

ENTERPRISE ZONES TAX EXPENDITURES



JANUARY 2020
2020-TE9

EVALUATION SUMMARY

THIS EVALUATION WILL BE INCLUDED IN COMPILATION REPORT SEPTEMBER 2020

	YEAR ENACTED	REPEAL/ EXPIRATION DATE	REVENUE IMPACT	NUMBER OF TAXPAYER CLAIMS	AVERAGE CLAIM AMOUNT	IS IT MEETING ITS PURPOSE?
INVESTMENT TAX CREDIT	1986	None	\$16,397,000	3,201	\$5,122	Yes, to a limited extent
NEW EMPLOYEE CREDIT	1986		\$3,583,000	815	\$4,396	
QUALIFIED JOB TRAINING PROGRAM CREDIT	1996		\$1,598,000	478	\$3,343	
MANUFACTURING MACHINERY SALES TAX EXEMPTION	1986		\$370,000	Could not determine	Could not determine	
RESEARCH AND EXPERIMENTAL ACTIVITIES CREDIT	1988		\$643,000	249	\$2,582	
EMPLOYEE HEALTH INSURANCE CREDIT	1987		\$504,000	122	\$4,131	
VACANT COMMERCIAL BUILDING REHABILITATION CREDIT	1989		\$268,000	107	\$2,505	
AGRICULTURAL PROCESSING EMPLOYEE CREDIT	1987		\$91,000	33	\$2,758	
COMMERCIAL VEHICLE INVESTMENT TAX CREDIT	2009		\$21,000	15	\$1,400	
TOTALS FOR ALL ENTERPRISE ZONE TAX EXPENDITURES			\$23,475,000	5,020	\$4,676	

WHAT DO THESE TAX EXPENDITURES DO?

The Enterprise Zones Tax Expenditures, established under the Urban and Rural Enterprise Zone Act [Title 39, Article 30, C.R.S.], provide tax credits and a sales tax exemption for businesses within economically distressed areas of the state, known as “enterprise zones.” To receive the tax expenditures, businesses must make investments, hire employees, make eligible purchases, and/or provide health insurance coverage or training to employees within enterprise zones.

WHAT IS THE PURPOSE OF THESE TAX EXPENDITURES?

The legislative declaration for the Urban and Rural Enterprise Zone Act indicates that when it established the Enterprise Zone Tax Expenditures, the General Assembly was primarily concerned with expanding available job opportunities within enterprise zones and that the policy of the State is “to provide incentives for private enterprise to expand and for new businesses to locate in [enterprise zones] and to provide more job opportunities for residents of such areas.”

WHAT DID THE EVALUATION FIND?

Overall, we found that the Enterprise Zones Tax Expenditures are meeting their purpose, but to a limited extent. Although we found that businesses that claimed these tax expenditures reported making substantial investments and hiring a significant number of employees within enterprise zones, it appears that much of this business activity would have likely occurred regardless of the tax expenditures. Further, although we found that these tax expenditures have likely had a positive impact on the State's economy, our analysis of several economic indicators showed no measurable difference in the performance of enterprise zones compared to similar areas outside of enterprise zones.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

The General Assembly may want to consider:

- Whether the Enterprise Zone Tax Expenditures are meeting their intended purpose.
- Establishing performance measures to clarify its intent for evaluating their effectiveness.
- Amending statute to better target the Enterprise Zone Tax Expenditures and improve their effectiveness.
- Clarifying the carryforward periods for the New Employee credit.

ENTERPRISE ZONE TAX EXPENDITURES

EVALUATION RESULTS

WHAT ARE THESE TAX EXPENDITURES?

In 1986, the General Assembly passed the Urban and Rural Enterprise Zone Act [Title 39, Article 30, C.R.S.], creating two income tax credits and one sales and use tax exemption to provide incentives for businesses to locate and expand their operations in Colorado. The ultimate goal of the Act was to boost employment in economically distressed parts of the state, known as “enterprise zones.” Legislation passed since then has generally increased the number of credits available to provide additional incentives to encourage businesses to locate and expand operations within enterprise zones and provide health insurance and training to their employees. Three additional enterprise zone tax expenditures, which were established from 1992 through 1999—an Aircraft Maintenance Machinery Sales Tax Exemption, a School-to-Work Program Credit, and a Rural Technology Credit—had all expired by 2004. EXHIBIT 1.1 provides information on each of the nine tax expenditures that are included in this review.

