not tax professionals will find them). The Commonwealth should also make information on all special business tax

Figure 4. The Tax Credit Database on Massachusetts’ *Open Checkbook* Website

The screenshot shows the 'View Tax Credits' page on the Massachusetts Open Checkbook website. The page includes a navigation menu with 'Home', 'View Payroll', 'View Pensions', and 'View Tax Credits'. Below the navigation is a 'View Tax Credits' section with a 'Show Search Criteria' button. The main content is a table titled 'Tax Credit Details' with the following columns: Tax Credit Program, Administering Department, Project Name, Tax Credit Year, Tax Credit Awarded, and Tax Credit Issued. The table lists 13 rows of data for various tax credit programs.

Tax Credit Program	Administering Department	Project Name	Tax Credit Year	Tax Credit Awarded	Tax Credit Issued
Brownfields Tax Credit	Department of Revenue				\$47,584,000
184 West Second Street, LLC	Department of Revenue		2011		\$630,700
277 Broadway LLC	Department of Revenue		2011		\$74,636
303 Third Street Developer LLC	Department of Revenue		2011		\$1,261,018
APCA Reproduct LLC	Department of Revenue		2011		\$84,091
Alta Management, Inc.	Department of Revenue		2011		\$13,287
American Stonehenge Realty Trust	Department of Revenue		2011		\$108,852
Andrew F. Smith	Department of Revenue		2011		\$18,158
BIS, INC.	Department of Revenue		2011		\$63,980
Beacon Tenderers, LLC	Department of Revenue		2011		\$57,539
Big Bend Development, LLC	Department of Revenue		2011		\$64,564
Brain and Outfit, Inc.	Department of Revenue		2011		\$55,419
C. Coderly, Inc.	Department of Revenue		2011		\$50,262
Central One Federal Credit Union	Department of Revenue		2011		\$40,574
Chendon Street Associates, LLC	Department of Revenue		2011		\$6,427,184

subsidies available through a link on *Open Checkbook*. This website is Massachusetts' central source for information on government spending and, as such, should be expanded to incorporate detailed information on all spending through the tax code as well as through the traditional budget. This would include program-by-program and subsidy-by-subsidy spending breakdowns, as well as evaluative reports on the net economic impact of all of the Commonwealth's subsidy programs (modeled on Massachusetts' annual report on film industry tax incentives).

Comprehensive

The public deserves information that is both broad and detailed. Each and every tax credit, deduction and exemption should be disclosed with checkbook-level specifics answering the common-sense questions taxpayers ask: Who receives tax subsidies? What do they cost? What are they for? Which beneficiaries are meeting their goals and which are not? Which businesses that fail to meet their goals have paid back part or all of their subsidies? In addition, where the tax break takes the form of a

discretionary, grant-like credit, the terms of the business' agreement or contract with the state should also be public.⁴⁶

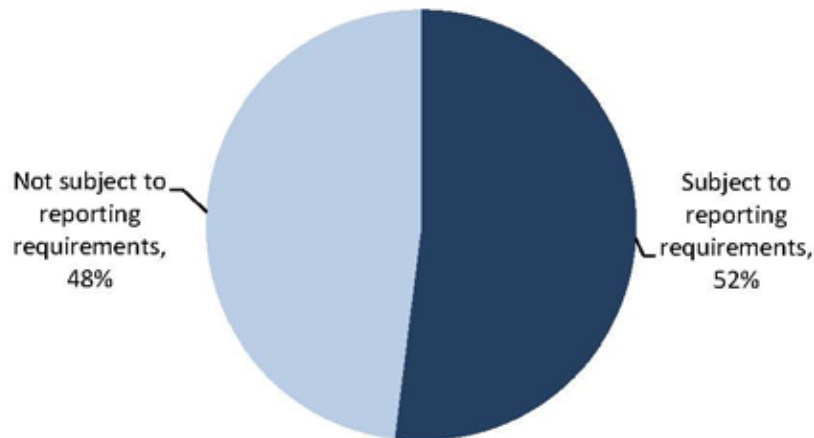
Massachusetts has a record of publicly documenting its tax expenditure budgets. By law, the Department of Revenue has produced an annual Tax Expenditure Budget (TEB) since fiscal year 1986.⁴⁷ In doing so, Massachusetts stands with 43 other states in publicly reporting tax expenditures annually.⁴⁸ The quality of the Massachusetts report has improved over time and today it documents and describes each tax expenditure item and its origin in statute, and provides item-by-item estimates for annual costs. However, it fails to inform the public and decision-makers in clear language of the public policy goal of each expenditure or provide specifics about the individual subsidies awarded.

The Bay State has made laudable advances in reporting more comprehensive information for a handful of subsidies. In 2010, Massachusetts passed new legislation requiring the Department of Revenue to report annually on certain refundable or transferable tax credits, identifying their beneficiaries, the amount of each credit,

Massachusetts Opens the State Budget to Public Scrutiny

As part of online transparency requirements included in the fiscal year 2011 budget, the Commonwealth's government transparency website, *Massachusetts Transparency*, expanded to include *Open Checkbook*, an easy-to-use resource providing detailed state spending information updated nightly. With "hover-over" features explaining terminology and context, as well as complex search functions, *Open Checkbook's* introduction boosted Massachusetts to fifth place out of 50 states in MASSPIRG Education Fund's 2012 *Following the Money* report which tracks the availability and quality of online government transparency tools.⁴⁵ Massachusetts now also includes detailed information on the recipients and value of more than \$86 million worth of tax breaks in 13 tax expenditure programs. The public would be further served by including similar information about the remaining special business tax breaks in addition to details about specific requirements for each subsidy and whether businesses met those requirements.

