



JANET T. MILLS
GOVERNOR

STATE OF MAINE
DEPARTMENT OF ECONOMIC
AND COMMUNITY DEVELOPMENT



HEATHER JOHNSON
COMMISSIONER

To: Government Oversight Committee, Maine State Legislature
From: Department of Economic and Community Development
Date: April 12, 2021
Re: Responses to questions about the Pine Tree Development Zone program

On March 11, 2021, the Government Oversight Committee sent the Department of Economic and Community Development (DECD) four questions regarding the Pine Tree Development Zone program. The Department's responses to the Committee's questions are as follows:

1. How might DECD address the alignment of the PTDZ program with the Maine Economic Development Strategy, 2020-2029 (Strategic Plan)?

Robust and well-targeted economic development incentives are a necessary tool for enabling business investments that will move Maine towards the goals of the state's Economic Development Strategy. A program like PTDZ can underpin projects supporting the primary strategies. For example, promoting innovation (Strategy C) can be bolstered by attracting an innovation-focused company with an incentive package anchored by PTDZ benefits. Attracting new talent (Strategy B) can be more viable for a Maine business when they receive the increased Employment Tax Increment Financing (ETIF) payments for new workers through PTDZ certification. Hubs of excellence (Strategy G) can grow further if the industries and businesses within these hubs receive State incentives to expand.

However, the Department does believe that the publication of the Economic Development Strategy, as well as the onset of economic changes due to the COVID-19 pandemic, warrants a full review of the State's key economic development incentives for businesses. While the PTDZ program does speak to some of the strategic plan methods in its current form, we believe the best approach is to review the State's incentive programs with the strategic plan as the starting point. The Department has already begun a review process to thoroughly consider what incentive programs would align best with the State's economic development goals, including benchmarking Maine against other states' programs and seeking input from Maine organizations and stakeholders involved in business attraction and expansion work. The intent is to have a proposal for any recommended policy changes prepared before the 2022 session of the Legislature begins.

The Department believes it is critical to the business community to maintain stability in the PTDZ program until this larger review is complete and input is incorporated from all interested parties. The original hope to complete this review in 2020 to coincide with the 2021 expiration of the PTDZ program was disrupted by the severe impact of the COVID-19 pandemic. As a result, the



JANET T. MILLS
GOVERNOR

STATE OF MAINE
DEPARTMENT OF ECONOMIC
AND COMMUNITY DEVELOPMENT



HEATHER JOHNSON
COMMISSIONER

Department is supporting an extension of the program to allow for the comprehensive review and potential revision of current incentive policy.

2. How will DECD use the Strategic Plan in combination with the final report of the Governor’s Economic Recovery Committee in its work with the 130th Legislature on efforts to revive weakened sectors of the economy, particularly at the small business level?

The PTDZ program is available for specific sectors of the economy that both the Strategic Plan and the final report of the Economic Recovery Committee identify as important to growth and recovery. These include the food and marine, forest products, making and manufacturing, and technical services sectors.¹ The PTDZ program is one way the State can use existing mechanisms to provide direct support to businesses engaged in activity related to strategic goals and initiatives. Part of the work of implementing the Strategic Plan will be to attract innovative businesses to Maine and to foster homegrown entrepreneurship in the targeted sectors.

Businesses that may have been financially impacted by the COVID-19 pandemic could benefit from the PTDZ program as they chart a path towards recovery. The incentives can lower their cost of making purchases as they restart operations and provide them additional capital through the income tax credit and ETIF payments if they are able to start bringing on new workers. The PTDZ program is available to small businesses in these industries—the business needs to add at least one new employee to qualify. However, the post-performance nature of the PTDZ income tax credit and associated ETIF payments mean they are most useful to a business that has some capital cushion to grow their operations and receive the benefits the following year. For a small business whose primary need is capital to restart operations once the pandemic subsides, the program may help smooth the runway in future years but would not provide upfront funding to get the wheels turning again.

The Department will continue to examine ways to align the State’s economic development incentive tools with the stated goals and strategies for recovery and growth. Reviewing Maine’s incentive programs with an eye towards continuing to revive weakened sectors will be an important part of this process, alongside the existing workstreams to implement the Strategic Plan and report of the Economic Recovery Committee.

¹ Maine Department of Economic and Community Development, “Maine Economic Development Strategy 2020-2029,” December 2019, 14.



JANET T. MILLS
GOVERNOR

STATE OF MAINE
DEPARTMENT OF ECONOMIC
AND COMMUNITY DEVELOPMENT



HEATHER JOHNSON
COMMISSIONER

3. How could DECD address the lack of a strong “but for” provision in PTDZ?

The Department implemented changes enacted by the Legislature in 2018 that enhanced the “but for” requirement by requiring companies’ “but for” letters be notarized. Still, the Department concurs in part with OPEGA’s finding that the “but for” provision in the PTDZ program—and the ETIF program—is not a guarantee that supported investments would not have occurred without the PTDZ program. We intend to identify better program administration and targeting methods as part of the ongoing incentive review process and do not want to presuppose the outcome of those discussions and research. However, we do not believe that strengthening the “but for” provision is a worthwhile objective at this time for the following reasons.

First, whether a project would or would not go forward “but for” the PTDZ benefits is not a question that can be answered objectively. The benefits last for ten years and cannot be predicted with substantial accuracy. The value of the PTDZ income tax credit depends on how much profit the company makes each year, and the ETIF payments depend on exactly how many people the company hires, their wages, the average income growth of the county they work in, and factors that affect their withheld income tax amounts.