EXHIBIT 1.1. DESCRIPTION OF ENTERPRISE ZONE EXPENDITURES COVERED IN EVALUATION

TAX EXPENDITURE	STATUTORY REFERENCE	YEAR CREATED	SUMMARY	CARRY-FORWARD PERIOD
Enterprise Zone Investment Tax Credit	Section 39-30-104(1)(a), C.R.S.	1986	Provides an income tax credit ¹ of 3 percent of the value of qualifying investments in an enterprise zone. The credit is generally capped at the lesser of \$750,000, or \$5,000 plus 50 percent of the taxpayer’s tax liability in excess of \$5,000. Eligible investments typically include depreciable tangible personal property such as machinery, livestock, furniture, appliances, and vehicles, and certain types of real property (excluding buildings) used in manufacturing, extraction, transportation, and energy.	14 years

EXHIBIT 1.1. DESCRIPTION OF ENTERPRISE ZONE EXPENDITURES COVERED IN EVALUATION				
TAX EXPENDITURE	STATUTORY REFERENCE	YEAR CREATED	SUMMARY	CARRY-FORWARD PERIOD
Enterprise Zone New Employee Credit	Section 39-30-105.1(1)(a)(I) & (II), C.R.S.	1986	Provides a \$1,100 income tax credit ¹ per new employee of new business facilities or certain types of replacement business facilities located in an enterprise zone if taxpayer employs more employees in the current year than in the previous year. If a business is in an enhanced rural enterprise zone ² the credit amount increases to \$3,100 for each new employee.	5 years (7 years if within an enhanced rural enterprise zone)
Enterprise Zone Manufacturing Machinery Sales Tax Exemption	Section 39-30-106, C.R.S.	1986	Exempts from sales and use tax machinery, machine tools/parts, and materials used for the construction and repair of machinery and machine tools/parts valued in excess of \$500 that are used exclusively for manufacturing tangible personal property in an enterprise zone, including property used in mining and other types of natural resource extraction and processing. Capped at \$150,000 per year for used machinery, parts, and materials.	Not applicable
Enterprise Zone Agricultural Processing Employee Credit	Section 39-30-105.1(3)(a) & (b), C.R.S.	1987	Increases the amounts available under the Enterprise Zone New Employee Credit. Provides an additional \$500 income tax credit ¹ per employee if taxpayer operates a business in an enterprise zone that adds value through manufacturing or processing agricultural commodities. If a business is in an enhanced rural enterprise zone ² , the credit amount increases to \$1,000 per employee.	5 years (7 years if within an enhanced rural enterprise zone)
Enterprise Zone Employee Health Insurance Credit	Section 39-30-105.1(1)(b), C.R.S.	1987	Provides a \$1,000 income tax credit ¹ per employee that taxpayer's business covers under a health insurance plan, as long as the business covers at least 50 percent of the total cost. The credit is available for the first 2 years that the business is located in an enterprise zone.	5 years
Enterprise Zone Research and Experimental Tax Credit	Section 39-30-105.5, C.R.S.	1988	Provides an income tax credit ¹ of 3 percent of the amount spent on qualifying research and experimental activities within an enterprise zone above the average total amount that the taxpayer spent on research and experimental activities in the prior 2 years. Taxpayer can only claim up to 25 percent of the credit amount each year.	Indefinite
Enterprise Zone Vacant Commercial Building Rehabilitation Tax Credit	Section 39-30-105.6, C.R.S.	1989	Provides an income tax credit ¹ for owners or tenants of a building located in an enterprise zone who make qualified expenditures to rehabilitate the building, if the building is at least 20 years old and has been unoccupied for at least 2 years. The credit amount is the lesser of 25 percent of the qualified expenditures or \$50,000. The credit cannot be taken if the federal rehabilitation tax credit is taken for the same building.	5 years

