State of Oklahoma
Incentive Evaluation Commission

Point-of-Sale Motion Picture Sales Tax Exemption
Final Draft Evaluation

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Key Findings and Recommendations

Incentive Overview

On or after July 1, 1996, the state of Oklahoma exempts sales of tangible personal property or services to a motion picture or television production company to be used or consumed in connection with an eligible production from the state and local sales and use tax. To qualify for the exemption, the motion picture or television production company must file required documentation and information with the Oklahoma Tax Commission (OTC).

Recommendation: Reconfigure

Key Findings:

- **The sales tax exemption pre-dates the Film Production Rebate, and the rebate may not be taken in conjunction with the sales tax exemption.** This was a requirement of the Film Rebate when it was enacted as the Compete with Canada Act. The relevant section of that legislation reads "A production company shall not be eligible to receive both a rebate payment pursuant to the provisions of Section 3621 et seq. of this title and an exemption from sales taxes pursuant to the provisions of paragraph 23 of Section 1357 of this title." The requirement was also included in the subsequent Filmed in Oklahoma Act. It is clear that the Legislature intended that the programs not be layered.

- **The sales tax exemption has been relatively little used.** The Oklahoma Tax Expenditure Report identifies the high-water mark for the incentive as the 2022 biennium, with estimated foregone revenue of $763,000. Since 2006, no other tax expenditure report has estimated the foregone revenue as reaching $150,000.

- **There are no minimum requirements related to film production budget, wages and salaries paid, or number of Oklahoma residents employed on the project.** It is an 'as of right' credit, meaning if the necessary documentation is provided to the OTC, the production is eligible for the exemption. As a result, the incentive criteria for evaluation related to job creation or employment and wages cannot be quantified.

- **Most productions will choose the tax rebates under the Film Production Rebate.** Because the two credits cannot be taken together, it becomes a process of determining which provides the better return. The Film Production Rebate is 20-30 percent of qualified expenditures, which includes a large share of crew salaries. By contrast, the sales tax exemption will forego sales taxes for taxable purchases (primarily tangible goods). The average combined state and local sales tax rate in Oklahoma is 9 percent. Productions that might choose the sales tax exemption might have budgets that do not meet the threshold for the Film Production Rebate, might not be awarded a rebate by the Department of Commerce, might not meet statutory requirements of that program, or might have significant up-front sales taxable purchases that make it beneficial to take the sales tax exemption. Given the activity within the two programs, the sales tax exemption is generally not the first choice.

- **Oklahoma is not alone in offering this type of sales tax exemption, but a few states target film production infrastructure.** Benchmarking identified nine states with some form of sales tax exemption for the motion picture industry. These can be split into those similar to Oklahoma's (for film production taxable purchases) and those that apply to film production infrastructure. Of the latter, Texas allows for an exemption for the construction, maintenance, expansion, improvement or renovation of a qualified media production facility. California has a similar exemption.

- **The return on investment, in terms of foregone state sales tax revenue compared to economic activity that translates into state tax revenue, is negative.**

- **The administrative aspects of the program are straightforward.** The statute identifies the requirements for a film production to receive the credit, which are clear. When that is the case, the OTC certifies the exemption.

- **The exemption is neutral on incentive best practices.** It does target a specific industry, although it is probably not the right tool for that targeting. The OTC tax expenditure report does estimate its foregone revenue (transparency). It is an 'as of right' credit and not discretionary. There is no dollar cap associated with it (although past use suggests this isn't a major issue).

- **Given its limited use, it is worth considering alternatives to the current construction.** In general, the project team identified and analyzed the following:

  - Maintain the current exemption with no changes. The current exemption does get some use, even if usually minimal, so some film productions are finding it useful.

  - Allow it to be layered with the Film Production Rebate. This has the potential to significantly expand the foregone revenue associated with the incentive. From the project team's perspective, this expansion would carry risk associated with the cost that could not be readily ameliorated with a dollar cap. The project team does not view this as an effective way to add to film production activity.

  - Dedicate it to infrastructure associated with the film post-production industry. This appears to have the greatest potential to be additive and provide growth opportunities for the film industry. As is discussed in the Film Production Rebate, one of the challenges for Oklahoma is developing the industry infrastructure that will make film production more than a 'one off' major project from year to year. One way to grow the industry is to create the infrastructure around it.