Figure 5. Share of Special Business Tax Subsidies Subject to Reporting Requirements



and the project for which the credit was received.⁴⁹ In the latest installment of the *Tax Credit Transparency Report*, for instance, Bay Staters learn that the production company behind the feature film “Ted” received more than \$9 million in subsidies in calendar year 2011.⁵⁰

Despite these gains, a lot of information remains absent from the public domain. Public subsidy-by-subsidy information like that available in the *Tax Credit Transparency Report* does not exist where it should for some of Massachusetts’ special business tax subsidies. In the aggregate, only 13 of the Commonwealth’s 25 active special business tax breaks—a little more than half—are subject to a closer look in a publicly released report or web-based transparency portal like *Open Checkbook*. Subsidies like the investment and research credits for non-life sciences businesses or the Abandoned Building Renovation Deduction should be subject this level of public disclosure. And while other subsidies, namely those operating through sales tax exemptions or unequal weighting of sales, property and payroll in the apportionment formula, would be more challenging to examine in the same detail, a big-picture look at their impact on the economy would be valuable. The SSF formula’s enacting legislation

originally called for an annual report, but the Commonwealth’s Department of Revenue has not published such a report since 2001.⁵¹

Some information is consistently unavailable to the public. When recipients of subsidies fall short of their goals or pay back state money, Massachusetts does a poor job publishing the relevant statistics and facts. According to Good Jobs First, of the five major special business tax subsidies it identified in Massachusetts,⁵² only the Life Sciences Tax Incentive Program publishes any information at all regarding unmet goals, publicly identifying companies that have fallen short of their job creation targets. But, like every other subsidy Good Jobs First analyzed, the Life Sciences Tax Incentive Program does not report the dollar amount of any recapture.⁵³ In addition, we found no statutory requirement that the government or an administering agency publish statistics on the incidence of unmet goals or clawbacks, or the identities of companies forced to pay back their subsidy, for any of the special business tax subsidies considered in this report.

The lack of such publicly available information undermines transparency. If the Economic Development Incentive Program, for instance, recaptures

taxpayer dollars from a high percentage of the businesses receiving subsidies, the public deserves to know because it may call into question the value of the entire program. Alternatively, if only a handful of businesses are succeeding it would benefit the Commonwealth and its taxpayers to know what the characteristics of those businesses are so the state can support more like them in the future. This is information that the people and decision-makers of Massachusetts need to make informed decisions about the future of special business tax subsidies.

Timely

Information should be updated frequently so the public and decision-makers can follow the money as it is spent.

Massachusetts currently does a good job of regularly releasing information to the public through legally mandated annual reports and budgets.

Evaluative

Projections of expected benefits and after-the-fact assessments provide citizens with the tools they need to weigh in on a proposed subsidy and understand the broader outcomes of spending on special business tax subsidies.

Massachusetts provides this kind of transparency only in its report on film industry tax subsidies, which thoroughly investigates their overall economic impact. The most recent report documents that in calendar year 2010, film production subsidies generated \$0.8 million in revenue for state government that partially offset the cost of the program; \$40.3 million in new spending, of which \$25.5 million went to residents and business in-state; and 19 net new full-time equivalent employees.⁵⁴ From an assessment of the number and value of tax credits applied for, to the net impact those credits have had on the state economy and job creation, this report publicizes the key information decision-

makers and citizens need. Aside from the annual report on the Life Sciences Tax Incentive Program produced by the Massachusetts Life Sciences Center,⁵⁵ the Commonwealth has yet to roll out similar assessments for other special business tax subsidies.

One-stop

Publishing details in a uniform way through a single online resource ensures that pertinent information can be easily and reliably found by taxpayers and decision-makers.

Currently, Massachusetts provides information in too many places and in too many forms. Between three different annual reports and an online tax expenditure budget display, Bay Staters must cobble together information on special business tax subsidies from a variety of sources, each incomplete and with differing areas of focus, in order to gather a single, comprehensive picture of the Commonwealth's special business tax subsidies.

Searchable

Leading states not only disclose information online but do so through user-friendly portals allowing the public to conduct intuitive, one-click searches for information by keyword or category.

The *Report on the Massachusetts Film Industry Tax Incentives* falls short on this score. This document is released online as a PDF file for download by the public and decision-makers. It lacks an interactive online component through which users can easily search for the details they find important.

The good news is that Massachusetts has already demonstrated a commitment to providing this kind of transparency to its citizens in other areas. Through *Open Checkbook* and, to a lesser extent, its online tax expenditure budget interface, the Bay State has shown how information can be provided in a user-friendly, web-based

format that is more useful than a take-it-or-leave-it document that cannot be broken down to focus on the things an individual cares about most. Unfortunately, *Open*

Checkbook only looks at items in the appropriated state budget and at a handful of tax credits, and the clickable tax expenditure budget lacks a search function.

