INDEPENDENT FISCAL OFFICE

TO: Honorable Members of the Pennsylvania Performance-Based Budget (PBB) Board

FROM: Matthew Knittel, Director
Independent Fiscal Office

DATE: January 5, 2024

RE: PBB Board Motion for IFO to Review Initial Tax Credit Reports

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On April 24, 2023, the PBB Board directed "… *the Independent Fiscal Office (IFO) to review each performance-based budget and tax credit performance review completed by the IFO in the prior five-year period for purposes of determining the following:*

- *Whether commonwealth agencies implemented the performance metrics recommended by the IFO, how the metrics were used, and the impact the metrics had on improving programmatic outcomes;*
- *Whether commonwealth agencies and the General Assembly used the performance-based budget reports and tax credit reviews to inform budget and policy decision-making, including any specific examples of such use by the agencies or General Assembly;*
- *Whether the General Assembly or the commonwealth agencies reviewed by the IFO have any recommendations on ways to improve the performance-based budget and tax credit review process and the IFO's evaluation of those recommendations.*

The review conducted by the IFO pursuant to this motion shall be in lieu of conducting any performance-based budget or tax credit reviews in calendar year 2023. The IFO should present its findings and recommendations to the board in January 2024."

This memo provides the results from the tax credit review. A separate memo provides results from the PBB reviews. The office would like to thank the Office of the Budget for coordinating the agency responses, agency staff for their timely completion of surveys and General Assembly staff that met with IFO to provide feedback.

Background

Act 48-2017 directed the IFO to review state tax credits over a five-year period. (See the Initial Tax Credit Review Schedule below.) As of January 2023, the IFO had conducted a review of all tax credits in existence when Act 48 was enacted and those reports were approved by the PBB Board. On April 24, 2023, the PBB Board met and approved a motion that required the IFO to evaluate the effectiveness of the first five-year review cycle.

The IFO surveyed agencies that administer tax credits reviewed by the IFO and met with legislative staff to obtain feedback related to the tax credit reviews. This memo is a summary of those findings and is submitted in response to the April 24, 2023 PBB Board motion. The three sections that follow discuss the Methodology, Summary Findings and Recommendations based on those surveys/discussions.

Year	Initial Tax Credit Review Schedule				
1	Film Production	New Jobs	Historic Preservation Incentive		
2	Research and Development	Keystone Innovation Zones	Mobile Telecom and Broadband	Organ and Bone Marrow	
3	Neighborhood Assistance	Resource Enhancement and Protection (REAP)	Entertainment Economic Enhancement Program	Video Game Production	Keystone Special Development Zones
4	Educational Tax Credits	Coal Refuse and Reclamation	Mixed Use Development	Brewers'	
5	Resource Manufacturing	Manufacturing and Investment	Waterfront Development	Rural Jobs and Investment	

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Methodology

In August 2023, a survey was distributed to seven agencies that administer a tax credit reviewed by the IFO during the first five-year cycle. The survey was agency specific and included the following seven questions for each tax credit:

- Did your agency implement any of the report recommendations? If yes, please indicate which recommendations.
- Did your agency implement any of the recommended performance metrics? If yes, please indicate which metrics.
- How were the metrics used?
- How did use of the metrics impact programmatic outcomes?
- If the metrics were not used, why not?
- Did the referenced tax credit review inform budget or policy decision-making related to the tax credit? If yes, in what way? Please be specific.
- What performance data (if any) would you want to use to evaluate program effectiveness, but do not currently have access to? If there are data that you wish you had, what are the impediments to collecting such data?

In addition, the IFO requested that each agency provide any general recommendations or feedback on ways that the tax credit review process could be improved moving forward.

In September 2023, the IFO met with House and Senate Appropriations Committee staff to discuss:

- Whether the General Assembly used the tax credit reviews to inform budget and policy decision-making, and if so, any specific examples of such use.
- Whether the General Assembly has any recommendations to improve the tax credit review process.

The next section provides a summary of agency and legislative responses.

Summary Findings

During the first five-year cycle, the IFO reviewed 20 tax credits, which resulted in recommendations for 85 programmatic changes and the collection of 29 new performance metrics.[1] Of the 85 recommendations included in the reports, roughly 70% likely require legislative action for implementation. Despite this, 16 of the IFO's recommendations (19%) were implemented and 7 of the suggested performance metrics (24%) are now tracked. (See table on page 5.) In accordance with IFO recommendations from the reports, one tax credit was repealed (New Jobs Tax Credit) and one tax credit was reprogrammed as a grant (Mobile Telecommunications Broadband Investment Tax Credit).

[1] The IFO recommended the repeal or reprogramming of funds for the New Jobs Tax Credit (NJTC) and the Mobile Telecommunications Broadband Investment Tax Credit (MTBI). The NJTC was repealed and the MTBI Tax Credit was reprogrammed, making the other five recommendations related to those programs and all 12 recommended performance metrics obsolete. The 12 recommended performance metrics are excluded from the total (29).