- **The project team recommends modifying the sales tax exemption to apply to film production infrastructure.** A model is Texas, which provides its exemption for the construction, maintenance, expansion, improvement, or renovation of a qualified media production facility. As discussed in the separate evaluation of the Film Production Rebate, a continuing challenge is to grow the industry in a way that is sustainable. While several major motion pictures and/or television series have been filmed in Oklahoma, the employment, salary and wages associated with the permanent aspects of the industry is still very small. Targeting industry infrastructure is probably the most strategic way to use this exemption.

Introduction

Incentive Evaluation Commission Overview

In 2015, HB2182 established the Oklahoma Incentive Evaluation Commission (the Commission). It requires the Commission to conduct evaluations of all qualified state incentives over a four-year timeframe. The law also provides that criteria specific to each incentive be used for the evaluation. The Commission has completed two cycles of qualified evaluations, from 2016-2019 and 2020 through 2023. This is now the first year of a new four-year cycle.

In 2023, the Legislature approved, and Governor Stitt signed into law SB 745, which made a number of changes to the incentive evaluation process that were recommended by the Commission. Among them was the ability of the Commission to review qualified incentives within the four-year evaluation cycle. In prior cycles, incentives had to be reviewed at least once every four years, which effectively locked in place the order that incentives would be evaluated. As a result, some incentives in this cycle may be reviewed in less or more than four years.

One reason for the change in the evaluation cycle was to allow incentives with similar purposes or that are targeted to specific industries or parts of the state to be evaluated in the same year. This allows for continuity in the discussion and comparisons of effect and effectiveness. This grouping is considered an evaluation best practice.[1] For 2024, there are two broad categories of evaluated incentives:

- Financing/Venture Capital/Early Business related.
- Tourism/Film/Quality of Life related.

This evaluation of the sales tax exemption for a motion picture or television production company, administered by the Oklahoma Tax Commission (OTC) is one of 12 evaluations being conducted by the Commission in 2024 and fits within Tourism/Film/Quality of life incentives category. Based on this evaluation and their collective judgment, the Commission will make recommendations to the Governor and the State Legislature related to this program.

This sales tax exemption has not been evaluated in either prior incentive evaluation cycle. The actual dollar value associated with the incentive is well under the $1 million of financial impact per year threshold set by the Incentive Evaluation Commission. At the recommendation of PFM, the Commission chose to evaluate it this year, but some of the assumptions for evaluating it have proven to not be the case.

2024 Criteria for Evaluation

To assist in a determination of program effectiveness, the Commission adopted the following criteria:

- Marginal wages and salaries paid to Oklahoma residents by films eligible for the exemption–comparison to period prior to the exemption.
- Film-related expenditures in Oklahoma by films eligible for the exemption – comparisons to period prior to the exemption.
- Growth in employment and wages in the industry in Oklahoma compared to nationally and benchmark states (shift share analysis).
- Additional identifiable business activity directly or indirectly produced by films eligible for the exemption.
- Additional identifiable benefits that accrue to the State by films eligible for the exemption.
- Return on investment (economic activity versus rebates paid).

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[1] "Best Practices for Planning Tax Incentive Evaluations: Lessons Learned from Indiana's Evaluation Process," Pew Charitable Trusts, August 2022, p.3. Accessed electronically at www.pewtrusts.org/-/media/assets/2022/08/best-practices_incentiveeval-planning_2022-3-24_final.pdf

2024 Evaluation Approach

To conduct its 2024 review of the Film Enhancement Rebate, the project team conducted the following activities:

- Submitted an information request to OF+MO and the OTC;
- Reviewed and analyzed OF+MO-provided data;
- Completed subject matter expert/internal stakeholder interviews with representatives from OF+MO;
- Benchmarked Oklahoma's incentive relative to peer state programs;
- Conducted an economic impact analysis of the incentive.

Industry Background

Oklahoma's Sales Tax Exemption for Eligible Productions

As explained in the discussion of the larger and more oft-used Film Production Rebate program, states began creating these types of credits or rebates in the late 1990s and into the 2000s. This sales tax exemption, which was effective in 1996, preceded much of that activity.