The Need for Full Disclosure and Robust Cost-Benefit Assessments for Tax Subsidies

In 2010, Liberty Mutual received \$46.5 million in state and local tax subsidies to support construction of a new \$300 million headquarters in Boston's Back Bay neighborhood.⁵⁶ In addition to Tax Increment Financing (TIF) through the City of Boston, the Commonwealth provided a tax credit through the Economic Development Incentive Program for the expansion project. The only Fortune 100 company headquartered in the city, Liberty Mutual promised 600 new jobs over the course of 20 years, as well as 500 construction positions to build the new 30-story office tower.⁵⁷

The agreement raised public concerns for a number of reasons. The new jobs promised amount to an average of just 30 per year, or a 1.2 percent annual increase in the firm's present Boston-based workforce, calling into question the value of the tax credits offered. In addition, with Liberty Mutual's annual consolidated revenue estimated at almost \$29 billion in 2008,⁵⁸ and recent news coverage highlighting CEO Ted Kelly's \$50 million annual compensation,⁵⁹ Liberty Mutual's need for taxpayer support is dubious. Further, Liberty Mutual received tax credits through a program designed to stoke economic revival in down-and-out neighborhoods.⁶⁰ According to the Boston Redevelopment Authority, the TIF that spurred the Commonwealth's matching state-level credit is available only for projects located within an Economic Opportunity Area (EOA).⁶¹ By law, an EOA is a "blighted," "decadent" or "substandard" area, descriptions ill-suited for the prosperous Back Bay.⁶²

Taxpayers deserve value for money in special business tax subsidies. With better public disclosure before shovels go into the ground, Bay Staters could weigh in on a proposed subsidy early in the process. This would allow citizens and their representatives to ask tough questions before any money is disbursed, and weed out subsidy ideas that provide limited bang for their buck. This is especially important when taxpayers are asked to invest limited tax revenue in profitable, privately owned businesses.

Policy Recommendation: Implement Strong Accountability and Transparency Standards for Tax Subsidies

With special business tax breaks growing in cost and number, and inadequate accountability and transparency standards leaving Bay Staters unable to evaluate too many of them, spending on tax subsidies in Massachusetts needs reform. Fortunately, there has never been a better time for Massachusetts to take the lead in transparency and accountability standards for tax subsidies. In the past two years alone:

- The Massachusetts Legislature and Governor Deval Patrick, as part of the fiscal year 2012 budget, approved the establishment of a bipartisan Tax Expenditure Commission “to study carefully for the first time the various exemptions, deductions, and credits in the Massachusetts tax code.”⁶³ After several public meetings and careful analysis of the available data, the Commission concluded its study of the Commonwealth’s entire tax expenditure budget, calling for, among other things, clearer policy goals, better public disclosure, and stronger accountability measures.⁶⁴
- Studies by the Pew Center on the States highlighted the need for reform in Massachusetts. In a nationwide survey of how states track and evaluate their tax subsidies, Massachusetts was ranked in the middle of the pack with “mixed results.”⁶⁵
- The Massachusetts Budget and Policy Center underscored the revenue lost to special business tax subsidies when it released a report that found that their cost is rising both in absolute terms and as a share of the state economy.⁶⁶
- Media outlets have focused public attention on a series of high-profile tax subsidies, including those received by insurance giant Liberty Mutual and Curt Schilling’s now-bankrupt video game company in Rhode Island, leading Bay Staters to ask if adequate safeguards exist to ensure special business tax subsidies operate in the public interest.⁶⁷
- Years of budget cuts to traditional spending items have generated

renewed interest from the public and lawmakers in reviewing all state spending.

A blueprint for reform has emerged in the Tax Expenditure Commission's report. The Commission rightly confirms that tax expenditures such as special business tax subsidies "are a form of government spending and should be subject to the same scrutiny by government policymakers as direct expenditures."⁶⁸ The Commission made a number of strong and sensible policy recommendations, including calling for tax expenditures to include clear public policy objectives; undergo periodic, data-based, cost-benefit analysis; face regular review; and be subject to well-articulated accountability standards.

Those recommendations are a solid foundation for reform, but are not sufficient. To improve transparency and accountability for special business tax subsidies, Massachusetts should also:

- Convert discretionarily awarded transferable and refundable tax subsidies into grant programs,
- Articulate clear public policy goals,
- Establish "expiration" dates,
- Impose cost caps,
- Implement robust "clawback" provisions, and
- Continue to improve public disclosure.

Convert Discretionarily Awarded Transferable and Refundable Tax Subsidies into Grant Programs

Massachusetts should convert its discretionarily awarded, transferable and refundable special business tax subsidies

into grants appropriated through the state budget. Many of the Commonwealth's special business tax subsidies resemble direct grants. For example, life sciences tax credits and the subsidies awarded through the Economic Development Incentive Program are disbursed discretionarily by an administering agency, and impact the Bay State's bottom line like any item of the state budget.

Direct state spending offers many advantages over spending through tax expenditures. First, direct expenditures come with budgets that require annual approval. This means that, unlike some of the subsidies studied in this report, the cost of direct expenditures cannot grow without the express consent of decision-makers and taxpayers. Additionally, inherent in the budget approval process is the occasion for formal review of the spending item. With the annual appropriation of state funds comes a chance for decision-makers and the public to weigh in on how well a subsidy is meeting its goals and whether it merits continued funding.

Turning special business tax breaks into grants would also make government spending on subsidies for economic development more efficient. Film production tax credits, for example, are transferable and often sold to brokers and then resold, at a profit, to other firms looking to slash their tax bills. Between 2006 and 2010, film production companies kept only 87 percent of the tax credits issued by the Commonwealth. Brokers and final buyers took the rest, skimming 13 percent off the top of the program. As a result, of the \$264.8 million Massachusetts spent on film production credits between 2006 and 2010, \$34.4 million did not end up benefiting film production companies, diluting the impact of the program as an incentive.⁶⁹ Awarding these same tax credits as grants through the state budget would eliminate this problem. By cutting out the middleman, Bay Staters would be

sure that each tax subsidy dollar was supporting its intended objectives.