EXHIBIT 1.1. DESCRIPTION OF ENTERPRISE ZONE EXPENDITURES COVERED IN EVALUATION

TAX EXPENDITURE	STATUTORY REFERENCE	YEAR CREATED	SUMMARY	CARRY-FORWARD PERIOD
Enterprise Zone Qualified Job Training Program Investment Tax Credit	Section 39-30-104(4)(a)(II), C.R.S.	1996	Provides an income tax credit ¹ equal to 12 percent of the total investment made in a qualified job training program for employees working predominantly within an enterprise zone. The training program itself is not required to occur within the enterprise zone.	12 years
Enterprise Zone Commercial Vehicle Investment Tax Credit	Section 39-30-104(1)(b), C.R.S.	2009	Provides an income tax credit ¹ equal to 1.5 percent of investments in a qualified property, which includes commercial trucks, truck tractors, tractors, or semitrailers with a weight of 54,000 lbs., or more, or any parts purchased at the same time for such vehicles, when the vehicle is predominantly housed and based at a taxpayer's trucking facility in an enterprise zone for at least 12 months following the purchase of the property.	12 years

SOURCE: Office of the State Auditor analysis of Colorado Revised Statutes and Department of Revenue regulations and guidance documents.

¹ Section 39-30-107.6, C.R.S., allows insurance companies, which are not subject to state income tax, to claim an equivalent reduction in their insurance premium tax.

² Enhanced rural enterprise zones are rural areas of the state that are particularly economically distressed based on criteria established by Section 39-30-103.2(1), C.R.S.

We evaluated these tax expenditures as a group because they are structured to work together to improve economic conditions within enterprise zones, with taxpayers generally able to claim multiple credits for a single qualifying business activity. For example, a business building a new manufacturing plant could qualify for the Enterprise Zone Investment Tax Credit for its capital investment in qualifying equipment and also the Enterprise Zone New Employee Credit, based on the number of new employees hired to work at the plant. Although we have provided separate analyses for these credits in some areas, we focused our review on their cumulative impact and effectiveness at meeting the overall purpose of the Urban and Rural Enterprise Zone Act.

In addition to the tax expenditures provided above, eligible taxpayers may claim the Enterprise Zone Renewable Energy Investment Credit [Section 39-30-104(2.6), C.R.S.] and the Enterprise Zone Contribution Credit [Section 39-30-103.5, C.R.S.], which are also intended to benefit the economies of enterprise zones. We have not included these expenditures in this evaluation report because, although these credits

have a similar purpose to the other nine expenditures included in this evaluation, they have substantial differences in their structure and requirements that we determined warranted separate evaluations. We evaluated the Enterprise Zone Renewable Energy Investment Credit in a report issued contemporaneously to this report, though as noted in this report, it is included in some of the data we used to evaluate the Investment Tax Credit, since its function is to make the Investment Tax Credit refundable for qualifying renewable energy investments. The Enterprise Zone Contribution Credit will be evaluated separately.

ENTERPRISE ZONE DESIGNATION AND ADMINISTRATION

According to Section 39-30-103, C.R.S., for an area to be designated as an enterprise zone, a municipality, county, or contiguous group of municipalities or counties must submit an economic development plan to the Office of Economic Development and International Trade (OEDIT). The proposed enterprise zone must have a population of 115,000 or less if it is an urban area or population of 150,000 or less if it is composed of rural areas. Rural areas are defined as those counties or municipalities that have a population under 50,000 and unincorporated areas of other counties that are at least 10 miles from a municipality with a population of 50,000. In addition, the area must meet at least one of the following criteria:

- An unemployment rate at least 25 percent above the state average for the most recent period of 12 consecutive months.
- A population growth rate of less than 25 percent of the state average for the most recent 5-year period.
- A per capita income of less than 75 percent of the state average.

The economic development plan submitted by the local government(s) must include the following information:

- The zone boundaries, which can include multiple counties and municipalities and/or partial sections of such areas.

- The zone's potential for business development and job creation.
- How the zone will support the maintenance of an economically viable central business district.
- The specific economic development objectives of the zone, including measurable outcomes.
- The person or agency to be designated as the administrator of the proposed zone. Zone administrators promote the program in their zone, assist businesses with applying for the Enterprise Zone Tax Expenditures, and approve eligible businesses (both before and after they have completed the qualifying business activity).