However, this sales tax exemption has not generated a lot of use. The following is the report on its use from the OTC's biennial tax expenditure reports:[2]

Table 1: Claimed Sales Tax Exemptions for Qualified Film or Television Productions

Fiscal Year	Exempted Amount
2006	Minimal[3]
2008	$57,000
2010	$3,000
2012	$10,800
2014	$142,000
2016	$145,200
2018	68,000
2020	$763,000
2022	$43,000

Source: Oklahoma Tax Commission

As demonstrated in the preceding table, in no year have the claimed sales tax exemptions met the $1 million threshold for review by the Incentive Evaluation Commission. A factor that likely limits its use is that the sales tax exemption may not be combined with the Film Production Rebate.[4] It is notable that this restriction is not found in some other states that have a similar sales tax exemption and film production credit or rebate.[5]

Film Production Activity: State Competition

As also noted in the evaluation of the Film activity has been concentrated primarily in California and secondarily in New York for decades. The following graph provides a historic representation of that fact.

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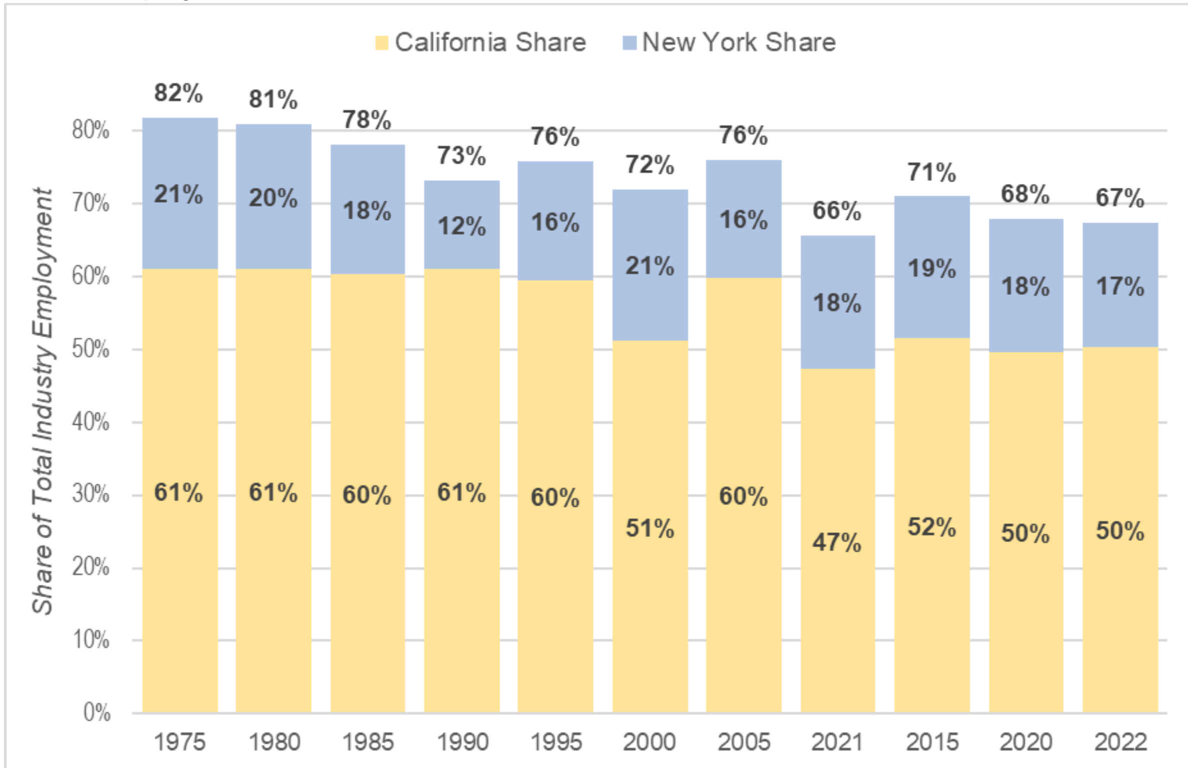
[2] The state tax expenditure reports for each biennium since 2006 may be found on the OTC website accessed electronically at https://oklahoma.gov/tax/reporting-resources/reports.html

[3] While dollar values were provided in each of the other tax expenditure reports related to this exemption, 'minimal' was how it was estimated in the 2006 report, which was accessed at https://oklahoma.gov/content/dam/ok/en/tax/documents/resources/reports/tax-expenditure/TaxExpenditureReport-2005-2006.pdf

[4] This restriction is found in the statute that created the Filmed in Oklahoma Act. Oklahoma State Statute Chapter 68-3624(E) reads "A production company shall not be eligible to receive both a rebate payment pursuant to the provisions of Section 3621 et seq. of this title and an exemption from sales taxes pursuant to the provisions of paragraph 23 of Section 1357 of this title."