Articulate Clear Public Policy Goals

As the Tax Expenditure Commission recommends, the Legislature and governor should identify and publish clear policy objectives for each special business tax break already on the books. Similarly, when new subsidies are proposed, legislation must include a clearly defined policy purpose and a credible finding that the tax subsidy can and will achieve the desired outcome. Additionally, when individual corporations or businesses receive a discretionarily awarded special business tax break, the Commonwealth should expect them to have company-level targets that fit with the overall policy goal, focusing on employment levels or in-state sales and revenue. For example, if a business receives tax credits through the EDIP, decision-makers and the public should expect the company to demonstrate a credible plan for achieving its job creation targets. Above all, these goals and objectives must be measurable. When a subsidy program or company promises quality job creation, it should explain what a “quality job” is and how many of them it plans to add to the economy. Ultimately, setting goals is effective only if you can measure progress toward those goals.

Two leaders in this area are Oregon and Minnesota. Oregon’s tax expenditure reports include program and function categories describing the general purpose of each expenditure item (for example, “economic and community development”). They also include evaluations by personnel from 28 state agencies assessing the degree to which expenditures related to their program responsibility or over which they

have knowledge “achieve their purpose and if they are a fiscally effective means of doing so.”⁷⁰ Minnesota publishes detailed accounts of its job creation targets on a company-by-company basis, documenting how many jobs the tax break recipient aimed to create or retain, their wage level, and the cost of associated health insurance benefits.⁷¹ In this way, Minnesota establishes clear goals, tracks progress, and can even evaluate the *quality*, as well as number, of jobs added or kept.

Establish Expiration Dates

Legislation authorizing all special business tax breaks should include regular expiration dates, forcing periodic review of the tax break. Under this provision the Legislature will have to regularly and actively renew every special business tax break, encouraging public debate over the tax break’s merits.

Massachusetts can join two states leading the way on setting tax expenditure expiration dates. In 2009, Oregon passed legislation establishing expiration dates for many, but not all, of their corporate tax subsidies.⁷² And, in 2008, Nevada instituted a state constitutional requirement that all tax expenditures expire at a date to be determined by the Legislature upon passage of the law.⁷³ In spring 2012, the then-Secretary of Administration and Finance for Massachusetts, Jay Gonzalez, indicated his support for so-called “sunset” dates for the special business tax subsidies that are awarded on a discretionary and grant-like basis, and called for enhanced reviews for other business tax expenditures targeting specific industries every five years.⁷⁴ The Tax Expenditure Commission adopted these recommendations in its report and formally called for a mix of sunset dates and enhanced periodic reviews to improve

oversight of the Commonwealth's tax expenditures.⁷⁵

The Commonwealth should ensure that each and every special business tax break on the books returns to the Legislature formal renewal at clearly specified, regular intervals of five or ten years. This would provide an opportunity for a full debate and discussion of the merits of each subsidy program.

Impose Cost Caps

Tax subsidies should not be authorized with a blank check from the Legislature leaving taxpayers liable for a potentially limitless sum of money. Therefore, in an effort to mimic the appropriations process, special business tax subsidies should, where possible, fall under spending limits. Cost caps for tax subsidies can be designed in a number of ways, from credit-wide caps imposed on an annual basis or over the life of the program, to company-level limits on what individual beneficiaries can receive through a particular subsidy.

Some states have adopted cost caps as a means to control aggregate spending on subsidies, especially in tough economic times. For example, the state of Iowa currently imposes an overall spending limit on certain business tax expenditures. Though the initial cap stood at \$185 million, in 2010 legislators voted to reduce that cap to \$120 million in response to a worsening fiscal environment.⁷⁶

Massachusetts, too, already makes use of cost caps in certain instances and should go further. In addition to the credit-wide, annual caps already present for some subsidies, the Tax Expenditure Commission was right to call for an overall dollar cap on foregone revenue for the Commonwealth's grant-like tax credits.⁷⁷ The Legislature should follow through on this and, where

practicable, impose limits on foregone revenue incurred by other subsidies.

Implement Robust "Clawback" Provisions

When corporations and businesses enjoy certain tax subsidies but fail to hold up their end of the bargain, Bay Staters should have the ability to promptly recoup foregone tax revenue through uniformly enforced clawbacks. Clawbacks will not be practical or appropriate for every special business tax subsidy (see note 34), but where beneficiaries make specific promises to deliver jobs or increase in-state sales or spending and receive a subsidy in exchange, Bay State taxpayers deserve a money-back guarantee in case a business falls short of its promises.