OEDIT staff are responsible for reviewing the economic development plan to ensure that the area meets statutory requirements and then forwarding it to the Colorado Economic Development Commission (Commission) within OEDIT, which is responsible for overseeing the Enterprise Zone. The Commission must approve the boundaries for the area to be designated as an enterprise zone and it is limited to approving a total of 16 enterprise zones in the state.

Furthermore, OEDIT staff are responsible for designating certain counties included within approved enterprise zones as enhanced rural enterprise zones, in which businesses may receive additional credit amounts. According to Section 39-30-103.2, C.R.S., OEDIT must designate a county within an enterprise zone as an enhanced rural enterprise zone if it meets at least two of the following five criteria:

- 1 County unemployment rate of more than 150 percent of the state average over the most recent year for which data is available.
- 2 County per capita income of less than 75 percent of the state average for the most recent period for which data is available.
- 3 County population growth rate of less than 25 percent of the state average for the most recent five-year period for which data is available.

- 4 Total non-residential property assessed value that ranks in the lower half of all counties in the state.
- 5 County population of 5,000 or less.

Once an enterprise zone is established, statute [Section 39-30-103(4)(b), C.R.S.] requires that the zone's administrator submit annual documentation to OEDIT on the economic conditions in the enterprise zone and the results of efforts to improve economic conditions, including whether the zone has met its economic development objectives according to measurable outcomes. OEDIT must summarize this information in an annual report to the General Assembly.

Beginning in 2014, Section 39-30-103(2)(c)(I), C.R.S., requires OEDIT and the Commission to review enterprise zone boundaries at least once every 10 years to ensure that they continue to meet the requirements for inclusion in an enterprise zone, and the boundaries of enhanced enterprise zones every 2 years. However, OEDIT and the Commission work with zone administrators, local governments, and public stakeholders on an annual basis to modify zone boundaries, based on local economic conditions and development objectives, with the Commission setting the final boundaries.

Currently, there are 16 enterprise zones in the state, with the most recent major boundary changes taking effect in 2016. About 84 percent of the State, by area, 26 percent of the State's population, and 39 percent of the State's jobs, are within one of the 16 enterprise zones. Of Colorado's 64 counties, 32 (50 percent) have been designated as enhanced rural enterprise zones. EXHIBIT 1.2 shows the areas of the state designated as enterprise zones and enhanced rural enterprise zones. Enterprise zone boundaries are not required to be contiguous, and as shown, some enterprise zones, in particular those in urban areas such as the Denver metro area, Colorado Springs, and Pueblo, have boundaries that tend to cover a patchwork of areas within the local governments participating.

EXHIBIT 1.2. MAP OF COLORADO'S ENTERPRISE ZONES



APPLYING FOR AND CLAIMING ENTERPRISE ZONE TAX EXPENDITURES

To claim the Enterprise Zone Tax Expenditures, with the exception of the Enterprise Zone Manufacturing and Machinery Sales Tax Exemption, taxpayers must first apply to their local zone administrator for “precertification” before they conduct the planned business activity that would qualify for a credit (e.g., hiring new employees, making investments). As part of the precertification process, taxpayers must attest that they are aware of the credits and that the credits are a “contributing factor to the start-up, expansion, or relocation of [their] business in the enterprise zone.” Once a business has been precertified and has completed

the associated business activity, it can apply to the zone administrator for certification. Once approved and certified, OEDIT provides the Department of Revenue with a list of taxpayers who have been approved for one or more enterprise zone credits, including how much the recipient has been certified to claim, and the taxpayer is issued a certificate showing the amount certified. Taxpayers must include the certificate with their tax returns.

Taxpayers claim the Enterprise Zone Tax Expenditures by completing the Enterprise Zone Credit and Carryforward Schedule (Form DR 1366) and filing that form with their Colorado income tax returns, where they also report the credit amount claimed. Pass-through entities, such as partnerships and S-corporations, must also file the DR 1366, which calculates the credit available for its partners or shareholders. The partners or shareholders must then complete and file a separate DR 1366 with their respective income tax returns to claim the credits. Insurers can also claim these expenditures; however, since insurers are exempt from state income tax and instead pay an insurance premium tax, they receive equivalent reductions when they file their Insurance Premium Tax Return with the Division of Insurance.