[5] This is discussed in the benchmarking section of the evaluation.

Figure 1: New York and California Share of Nationwide Motion Picture and Video Production and Post-Production Employment, 1975-2022



Source: PFM analysis of BLS QCEW data for NAICS codes 51211 and 51219

That said, the share for California and New York is eroding, and this can be at least partially attributed to the rise of significant film incentive programs in a number of states. The states that have made the largest investments (in terms of foregone revenue from film tax credits besides California and New York) include Georgia (an uncapped credit that has been over $1.0 billion in claims in some years), Louisiana ($150 million cap), New Jersey ($100 million cap), New Mexico ($110 million and growing by $10 million a year to $160 million), and Pennsylvania ($100 million cap).

According to an analysis by the National Conference of State Legislatures, 38 states offer some form of film and television incentive program.[6] They also note that, since 2021, at least 18 states have enacted measures to implement or expand film tax incentives.

The number of states that offer a sales tax exemption for eligible purchases related to this industry is not nearly as extensive. Besides Oklahoma, the project team identified similar types of sales tax exemptions in seven other states – California, Connecticut, Florida, Maryland, Massachusetts, Texas, and Virginia.

It is understandable why most film and related productions would choose the Oklahoma film production rebate rather than the sales and use tax exemption. While both relate only to eligible purchases or related expenditures, the production rebate starts at a 20 percent rebate and can grow to 30 percent, while the sales and use tax exemption will cover the state rate (4.5 percent) and the local rate (which, according to the Tax Foundation is an average of 4.5 percent in 2024), for a total of 9 percent.[7]

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6 "State Film and Television Incentive Programs," National Conference of State Legislatures, April 8, 2024, accessed electronically at https://ncsl.org/fiscal/state-film-and-television-incentive-programs

7 "State and Local Sales Tax Rates, Midyear 2024," July 9, 2024, The Tax Foundation, accessed electronically at https://taxfoundation.org/data/all/state/2024-sales-tax-rates-midyear/

Incentive Usage and Administration

Incentive Characteristics[8]

The sale of tangible personal property and services to a motion picture or television production company are exempt from sales and use taxes in Oklahoma, if used or consumed in connection with an eligible production. An eligible production is a documentary, special, music video, or a television commercial or television program that will serve as a pilot for or be a segment of an ongoing dramatic or situation comedy series, filmed or taped for network or national or regional syndication; or a feature-length motion picture intended for theatrical release or for network or national or regional syndication or broadcast. To be eligible for the exemption, a motion picture or television production company must make the purchases for use in producing an eligible production. It is also necessary for the company to first receive an exemption letter form the OTC for its eligible production.

The following are examples of (but not limited to) exempt items:

- Accommodations and meals.
- Production equipment purchases and rentals.
- Set construction and rigging materials.
- Production office equipment and supplies.
- Prop and wardrobe purchases and rentals.
- Utilities used by the production company on location and in the production office.

Unlike the Film Production rebate, there is no minimum production budget or requirements related to the use of Oklahoma labor to qualify for the exemption. This is a ‘by right’ exemption, meaning the OTC has no discretionary authority in granting the exemption.

Application Process

An application for exemption is made by submitting to the Business Tax Services Division, OTC, a completed Form 13-88, contained in Packet E, available online at www.tax.ok.gov.[9]

Once the application is received, the OTC reviews it and makes a determination as to the applicant's eligibility. Upon approval, a letter certifying that the exemption is allowed is sent to the applicant. Certification may be denied, cancelled, suspended, or revoked by the OTC for non-compliance with the applicable administrative rules, Oklahoma tax statutes, or for other good cause shown.

Use of the Exemption

Persons claiming the exemption provide their vendors with a copy of the certification letter issued by the OTC and a signed statement that the purchase is being made exempt from sales tax. Any letter certifying an exemption is valid only for use by the person claiming the exemption and is not transferable. The exemption may not be used by any other entity, even if that entity claims to be an agent, administrator, party to a contract or other relationship. Each entity desiring to obtain a letter certifying an exemption must make application in its own name.

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[8] These are all included in administrative rules for the program, Oklahoma Administrative. Code § 710:65-13-194.
[9] The packet and form are included in the Appendix.

Economic and Fiscal Impact

Economic Impact Analysis

A detailed description of the IMPLAN economic impact methodology is provided in Appendix C.