Recapture provisions have proven effective in other states. In 2009, for instance, Oklahoma recaptured \$1 million in tax breaks awarded to a company that used its award as leverage to extract an even sweeter deal in Wisconsin before promptly pulling up stakes.⁷⁸ And in the summer of 2012, the Iowa Economic Development Authority sought the repayment of a forgivable loan after a business fell 66 percent short of its job creation target in the state.⁷⁹

Massachusetts already has examples of clawback mechanisms but needs to make the rules that govern them clearer. To avoid repeating the confusion that ensued when Evergreen Solar closed its plant in 2011, the Commonwealth should unambiguously specify what conditions will automatically trigger subsidy recapture, how much the beneficiary will owe and under what circumstances, and ensure that both companies and legislators are clear on these provisions.⁸⁰ The public and decision-makers count on clawbacks to safeguard their tax dollars and deserve

to know exactly how those provisions will work. Companies engaged in long-term financial planning would also benefit from the greater certainty, knowing for sure when they cannot count on keeping the funds. In fact, the Life Science Tax Incentive Program has such well-defined guidelines that its clawback provision encourages self-policing: 16 life sciences companies have failed to deliver the jobs they promised and voluntarily returned \$12.2 million, avoiding the DOR's knock at the door.⁸¹

Clawbacks should be demanding, too. This could mean establishing high minimum performance thresholds for companies in order to keep subsidies, or permitting lower thresholds while prorating clawbacks relative to performance. For instance, a clawback provision could be triggered when a company fails to achieve 90 percent or more of its job creation target. Alternatively, a clawback provision could permit a lower triggering threshold while imposing clawbacks on a sliding scale relative to the percentage of the job creation target the company achieved.

Continue to Improve Public Disclosure

Accountability and transparency go hand in hand. To ensure Bay Staters and their representatives in state government have the information they need and deserve to make informed decisions about the merits of special business tax subsidies, Massachusetts should continue to improve its standards of public disclosure for tax expenditures. In recent years, the Commonwealth has made important gains in overall government transparency: since receiving an "F" in 2010 in MASSPIRG Education Fund's *Following the Money* report,⁸² an annual study and assessment

of state government transparency websites, the Bay State is now near the top of the class. In the 2012 installment of the scorecard, MASSPIRG Education Fund awarded Massachusetts an "A-" in recognition of the *Massachusetts Transparency* website and the online budget resource, *Open Checkbook*.⁸³ Nonetheless, though the Commonwealth has taken steps to shine a brighter light on some special business tax subsidies, including 13 refundable and transferable tax credits in *Open Checkbook*, there is more to do.

First and foremost, the Commonwealth should continue to improve the reach of its online transparency tools, ensuring that all tax subsidies are as open to public scrutiny as the state budget and refundable and transferable tax credits through *Open Checkbook*. Public policy objectives, company-by-company goals (where applicable), expiration dates, and the nature and incidence of clawbacks should be published online for each tax subsidy program highlighted in this report through a central, user-friendly and searchable portal at *Massachusetts Transparency*. This would provide citizens with the accessible, comprehensive, timely, one-stop resource they deserve to track their tax dollars and assess the merits of special business tax subsidy programs. The details of proposed subsidies as well as those already agreed upon should be available, giving the public an opportunity both to weigh in before a new project breaks ground and to track performance after the subsidy has been granted.

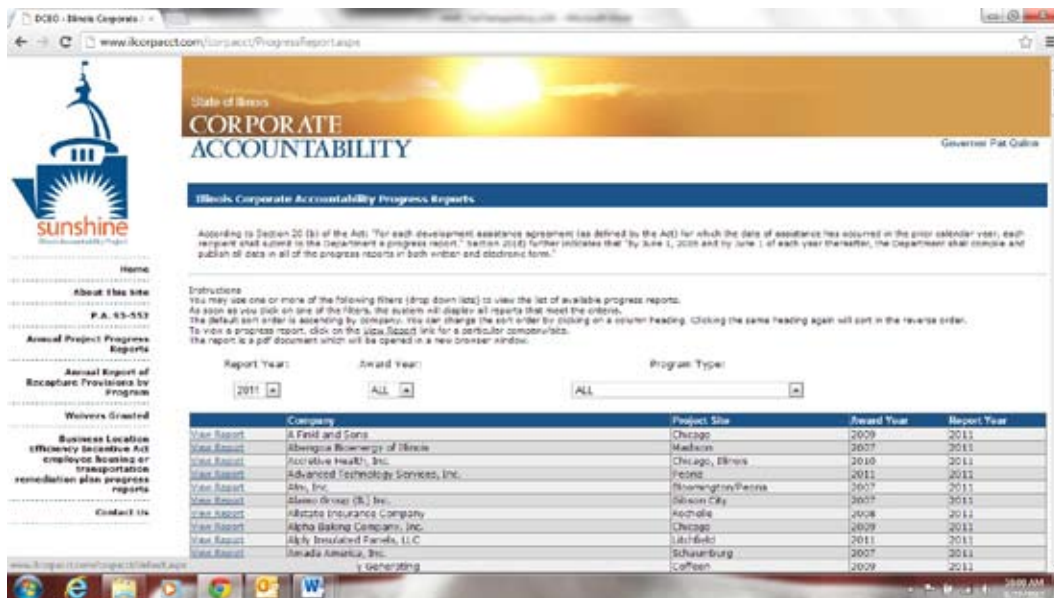
Here, Massachusetts could take cues from Illinois which offers one of the country's best online transparency tools for tax expenditures.⁸⁴ Illinois' website, *Corporate Accountability*, lets the user filter through an alphabetically ordered list of all state-awarded subsidies using drop-down menus to select the tax expenditure program, award year or report year of interest. It also offers a link to each recipient's custom report and links the user to Illinois' *Annual*

Report of Recapture Provisions by Program, a document analyzing the incidence of clawbacks within each subsidy program. The Bay State has shown itself to be a leader in online transparency for budget expenditures and there should be nothing stopping it from improving on Illinois' example and taking the lead here, too.