For the Enterprise Zone Manufacturing Machinery Sales Tax Exemption, the exemption is generally applied by the vendor at the time of sale and the vendor is responsible for reporting the amount of exempt sales on the Department of Revenue's Retail Sales Tax Return Form (Form DR 0100) in the "Exemptions Schedule-Part B" section, on Line 2 for "Machinery." Buyers of eligible items must list the items, their price, how they are used in manufacturing, and what product will be created using the items, then certify that they are eligible for the exemption on the Department of Revenue's Sales Tax Exemption on Purchases of Machinery and Machine Tools Form (Form DR 1191) prior to making the purchase. They must provide copies of this form to the vendor and the Department of Revenue. The exemption also applies to use tax, with out-of-state vendors and Colorado purchasers required to report the amount of exempt sales on the Department of Revenue's

Retailer's Use Tax Return Form (Form DR 0173) or the Consumer Use Tax Return Form (Form DR 0252), respectively.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURES?

Based on Section 39-30-102(2), C.R.S., the intended direct beneficiaries of the Enterprise Zone Tax Expenditures are new and existing businesses locating and/or expanding in economically depressed areas of the state. Based on our analysis of OEDIT data, these tax expenditures are widely used, with about 3,100 unique businesses at 4,600 business locations certified in Fiscal Year 2018, which was about 7 percent of the overall business establishments in enterprise zones and 2 percent of the business establishments statewide. EXHIBIT 1.3 shows the number and amount of enterprise zone credits certified, by industry sector, during Fiscal Year 2018.

EXHIBIT 1.3. NUMBER OF BUSINESSES AND AMOUNT OF ENTERPRISE ZONE CREDITS CERTIFIED, BY INDUSTRY SECTOR, FISCAL YEAR 2018¹

INDUSTRY	NUMBER OF BUSINESSES CERTIFIED	PERCENTAGE OF TOTAL BUSINESSES CERTIFIED	AMOUNT OF CREDITS CERTIFIED (MILLIONS)	PERCENTAGE OF TOTAL CREDITS CERTIFIED
Agriculture, Forestry, Fishing and Hunting	1,581	50%	\$5.2	10%
Manufacturing	235	8%	\$13.2	24%
Construction	225	7%	\$1.2	2%
Retail Trade	215	7%	\$4.1	8%
Professional, Scientific, and Technical Services	149	5%	\$0.9	2%
Health Care and Social Assistance	80	3%	\$2.4	5%
Transportation and Warehousing	59	2%	\$6.2	11%
Mining, Quarrying, and Oil and Gas Extraction	34	1%	\$6.1	11%
Utilities	11	<1%	\$6.6	12%
Other ²	512	17%	\$8.2	15%
TOTAL	3,101	100%	\$54.1	100%