The economic and fiscal impact of the film sales tax exemption was measured by accounting for the sales tax exemptions that were claimed. This foregone tax revenue would be considered additional dollars that qualifying companies could utilize in their film production process, either through additional payroll or other production expenses. The economic and fiscal impacts are summarized in the following table.

Table 2: Economic and Fiscal Impacts, 2018 - 2022

Effect	Jobs	Labor Income	Value Added	Output	Est. OK Tax Revenue
Direct	5	$129,864	$189,162	$873,000	$26,271
Indirect	3	$127,852	$204,850	$463,523	$10,110
Induced	1	$52,543	$93,449	$172,512	$5,743
Total	9	$310,259	$487,461	$1,509,035	$42,124

As has been discussed, this is a little used sales tax exemption, and the generated tax revenue does not create a positive return on investment for the state.

Incentive Benchmarking

Benchmarking

A detailed description of comparable state programs can be found in **Appendix E.**

For evaluation purposes, benchmarking provides information related to how peer states use and evaluate similar incentives. At the outset, it should be understood that no states are ‘perfect peers’ – there will be multiple differences in economic, demographic and political factors that will have to be considered in any analysis; likewise, it is exceedingly rare that any two state incentive programs will be exactly the same.[10] These benchmarking realities must be taken into consideration when making comparisons – and, for the sake of brevity, the report will not continually re-make this point throughout the discussion.

The process of creating a comparison group for incentives typically begins with bordering states. This is generally the starting point, because proximity often leads states to compete for the same regional businesses or business/industry investments. Second, neighboring states often (but not always) have similar economic, demographic or political structures that lend themselves to comparison.

In the case of the Motion Picture Sales Tax Exemption, nine states were identified with a similar type of sales tax exemption.

California provides an exemption from the state (but not city or county) sales and use tax for the sale, storage, use, or other consumption of machinery, equipment including component parts used primarily in teleproduction or other postproduction services. The exemption also includes property sold or purchased primarily to maintain, repair, measure, or test any property used in teleproduction or postproduction services. The partial exemption may also apply to rental receipts for teleproduction or postproduction equipment and machinery.

Connecticut provides an exemption from sales and use tax for items purchased for use in audio or video production or broadcasting.

Florida provides a sales and use tax exemption on production-related purchases by a qualified production company producing motion pictures, made for television motion pictures, television series, commercial advertising, music videos, or sound recordings in Florida. The purchase must be of tangible personal property and must be used exclusively as an integral part of the production activities in Florida. The equipment must be depreciable with a useful life of at least three years. The exemption may also be extended to parts and accessories for qualified production equipment.

Maryland provides an exemption from the 6 percent state sales and use tax to qualified feature, television, cable, commercial, documentary, music video, or related projects. The exemption is for taxable sales, rentals and services.

Massachusetts provides a sales tax exemption for any motion picture production company that spends $50,000 or more in Massachusetts on qualifying costs during a consecutive 12-month qualifying period. Eligible uses are for feature-length film, video, digital media project, a TV series with a maximum of 27 episodes, a commercial for theatrical or TV viewing or as a TV pilot. Multiple episodes of a TV series or multiple commercials for the same client may be aggregated to qualify.

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[10] The primary instances of exactly alike state incentive programs occur when states choose to ‘piggyback’ onto federal programs.

Texas allows for a sales and use tax exemption for the construction, maintenance, expansion, improvement, or renovation of a media production facility at a qualified media production location over a two year period. Media production facilities include, but are not limited to animation/CGI studios, post production facilities, sound stages, video game development studios and production office space.

Separately, a producer or production company may claim a sales or use tax exemption on items or services necessary to and used or consumed directly during the production of a project intended for commercial distribution such as a feature film, commercial, television project, or recording of live performances.

Virginia provides a sales tax exemption for audiovisual works production that applies to any audio or video tape, film, or other audiovisual work where it is acquired for the purpose of licensing, distributing, broadcasting, commercially exhibiting, or reproducing the work. The exemption also applies to production services or fabrication in connection with the production of any portion of such audiovisual work and other tangible personal property incident to the performance of such services or fabrication. The exemption also applies to equipment and parts and accessories used or to be used in the production of such audiovisual works.

Benchmarking Return on Investment Studies of the Film Incentives

While states continue to offer the incentives (and expand them in many instances), the impact studies mostly conclude that they do not provide a positive return on investment for the state.