This transparency tool should go even further and disclose which businesses or subsidy programs fail to meet their targets, as well as statistics on the incidence and size of clawbacks. The nonpartisan watchdog group Good Jobs First believes online disclosure of this information indicates

seriousness in enforcement while providing important information to taxpayers about trends within a tax subsidy program.⁸⁵ For example, if the Economic Development Incentive Program recaptures taxpayer dollars from a high percentage of the businesses that take advantage of its tax credits, the value of the entire program may come under question in the eyes of the public. This is information that the people and decision-makers of Massachusetts deserve and need to make informed decisions about the future of special business tax subsidies.

Figure 6. Illinois' Corporate Accountability Website



Appendix

Massachusetts' Special Business Tax Subsidies since Fiscal Year 1996⁸⁶

Description	Tax Category	Cost in Fiscal Year 2012 (\$ millions)	Reported in Open Checkbook?	Expiration Date	Clawback Provision?	Cost Cap?
Abandoned Building Renovation Deduction	I	4.0	N	None	N	N
Economic Development Incentive Program Credit	I	2.9	Y	None	Y	\$25m*
Credit for Employing Former Full-Employment Program Participants	I	Expired				
Brownfields Credit	I	3.2	Y	Jan. 1, 2014	Y	N
Historic Buildings Rehab. Credit	I	2.5	Y	Dec. 31, 2017	Y	\$50m*
Film Credit, Payroll and Production	I	1.5	Y	Jan. 1, 2023	N	N
Medical Device Credit	I	0.4	Y	None	N	N
Dairy Farmer Tax Credit	I	0.7	Y	None	N	\$4m*
Additional Deduction for Certain Business in a Poverty Area	C	Expired				
Abandoned Building Renovation Deduction	C	Negligible	N	None	N	N
Unequal Weighting of Sales, Payroll and Property in Apportionment Formula (Double-Weighting of Sales and Single Sales Factor)	C	247.6	N	None	N	N
Investment Tax Credit	C	57.9	N	None	Y	N
Research Credit	C	113.5	N	None	N	N
Economic Development Incentive Program Credit	C	21.7	Y	None	Y	\$25m
Credit for Harbor Maintenance Taxes Paid	C	1.0	N	None	N	N
Brownfields Credit	C	24.6	Y	Jan. 1, 2014	Y	N
Historic Buildings Rehab. Credit	C	47.5	Y	Dec. 31, 2017	Y	\$50m
Jobs Incentive Payment for Biotechnology and Medical Device Companies	C	Expired				
Film Credit (Payroll and Non-Wage Production)	C	82.6	Y	Jan. 1, 2023	N	N
Medical Device-User Fee Credit	C	3.6	Y	None	N	N
Life Sciences Tax Incentive Program	C	20.0	Y	Dec. 31, 2018	Y	\$25m
Dairy Farmer Tax Credit	C	6.3	Y	None	N	\$4m
Exemption for Sales to Motion Picture Production Companies	S	0.5	N	Jan. 1, 2023	Y	N
Exemption for Aircraft and Aircraft Parts	S	11.2	N	None	N	N
Exemption for Materials, Tools, Fuels and Machinery Used in Powering Industrial Manufacturing Plants	S	0.0	N	None	N	N
Exemption for Materials, Tools, Fuels and Machinery Used in Newspaper Printing	S	60.4	N	None	N	N
Exemption for Plant and Seed**	S	N/A				
Exemption of Feed**	S	N/A				
Exemption for Commercial Fishing Vessels**	S	N/A				
Exemption for Fuels, Supplies and Repairs for Vessels Engaged in Interstate or Foreign Commerce	S	0.7	N	None	N	N
Exemption for Fuel Used in Operating Aircraft and Railroads	S	56.0	N	None	N	N

*Subject to a combined cost cap shared with the corresponding subsidy applicable to corporate taxes

**Included in a different Tax Expenditure Budget Item since FY01

I = Income C = Corporate S = Sales

Notes

1 Brad Petrishen, “Fidelity to Close Marlborough Facility, Move 1,100 Jobs,” *The MetroWest Daily News*, 15 March 2011.

2 1995 Acts ch. 280.

3 At the local level, beneficiaries of EDIP credits can also negotiate a property tax exemption on a portion of the new real estate tax revenue generated by a project. This is known as tax increment financing (TIF) and is not studied in this report.

4 Mark Arsenault and Todd Wallack, “High-risk Video Game Venture Has R.I., Curt Schilling Reeling,” *The Boston Globe*, 18 May 2012.

5 Louise Story, “As Companies Seek Tax Deals, Governments Pay High Price,” *The New York Times*, 1 December 2012. For the most comprehensive, centralized list available of over 248,000 economic development awards in all fifty states and the District of Columbia (most information sourced from state websites or obtained through Freedom of Information Act requests), see the Subsidy Tracker database produced by Good Jobs First (www.goodjobsfirst.org/subsidy-tracker).

6 Todd Wallack, “Massachusetts Doled Out

\$171 Million in Tax Credits,” *The Boston Globe*, 5 June 2012.

7 MASSPIRG, *New State Budget and Tax Credit Transparency Reforms Signed into Law* (press release), 2 July 2010.

8 The Massachusetts Growth Capital Corporation is one of the Commonwealth’s independent authorities and quasi-public agencies, created by law and funded to some extent by state funds.

9 According to Massachusetts’ General Laws, tax expenditures are “state revenue foregone as a direct result of the provisions of any general or special law which allows exemptions, exclusions, deductions from, or credits against, the taxes imposed on income, corporations, and sales,” (Mass. Gen. Laws ch. 29, § 1).