Of the primary benefits, only the sales tax exemption provides a direct cost-savings that can be calculated ahead of time—but again, it depends on the businesses knowing how much they will purchase over ten years. No company is able to predict its income and expenditures that far in advance. Particularly for new projects, which is what PTDZ supports, businesses’ financial projections are best guesses and only extend two to five years. In this context, it is not possible to answer with certainty whether a project would only be financially viable with the PTDZ benefits. Department staff would be skeptical of a project’s prospects if the business’s plans relied entirely on the receipt of PTDZ tax credits and reimbursements to be financially viable, as the “but for” language implies.

An alternative understanding of the “but for” provision is that it leaves the Department to subjectively gauge whether a proposed investment project would not go forward “but for” the offered incentives. For the “but for” letter to be used this way, Department staff would need to use a combination of market knowledge and relationship-building to feel out whether a business executive is sufficiently influenced by the promise of incentives to commit to a PTDZ-eligible location for their project. This determination would be highly subjective.

This subjective view of the “but for” requirement is a poor fit for the PTDZ program, which is otherwise fixed by statute. The eligibility criteria and amount, type, and duration of benefits is set by law. The Department does not negotiate incentive packages with businesses, and it is not suited



JANET T. MILLS
GOVERNOR

STATE OF MAINE
DEPARTMENT OF ECONOMIC
AND COMMUNITY DEVELOPMENT



HEATHER JOHNSON
COMMISSIONER

to subjectively gauge the validity of a business's "but for" statement when the rest of the law leaves little to subjective judgment. Absent explicit knowledge to the contrary, it would be questionable for the Department to decide a certain business is being dishonest when they submit a "but for" letter when there is no objective way to evaluate their statement and the Department otherwise has no leeway to negotiate the incentives offered to the business.

Whether "but for" provisions are appropriate tools for incentive programs is the subject of continuous discussion nationally. There is general consensus that it is an imperfect tool, but one without a perfect replacement, as OPEGA has noted. Some alternatives have included estimating the probability a certain proportion of projects are successfully incentivized, attempting to ensure at least a minimum positive return on investment.² The 2018 *Comprehensive Evaluation of Maine's Research & Development and Economic Development Incentive and Investment Programs* used this method to estimate the financial return to the State for varying levels of incentive probability.³ A recent report by the Center for Regional Economic Effectiveness proposed using a probability estimation for gauging the importance of incentives to a given project when evaluating proposals as well.⁴

One takeaway from this research is that it is an unreasonable standard to assume that business investments 100% *would* or 100% *would not* happen "but for" an incentive package. A better understanding of business incentives would be that they encourage certain behavior (e.g., investing in certain sectors, paying certain wages) and guide more capital towards sectors or regions that warrant State support.

Based on this ongoing research and the structure of the PTDZ program, DECD does not intend to pursue a strengthened "but for" provision. Instead, a major focus of the incentive program review the Department is undertaking will be the best methods for targeting State funds where needed, monitoring their use, and evaluating their effects.

² Timothy Bartik, "'But For' Percentages for Economic Development Incentives: What Percentage Estimates Are Plausible Based on the Research Literature?," *Upjohn Institute Working Papers*, no. 18-289 (July 1, 2018), <https://doi.org/10.17848/wp18-289>.

³ Barbara Strozzi, "Comprehensive Evaluation of Maine's Research & Development and Economic Development Incentive and Investment Programs" (Investment Consulting Associates, January 2018), 33-44, <https://www.maine.gov/decd/sites/maine.gov/decd/files/inline-files/Comprehensive%20Evaluation%20of%20Maine%E2%80%99s%20Research%20%26%20Development%20and%20Economic%20Development%20Incentive%20and%20Investment%20Programs%20-%20January%202018.pdf>.

⁴ Center for Regional Economic Competitiveness and Smart Incentives, "Estimating the Influence of Incentives on Investment Decisions: A New Approach to the but-for Question" (Smart Incentives, November 2020), <https://smartincentives.org/wp-content/uploads/Estimating-the-Influence-of-Incentives-Nov-2020.pdf>.



JANET T. MILLS
GOVERNOR

STATE OF MAINE
DEPARTMENT OF ECONOMIC
AND COMMUNITY DEVELOPMENT



HEATHER JOHNSON
COMMISSIONER

4. What recommendations does DECD have to strengthen program management and oversight of PTDZ to help ensure the program is effective?

Strong recommendations for improved program management and oversight are a key goal of the ongoing incentive program review. For economic development incentives to be beneficial to Maine's economy, State funding (or foregone revenue) must go where it can have the greatest impact. For the impact of incentives to be accurately evaluated, they must be structured in such a way that data on spending and outcomes is easily tracked and reported. Streamlined program management can not only improve program effectiveness through State evaluation but make the program more appealing and accessible to businesses. To these ends, as part of the review process, the Department will seek out methods to improve targeting, provide clearer benefits and reporting, and supply more transparent data.

Crucially, the State's incentive policies can only be as effective as the tools used to manage them. The Department has begun implementation of Salesforce, which will be a more modern tool for business relations, reporting, and analysis to manage PTDZ and other DECD programs. The current program management system is outdated and severely constrains the level and accuracy of metric-based evaluations of the PTDZ program. The Department's initiative to implement Salesforce, a customer relationship management (CRM) tool, will significantly improve staff ability to connect businesses to the right programs, obtain and analyze program data, and reduce administrative burdens on staff and businesses. Upgrading to this tool had been delayed most recently by the COVID-19 pandemic and its effect on funding, but once implemented, the Department will have in place a key building block of strengthened program management and oversight.