General Assembly Response

Since the first tax credit review was issued, the General Assembly has enacted changes consistent with 13 recommendations from the IFO's tax credit reports. These changes include:

- Provided for a $1,000 Historic Preservation Tax Credit (HPTC) application fee that is used to offset program costs. (Act 13-2019)
- Enacted statutory HPTC application and award deadlines. (Act 13-2019)
- Increased HPTC program cap from $3 million to $5 million annually. (Act 13-2019)
- Repealed the New Jobs Tax Credit. (Act 13-2019)
- Repealed the Mobile Telecommunications Broadband Investment Tax Credit and replaced it with a competitive grant program. (Act 132-2020)
- Moved the Research and Development (R&D) Tax Credit application deadline from September 15 to December 1 and the notification deadline from December 15 to May 1 to (1) facilitate the taxpayer's ability to include supporting documents with the tax credit application and (2) allow a more thorough evaluation of submitted applications. (Act 25-2021)
- Enacted statutory changes to deter fraudulent activity related to the R&D Tax Credit. (Act 25-2021)
- Enacted statutory reforms to facilitate enforcement of the R&D Tax Credit. (Act 25-2021)
- Moved the Keystone Innovation Zone (KIZ) Tax Credit application deadline from September 15 to December 1 and the notification deadline from December 15 to May 1 to (1) facilitate the taxpayer's ability to include supporting documents with the tax credit application and (2) allow a more thorough evaluation of submitted applications. (Act 25-2021)
- Enacted statutory changes to deter fraudulent activity related to the KIZ Tax Credit. (Act 25 -2021)
- Reduced the share of Educational Tax Credits (ETC) that may be retained for non-program purposes from 20% to 10%. (Act 33-2023)
- Provided for the collection of certain ETC performance data. (Act 33-2023)
- Required the Department of Community and Economic Development to publish specified ETC data in spreadsheet form on their website. (Act 33-2023)

Legislative Staff Response

Feedback from legislative staff varied across the legislative caucuses and tax credits, but staff generally reported that they found the tax credit reviews useful. Staff found it particularly helpful to have data on the tax credits readily available (e.g., number of claimants and who benefits) and noted that several reviews resulted in legislative changes. Feedback also indicated that data limitations (i.e., some credits do not require submission of relevant metrics) limit the overall usefulness of the reviews because it precludes comparisons of outcome metrics across tax credits. The consensus was that the tax credit reviews should move forward in some manner, but there were no consistent recommendations regarding how that should proceed.

Agency Responses

Agency responses regarding the usefulness of the tax credit reviews and the impact on outcomes and decision-making were limited and also varied across tax credits and agencies. Most agencies generally found the focus on efficiency/outcomes and the identification of key performance metrics helpful. In a few cases, the reviews resulted in the implementation of changes that improved program efficiency.

No recommendations to improve the tax credit review process were received from any agency that administers tax credits.

Tax Credit Recommendations and Performance Metrics Summary

	# Recommendations		# New Performance Metrics	
Tax Credit	Established	Implemented	Established	Tracked
Brewers'	3	0	--	--
Coal Refuse Energy and Reclamation	5	0	--	--
Educational	7	3	6	0
Entertainment Economic Enhancement Program	3	0	--	--
Film Production	6	1	--	--
Historic Preservation	8	3	8	0
Keystone Innovation Zone	7	2	5	3
Keystone Special Development Zones	4	0	--	--
Manufacturing	3	1	7	3
Mixed-Use Development	3	1	--	--
Mobile Telecom. Broadband Investment [1]	3	1	**	**
Neighborhood Assistance Program	4	0	--	--
New Jobs[2]	4	1	**	**
Organ and Bone Marrow Donation	3	0	--	--
Research and Development	7	3	--	--
Resource Enhancement and Protection Program	3	0	1	1
Resource Manufacturing	3	0	1	0
Rural Jobs and Investment	2	0	--	--
Video Game Production	4	0	--	--
Waterfront Development	3	0	1	0
Total	**85**	**16**	**29**	**7**

Note: Roughly 70% of the IFO's tax credit recommendations would likely require legislative action to implement.

1 The tax credit was repealed and replaced with a grant program in accordance with report recommendations. The recommended performance metrics (3) are excluded from this table as they are no longer applicable.

2 The tax credit was repealed in accordance with report recommendations. The recommended performance metrics (9) are excluded from this table as they are no longer applicable.

Sources: DCED, DCNR, DEP, DOR, PHFA, PHMC and the SCC.

Recommendations

If the PBB Board determines that tax credit reviews should resume, then the IFO provides the following two options for the review process:

Option 1: Review most tax credits in five-year cycles and omit the smallest tax credits. Under this option, the PBB Board and the IFO would determine a five-year schedule to review most tax credits, but omit small credits (e.g., tax credits below $20 million). (Note that a new schedule could be developed every five years.) New reports for tax credits that have already been reviewed by the IFO would be considered updates and omit certain material that was included in the original report (e.g., the application process).

Option 2: Focus on six to eight tax credits that would be reviewed every two years. Under this option, the PBB Board and the IFO would select six to eight tax credits for review and half of the selected tax credits would be analyzed each year. New reports for tax credits that have already been reviewed would be considered updates (with certain material omitted), and the PBB Board could modify the schedule as needed.