Findings in Other State Studies

Many of the other state evaluations had a broader scope that looked at issues beyond economic impact. The methods used to weigh economic impact and return on investment also vary. In general, however, most of the studies identify some basic findings that are also evident, to some degree, in this study. These include:

- The industry is nomadic, and it will shop for locations based on the available incentives.[11]
- Because of the temporary/nomadic nature of the industry, most spending will be for labor costs, and a low proportion will be for capital investment.[12]

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[11] As was noted in the “Evaluation of Alabama’s Entertainment Industry Incentive Program…” (2017), “perhaps the worst efficiency-related outcome of state entertainment industry incentive programs is that they pit the states against each other in a high-stakes competition for highly mobile activity. This almost certainly results in a significant portion of the benefits going to out-of-state entities and does not leave a lasting economic impact in any particular filming location.”

[12] The Rhode Island Department of Revenue “Evaluation of Motion Picture Production Tax Credits (2022) notes that “The small amount of capital investment can be explained by the fact that many of the …recipient firms are short-term entities incorporated by out-of-state production firms for the length of the production and lacking a substantial physical presence in the state. These firms do not make typical capital investments such as owning or renting real estate for offices and production space. Furthermore, to the extent that firms with a significant, long-term physical presence in Rhode Island do take advantage of the [credit], these firms’ capital investments would not be associated with a single motion picture production and therefore would not be eligible to be considered certified production expenses for the purposes of the [credit].”

- Much of the associated spending for the incented projects will occur out of state, which lessens the expected economic impact.[13]
- There are indirect positive effects associated with entertainment productions, but it is difficult to attach a dollar value to them.[14]
- As a result, the return on investment, as measured by state tax dollar collections associated with the incented projects versus the tax incentives, is generally (but not always) determined to be negative for the state.[15]
- There are also doubts that film tax credits have a major impact on employment and film production within the states. A 2018 study on California's Film Production Tax Credit 2.0 found no link between the program and film production within the state, nor did it find that other states' spending in similar programs led to a decrease in filming within California.[16]

Outside Studies

Besides state evaluations, there have been many academic studies of related incentives, as well as studies funded by the Motion Picture Association and/or other groups. Among academic studies, one often-cited paper examined the effect of motion picture incentives from 1998 through 2013 on all 50 states. For a variety of reasons, it found little efficacy related to the incentives and growth of the industry in that state. Interestingly, it found that a significant factor that limited growth in other states was the industry concentration in California and New York State.[17] Another academic paper compared the economic impact of the Georgia film tax credit based on a report by the Georgia Department of Economic Development to the author's separate findings. In this case, the author found a significantly lower economic impact.[18]

In many instances, these studies tend to focus on different impacts and results. As was noted in a recent informational brief by the Louisiana Legislative Auditor (LLA), return on investment (and, for that matter, economic impact) can be calculated in different ways. The LLA noted, for example, that a study by the Louisiana Department of Economic Development examined return on investment (ROI) based on an increase in household income versus the cost of the credits issued; in contrast, a study by the

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[13] The Georgia Department of Audits and Accounts 'Impact of the Georgia Film Tax Credit (2020)' noted that 'While the $818 million to nonresident workers included is included in the direct labor income, it has little impact on the Georgia economy because nonresidents are expected to spend their wages in their home state. Production companies are typically required to pay for nonresidents' living expenses (e.g., hotel, transportation, per diem) while the worker is away from home. These living expenses were included in our impact analysis. As a result, nonresidents are unlikely to spend significant portions of their wages while in Georgia."

[14] The Alabama evaluation notes that "To be sure, certain productions can bring indirect advertising, visibility, and prestige effects that might increase tourism or general interest in an area, but those effects are exceedingly difficult to quantify."

[15] See, for example, Independent Fiscal Office, "Pennsylvania Film Production Tax Credit, An Evaluation of Program Performance (January 2019), p. 15 for a summary of recent state RIOs from other evaluations.

[16] Michael Thom, "Time to Yell 'Cut?' an Evaluation of the California Film and Production Tax Credit for the Motion Picture Industry," California Journal of Politics and Policy 10, no. 1, May 13, 2018, accessed online at https://doi.org/10.5070/p2cjpp10138993.

[17] Michael Thom, "Lights, Camera but No Action? Tax and Economic Development Lessons from State Motion Picture Incentive Programs," American Review of Public Administration, 2018, accessed online at https://doi.org/10.1177/0275074016651958.