10 Kurt Wise, Massachusetts Budget and Policy Center, *Business Tax Breaks in Massachusetts*, 7 August 2012.

11 Corporations and businesses paid \$2.32 billion in state taxes in fiscal year 2012 per Massachusetts Department of Revenue, *June 2012 Tax Collection Summary* (press release), 18 July 2012.

12 See note 10.

13 Ibid., 7.

14 Ibid., 12-13.

15 Throughout, this report uses data sourced from the Massachusetts Budget and Policy Center. These data were originally provided by the Massachusetts Department of Revenue and reflect additional detail than what is available through the Department's website. Therefore, the figures described in this report do not necessarily match those provided in publicly available materials.

16 Massachusetts Budget and Policy Center, *The Fiscal Year 2012 General Appropriations Act*, 19 July 2011, 6; 21.

17 Ibid., 11.

18 Ibid., 33.

19 See note 10, 11.

20 Data collected and combined from the Massachusetts Budget and Policy Center and the materials attached to the *Report of the Tax Expenditure Commission*.

21 This table lists all 31 individual special business tax subsidies that have been active and in place at some point since fiscal year 1996. However, using data collected from the Massachusetts Budget and Policy Center and the Massachusetts Department of Revenue, we identified 25 special business tax subsidies that remain in place and distinct in fiscal year 2012. Unless otherwise indicated, this figure forms the basis for analysis throughout the remainder of the report.

22 In fiscal year 2001, Massachusetts began counting these items as part of a single, pre-existing tax expenditure designed to help businesses and corporations avoid pyramiding and double taxation.

23 In all, 18 states currently use the SSF formula to calculate tax liability for all or some of their businesses. Several more are phasing it in per Federation of Tax Administrators, *State Apportionment of Corporate Income*, 23 May 2012.

24 The unequal weighting of sales, payroll, and property in the apportionment formula is an unusual tax subsidy in that the rules it allows for (double-weighting of sales and the SSF formula) fundamentally alter what a beneficiary owes in taxes rather than awarding a credit or exemption

against an existing tax obligation. Therefore, insofar as these particular apportionment rules are concerned, the practical applicability of some of the policy recommendations contained in this report will be somewhat constrained. For example, implementing clawback mechanisms would be a challenge. Similarly, to meet the disclosure requirements this paper calls for, the beneficiaries of special apportionment rules would need to disclose information to the public that is typically kept confidential under law. This study offers broadly applicable and far-reaching policy reforms while recognizing that exceptions will be necessary in unusual circumstances, and that our policy recommendations will not be practical in every instance.

25 State Auditor Suzanne Bump, Office of the State Auditor, *Follow the Dollars: Tax Expenditures*, Spring 2012, 3.

26 "Sunset" data from the Department of Revenue, *Tax Expenditure Master Database*, 2 November 2011; cost totals from the Massachusetts Budget and Policy Center.

27 Commonwealth of Massachusetts, *Report of the Tax Expenditure Commission*, 30 April 2012.

28 See note 2.

29 The legislation promulgating the SSF formula required defense companies to maintain their payroll at 90 percent or more of the 1996 level through the close of calendar year 1999, and mutual funds to increase their employment by 25 percent in the first five years the law was in effect. These requirements no longer apply (Mass. Gen. Laws c. 63, § 38).

30 Michael Levenson, "Bid to Ax Tax Break for Films Rejected," *The Boston Globe*, 12 March 2010.

31 2005 Acts ch. 158.

32 Throughout this report, data on transparency requirements comes from the most recent *Tax Expenditure Master Database*, 2 November 2011, downloaded from www.mass.gov/dor/tax-professionals/news-and-reports/.

33 John Keenan and Brian Wallace, "The Show Must Go On," *The Boston Herald*, 21 March 2009.

34 The SSF formula represents a likely exception because the subsidy fundamentally alters what

the beneficiary owes in taxes, rather than awarding a credit against tax or exempting them entirely. It would be practically challenging to “claw back” the taxes saved through use of an apportionment formula. A sensible alternative would be to reinstate job creation requirements similar to those originally included in the law for mutual funds: if a beneficiary does not increase its Massachusetts-based employment level by the percentage specified in law within a pre-determined time period, the company should be required to calculate its tax liability using the standard apportionment formula.

35 Todd Wallack, “Evergreen, Fidelity Defend Site Closures,” *The Boston Globe*, 30 March, 2011.

36 402 CMR 2.16.

37 Massachusetts Department of Revenue, *Tax Expenditure Master Database*, 2 November 2011.

38 Note: six of these subsidies are sales tax exemptions where capping the total cost to the state would be practically challenging.

39 See note 1.

40 Mass. Gen. Laws c. 63, § 38.

41 Commonwealth of Massachusetts Executive Office of Administration and Finance, *House 2 - FY2013 Budget Recommendation*, downloaded from www.mass.gov/bb/, 17 September 2012.

42 Massachusetts Department of Revenue, *Tax Expenditure Budget*, downloaded from www.mass.gov/dor/tax-professionals/news-and-reports/, 17 September 2012.

43 Massachusetts Department of Revenue, *Tax Credit Transparency Report 2011*, downloaded from www.mass.gov/dor/tax-professionals/news-and-reports/, 17 September 2012.

44 Massachusetts Department of Revenue, *A Report on the Massachusetts Film Industry Tax Incentives*, downloaded from www.mass.gov/dor/tax-professionals/news-and-reports/, 17 September 2012.