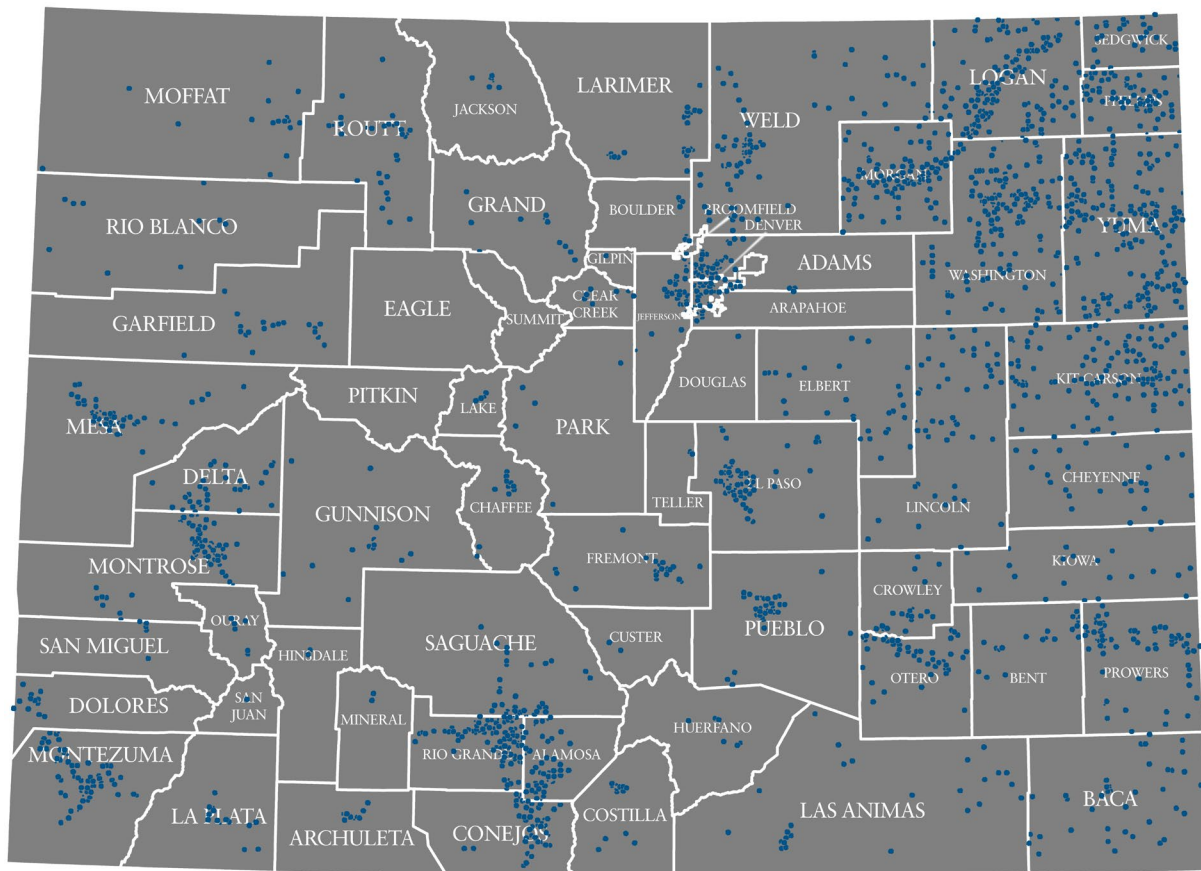
SOURCE: Office of the State Auditor analysis of OEDIT data.

¹ Includes totals for the Enterprise Zone Renewable Energy Credit, which are included within data for the Investment Tax Credit.

² Includes the following sectors, which each comprise less than 5 percent of the total businesses certified and total credits certified: wholesale trade; information; finance and insurance; real estate, rental, and leasing; management of companies and enterprises; administrative and support; waste management and remediation services; educational services; arts entertainment, and recreation; accommodation and food services; and other services.

The beneficiaries of enterprise zones are widely distributed across the state, with beneficiaries primarily clustered around urban areas, major highways, and the northeastern portion of the state where there is a concentration of agricultural and oil and gas businesses. EXHIBIT 1.4 shows the locations of taxpayers who were certified for an enterprise zone credit during Fiscal Year 2018.

EXHIBIT 1.4. LOCATION OF ENTERPRISE ZONE CERTIFICATIONS FISCAL YEAR 2018



SOURCE: Office of the State Auditor analysis of OEDIT Enterprise Zone Certification data.

EXHIBIT 1.5 provides the percentage of credit amounts certified within each enterprise zone for Fiscal Year 2018. As shown, certified credit amounts are also widely distributed, with higher concentrations within the Weld County, Adams County, and Northeast-Central enterprise zones.

EXHIBIT 1.5. PERCENTAGE OF ENTERPRISE ZONE CREDITS CERTIFIED BY ENTERPRISE ZONE FISCAL YEAR 2018	
ENTERPRISE ZONE	PERCENTAGE OF TOTAL CERTIFICATION AMOUNTS
Weld County	19%
Adams County	15%
Northeast-Central	10%
Denver	10%
Southeast-Central	8%
Pikes Peak	6%
Central & Southern	6%
Pueblo	6%
Jefferson County	4%
Mesa County	4%
Northwest	4%
Larimer County	2%
Region 10	2%
South Metro	2%
North Metro	1%
Southwest	1%
SOURCE: Office of the State Auditor analysis of OEDIT data.	