[18] John Charles Bradbury, "Film Tax Credits and the Economic Impact of the Film Industry on Georgia's Economy," Kennesaw State University Policy Brief, August 15, 2019, accessed online at https://dx.doi.org/10.2139/ssrn.3407921.

Louisiana Department of Revenue focused on fiscal ROI – the increase in state revenue versus the cost of the credits issued.

Motion Picture Association (MPA) studies have reached different conclusions. The MPA has funded studies in numerous states and has used those to make the case for existing, new, or expanded film tax credits.

Appendices

Appendix A: Program Statute

§68-1357.9. Service transactions among related entities - Exemptions.

A. There are exempt from the taxes imposed by Section 1351 et seq. of Title 68 of the Oklahoma Statutes service transactions among related entities.

B. For purposes of this section, "related entity" includes persons as defined by subsection (b) of Section 267 of the Internal Revenue Code.

C. An exemption authorized by this section does not apply to a service that would have been taxable under Section 1351 et seq. of Title 68 of the Oklahoma Statutes as it existed on July 1, 2003.

D. Services that are exempt under this section may not be purchased for resale by the providing company.

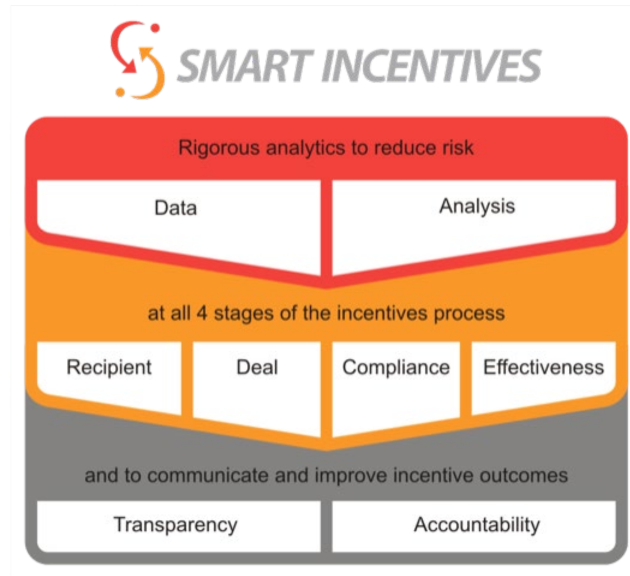
E. Tangible personal property that is transferred as an integral part of a service exempted under this section may not be purchased for resale by the providing company. Added by Laws 2003, c. 462, § 1, eff. July 1, 2003.

23. Sales of tangible personal property or services to a motion picture or television production company to be used or consumed in connection with an eligible production. For purposes of this paragraph, "eligible production" means a documentary, special, music video, or a television commercial or television program that will serve as a pilot for or be a segment of an ongoing dramatic or situation comedy series filmed or taped for network or national or regional syndication or a feature-length motion picture intended for theatrical release or for network or national or regional syndication or broadcast. The provisions of this paragraph shall apply to sales Oklahoma Statutes - Title 68. occurring on or after July 1, 1996. In order to qualify for the exemption, the motion picture or television production company shall file any documentation and information required to be submitted pursuant to rules promulgated by the Tax Commission.

Appendix B: Incentive Best Practices

There has been extensive writing around what constitute business incentives best practices. From the project team's review of many sources,[1] it has identified 10 important best practices and sought to incorporate them into the analysis and discussion of this incentive.

As a starting point, business incentives should be viewed as a process, not an event. The award of an incentive and the incentive features are part of that process, and many of the identified best practices reflect that. The process itself should take into consideration each of these factors, which PFM's subcontractor, Smart Incentives, demonstrates in the following illustration:



While the project team believes this is a strong set of best practices, there may well be others that are as (or more applicable) in specific situations. It is also likely that some of the best practices will come into conflict in some situations. For example, application and reporting requirements may reduce the simplicity of business compliance. As a result, these will always be subject to analysis on a case-by-case basis.

The 10 best practices are:

1. **For maximum impact, incentives should be targeted.** Examples of useful targeting include companies or industries that export their goods or services out-of-state; high economic impact companies or industries – such as those with higher wages and benefits, significant job creation, or significant capital investment.

2. **Incentives should be discretionary.** In most instances, an application process enables the state government to require company disclosure of information related to eligibility criteria and enables the state to reject applications that do not meet its standards.