45 Benjamin Davis, Frontier Group, and Phineas Baxandall and Ryan Pierannunzi, MASSPIRG Education Fund, *Following the Money 2012: How the 50 States Rate in Providing Online Access to Government Spending Data*, March 2012.

46 The special apportionment rules are likely exceptions to this: providing comprehensive information of this nature for the beneficiaries of the SSF and double-weighted sales formulae will be practically challenging without disclosing typically confidential information.

47 Statutory requirement: Mass. Gen. Laws, ch. 29, § 5B; date of first tax expenditure budget: Commonwealth of Massachusetts, *Report of the Tax Expenditure Commission*, 30 April 2012, 4.

48 Michael Leachman, Dylan Grundman, and Nicholas Johnson, Center on Budget and Policy Priorities, *Promoting State Budget Accountability through Tax Expenditure Reporting*, May 2011.

49 Mass. Gen. Laws ch. 62C, § 89. The affected subsidies studied in this report are: Film Production Credits, Historic Building Rehabilitation Credits, Brownfields Credits, Medical Device Company Credits, Dairy Farmer Credits, Life Sciences Industry Credits, and Economic Development Incentive Program credits.

50 See note 43.

51 Personal communication with Kazim Ozyurt, Massachusetts Department of Revenue, 2 January 2013.

52 Good Jobs First analyzed five tax subsidies in their report, *Money Back Guarantees for Taxpayers*. These were the Economic Development Incentive Program, Film Production Tax Credits, Investment Tax Credits (Manufacturers), the Life Sciences Tax Incentive Program, and Research Tax Credits.

53 Phillip Mattera, et al., Good Jobs First, *Money Back Guarantees for Taxpayers: Clawbacks and Other Enforcement Safeguards in State Economic Development Subsidy Programs*, January 2012.

54 See note 44.

55 Massachusetts Life Sciences Center, *Fiscal Year (FY) 2012 Annual Report: Outpacing the Competition*, 28 September 2012.

56 Todd Wallack, “State Street Isn’t Seeking State Tax Credits for New Boston Office Tower,” *The Boston Globe*, 14 August 2012.

57 WBUR, “Liberty Mutual to Expand Back Bay Headquarters,” *WBUR*, 11 February 2010.

- 58 Boston Redevelopment Authority, *Mayor Menino Announces Major Shot in the Arm to Boston's Economy* (press release), 11 February 2010.
- 59 Todd Wallack, "Liberty Mutual's \$50m CEO Pay Stands Out," *The Boston Globe*, 11 April 2012.
- 60 Shirley Kressel, "Petition to Revoke Liberty Mutual Tax Break," *South End News*, 29 May 2012.
- 61 Boston Redevelopment Authority, *Liberty Mutual Tax Increment Financing Request Q&A*, downloaded from www.bostonredevelopmentauthority.org.
- 62 Mass. Gen. Laws ch. 23A, § 3E.
- 63 See note 27, 1.
- 64 See note 27.
- 65 Pew Center on the States, *Evidence Counts: Evaluating State Tax Incentives for Jobs and Growth*, April 2012.
- 66 See note 10.
- 67 See note 59; Casey Ross, "Liberty Mutual Sets Hub Expansion," *The Boston Globe*, 12 February 2010; Todd Wallack, "Curt Schilling's 38 Studios Files for Bankruptcy," *The Boston Globe*, 7 June 2012.
- 68 See note 27, 15.
- 69 Todd Wallack, "Studios' Credits Let Others Cut Taxes," *The Boston Globe*, 3 January 2012.
- 70 Oregon Department of Administrative Services and Oregon Department of Revenue, *State of Oregon 2009-2011: Tax Expenditure Report*, 2.
- 71 Minnesota Department of Employment and Economic Development, *Business Subsidy Annual Reports*, downloaded from www.positivelyminnesota.com/Government/Business_Subsidy_Reporting/, 17 September 2012.
- 72 H.B. 2067, 75th Leg., Reg. Sess. (Ore. 2009).
- 73 Nevada Const. art. 10, § 6.
- 74 Matt Murphy, "Patrick Aide Calls for Tax Break Reviews," *Commonwealth Magazine*, 28 March 2012.
- 75 See note 27.
- 76 See note 48, 34.
- 77 See note 27.
- 78 "Sunk: Mercury Marine Fiasco Casts Light on Costs of State Subsidy Wars," *OK Policy Blog*, 3 November 2009.
- 79 Jim Offner, "Peregrine Financial Defaulted on Iowa Jobs Deal," *Waterloo-Cedar Falls Courier*, 16 July 2012.
- 80 It is especially important for states to establish clear rules for evaluating company performance relative to goals during economic downturns.
- 81 Robert Weisman, "Massachusetts Life Sciences Initiative Brings Fewer Jobs than Expected," *The Boston Globe*, 14 June 2012.
- 82 Phineas Baxandall and Kari Wohlschlegel, MASSPIRG Education Fund, *Following the Money: How the 50 States Rate in Providing Online Access to Government Spending Data*, April 2010.
- 83 See note 45.
- 84 State of Illinois, *Illinois Corporate Accountability Progress Reports*, downloaded from www.ilcorpacct.com/corpacct/, 17 September 2012.
- 85 See note 53, 3.
86. Cost totals from Massachusetts Budget and Policy Center; other data from Massachusetts' most recent *Tax Expenditure Master Database*, 2 November 2011, downloaded from www.mass.gov/dor/tax-professionals/news-and-reports/.