We inferred that the indirect beneficiaries of the Enterprise Zone Tax Expenditures are employees who are hired by participating businesses and residents of enterprise zones, to the extent that these expenditures improve local economic conditions. Businesses certified for one or more enterprise zone credits in Fiscal Year 2018 reported employing a total of about 117,000 employees across the state, which is about 10 percent of the jobs within Colorado’s enterprise zones, and 4 percent of total jobs in Colorado in 2018.

WHAT IS THE PURPOSE OF THESE TAX EXPENDITURES?

The legislative declaration for the Urban and Rural Enterprise Zone Act [Section 39-30-102, C.R.S.] indicates that when it established the Enterprise Zone Tax Expenditures, the General Assembly was primarily concerned with expanding available job opportunities within enterprise zones and that the policy of the State is “to provide incentives for private enterprise to expand and for new businesses to locate in [enterprise zones] and to provide more job opportunities for residents of such areas.”

ARE THE TAX EXPENDITURES MEETING THEIR PURPOSE
AND WHAT PERFORMANCE MEASURES WERE USED TO
MAKE THIS DETERMINATION?

We determined that the nine Enterprise Zone Tax Expenditures covered in this evaluation are likely meeting their purpose, but only to a limited extent. Specifically, these expenditures have likely provided a small incentive for businesses to invest, hire, and conduct related business activities in enterprise zones and participating businesses have made substantial investments and hired a significant number of employees in the state. However, it appears that much of the investment and hiring would have occurred even in the absence of these tax expenditures and our review of economic data found no evidence that they have had a measurable impact on the employment rate, per capita income, or population growth within enterprise zones as compared to non-enterprise zones.

Statute does not provide quantifiable performance measures for these tax expenditures. Therefore, we created and applied the following performance measures to determine the extent to which they are meeting their purpose:

PERFORMANCE MEASURE #1: *To what extent have the ENTERPRISE ZONE TAX EXPENDITURES caused businesses to make investments within enterprise zones?*

RESULT: We found that the Enterprise Zone Tax Expenditures likely provide a small incentive for businesses to make investments in enterprise zones, which can include capital investments related to maintaining, expanding, newly establishing, or relocating from outside the state a business within an enterprise zone. Although our review of OEDIT data indicates that the businesses claiming these tax expenditures have made a large amount of investments, our review of the available evidence indicates that it is likely that much of these investments would have occurred without the tax expenditures.

Based on OEDIT data, businesses certified to receive the Enterprise Zone Tax Expenditures because of qualifying investments reported making an average of about \$1.6 billion annually in qualifying investments during Fiscal Years 2014 through 2018. These investments are equivalent to about 3 percent of the \$56.1 billion in capital investment made by all businesses in the state during Calendar Year 2017, based on our analysis of the most recent available year of baseline economic data provided by IMPLAN, an economic modeling software. EXHIBIT 1.6 shows the total amount of investments associated with each of the five investment-related Enterprise Zone Tax Credits certified during Fiscal Year 2018. As shown, the Investment Tax Credit accounts for a large majority of the total investments.

EXHIBIT 1.6. INVESTMENT ASSOCIATED WITH CREDITS CERTIFIED FOR INVESTMENT-RELATED ENTERPRISE ZONE CREDITS ¹ FISCAL YEAR 2018 (MILLIONS)		
CREDIT	AMOUNT	PERCENTAGE OF TOTAL
Investment Tax Credit ²	\$1,423.0	96%
Research and Experimental Tax Credit	\$31.6	2%
Job Training Program Investment Tax Credit	\$20.1	1%
Commercial Vehicle Investment Tax Credit	\$11.6	<1%
Vacant Commercial Building Rehabilitation Tax Credit	\$1.7	<1%
TOTAL	\$1,488.0	100%
SOURCE: Office of the State Auditor analysis of OEDIT data.		
¹ The Enterprise Zone Manufacturing Machinery Sales Tax Exemption is not included to avoid duplicating the total amount invested. Although we estimate that taxpayers claimed about \$370,000 for the exemption, which would indicate about \$12.8 million in related purchases, most of this amount would also likely be eligible for the Investment Tax Credit and we lacked data necessary to avoid duplicating these totals.		
² Total includes the Renewable Energy Investment Tax Credit, which is combined with OEDIT data on the Investment Tax Credit.		