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[1] Three resources in particular were relied upon on putting together the list of best practices. They are "What Factors Influence the Effectiveness of Business Incentives?" The Pew Charitable Trusts, April 4, 2019, accessed electronically at https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2019/04/what-factors-influence-the-effectiveness-of-business-incentives; "Improving Economic Development Incentives," Timothy J. Bartik, W.E. Upjohn Institute for Employment Research, 2018, accessed electronically at https://research.upjohn.org/cgi/viewcontent.cgi?article=1000&context=up_policybriefs; "Best Practices for the Design and Evaluation of State Tax Incentives Programs for Economic Development," Matthew N. Murray and Donald J. Bruce, January 2017, included within another evaluation at https://media.al.com/news_mobile_impact/other/AL%20ENTERTAIN%20NEWMKTS%203%209%2017.pdf

3. **Incentives should leverage significant private capital.** Ideally, the incentive should leverage private investment that is at least several multiples of the state investment.

4. **Incentives should provide most of the benefit within 1-3 years and have a limited duration.** Company discount rates are much higher than for the state, and businesses will significantly devalue incentive payments in later years.

5. **Incentives should take into consideration state and/or local as well as industry economic conditions.** Incentives that are provided in high performing areas or for stable and profitable businesses or industries will likely fail the 'but for test' – meaning the activity would likely occur without the state incentive.

6. **'Smart' incentives help businesses overcome practical barriers to growth.** In particular, customized assistance for locally owned, small and medium-sized businesses can have significant impact.

7. **Incentives should be transparent.** The incentive purpose should be clearly articulated, as are eligibility requirements, and regular, detailed reporting should be required from all program recipients.

8. **Incentives should require accountability.** When upfront financial incentives are offered in return for job creation, retention, or capital investment, there should be contract language in place that allows the state to 'claw back' state resources should the company not meet performance requirements.

9. **Incentives should have caps.** To ensure the state's financial health, program dollar caps or limits should be in place. Incentive programs should also have a limited duration, with sunsets in place to require regular review of incentive performance.

10. **Incentives should be simple and understandable.** The state should be able to easily and effectively administer the incentive, and users should be able to readily comply with its requirements.

Appendix C: IMPLAN Economic Impact Methodology

The economic impact methodology utilized to determine the multiplier effects is IMPLAN (Impact Analysis for PLANning), a proprietary model; PFM has obtained a license for use of the IMPLAN model for these evaluations.

IMPLAN's Social Accounting Matrices (SAMs) capture the actual dollar amounts of all business transactions taking place in a regional economy as reported each year by businesses and governmental agencies. SAM accounts are a better measure of economic flow than traditional input-output accounts because they include "non-market" transactions. Examples of these transactions would be taxes and unemployment benefits.

Multipliers

SAMs can be constructed to show the effects of a given change on the economy of interest. These are called Multiplier Models. Multiplier Models study the impacts of a user-specified change in the chosen economy for 440 different industries. Because the Multiplier Models are built directly from the region-specific SAMs, they will reflect the region's unique structure and trade situation.

Multiplier Models are the framework for building impact analysis questions. Derived mathematically, these models estimate the magnitude and distribution of economic impacts, and measure three types of effects which are displayed in the final report. These are the direct, indirect, and induced changes within the economy.

- **Direct** effects are determined by the Event as defined by the user (i.e., a $10 million order is a $10 million direct effect).
- The **indirect** effects are determined by the amount of the direct effect spent within the study region on supplies, services, labor, and taxes.
- Finally, the **induced** effect measures the money that is re-spent in the study area as a result of spending from the indirect effect.

Each of these steps recognizes an important leakage from the economic study region spent on purchases outside of the defined area. Eventually, these leakages will stop the cycle.

Fiscal Impacts

The IMPLAN tax report captures all tax revenue in the study area, across all levels of government that exist in that study area, for the specific industries and institutions affected by an event or group of events. Tax Impact results are based on the collected and reported taxes within the region for the given data year. IMPLAN taxes shown (and collected) are industry and geographically specific. The IMPLAN tax impact report splits the tax impacts into the various tax categories based on the picture of that region's economy. But, there is no industry-specific profile for taxes paid by tax category, so the distribution across tax categories is an all-industry average. While this is a limitation of the IMPLAN fiscal reporting, the IMPLAN tax report serves as an appropriate measure of jurisdictional tax results in the aggregate. Tax results cannot be added to any summary or detailed results as they are already included as a portion of Output. State taxes do not include taxes or district assessments levied by Federal, county, sub-county, city or township governments.