The business investments associated with enterprise zones appear to be distributed across both urban and rural areas of the state. EXHIBIT 1.7 shows the amount businesses reported investing within each county during Fiscal Year 2018.

A map of Colorado showing its 64 counties. The counties are labeled as follows:

- MOFFAT
- ROUTT
- JACKSON
- LARIMER
- WELD
- LOGAN
- SEDGWICK
- PHILLIPS
- RIO BLANCO
- GARFIELD
- GRAND
- BOULDER
- BROOMFIELD
- DENVER
- MORGAN
- WASHINGTON
- YUMA
- EAGLE
- GILPIN
- CLEAR CREEK
- ADAMS
- ARAPAHOE
- SUMMIT
- JEFFERSON
- DOUGLAS
- ELBERT
- KIT CARSON
- CHEYENNE
- PITKIN
- LAKE
- PARK
- TELLER
- EL PASO
- LINCOLN
- CHAFFEE
- FREMONT
- CROWLEY
- OTERO
- BENT
- PROWERS
- MESA
- DELTA
- GUNNISON
- SAGUACHE
- CUSTER
- PUEBLO
- BAK
- OURAY
- HINSDALE
- MINERAL
- RIO GRANDE
- ALAMOSA
- HUERFANO
- COSTILLA
- LAS ANIMAS
- SAN MIGUEL
- DOLOR
- MONTEZUMA
- LA PLATA
- ARCHULETA
- CONEJOS

Although the amount of capital investment associated with the enterprise zone tax expenditures is substantial, the amount of investment that was caused by them is likely much less because many of the businesses claiming the credits would likely have made the investments even in the absence of the credits. To assess the proportion of investments associated with the Enterprise Zone Tax Expenditures that would not have occurred in the absence of the credits, we reviewed the relative benefit of the tax expenditures compared to the cost of the investment, the types of businesses that received credits, interviewed zone administrators in each enterprise zone and other economic development stakeholders, and conducted a survey of taxpayers

certified for credits in Fiscal Year 2018. Based on this review, we found that most of the investments would have occurred regardless of the Enterprise Zone Tax Expenditures, though some stakeholders indicated that they can play a significant role in some businesses' decisions.

First, we found that the typical tax benefit provided by the enterprise zone credits is small in comparison with the investment amounts. Specifically, although about \$380 million in credits were certified for Tax Years 2012 through 2016, Department of Revenue data shows that only about \$128 million (34 percent) in credits were claimed during that period. Although taxpayers can carry forward most of the credits for use in future years, there is a consistent pattern of taxpayers not claiming the full value of credits, which indicates that a substantial portion of the credits issued each year will never be claimed or will be claimed in future years which reduces their tax benefit. For example, taxpayers were certified for \$54 million in credits associated with the \$1.5 billion in investments made for Fiscal Year 2018. If, consistent with recent program trends, only 34 percent of these credits are actually claimed, taxpayers will receive a tax savings of \$18.3 million or about 1 percent of the value of the investments.

Based on our review of economic research, tax incentives that provide a benefit that is small in comparison to businesses' costs, or that are delayed to future years, are less effective at incentivizing businesses' location and investment decisions. Instead, other factors, such as local labor market costs, proximity to necessary resources, infrastructure, and customer markets tend to drive businesses' decisions regarding the location of capital investments. Although tax incentives could be the deciding factor for some businesses, most economic studies we reviewed, which tended to focus on incentives in other states that are larger than Colorado's Enterprise Zone Tax Expenditures, indicates that only a small percentage of the investment decisions qualifying for tax incentives are driven by the incentives as opposed to other factors. In addition, one of the few economic studies of Colorado's enterprise zone program, a 2009 research paper by University of North Carolina, Charlotte economist Stephen Billings, found that enterprise zone tax expenditures have no

effect on where new establishments locate in Colorado, though the study did find that they have a positive impact on overall employment.

Second, it appears that many of the enterprise zone credits issued in Fiscal Years 2017 and 2018 were related to business activities that are already location dependent and likely to occur in geographic areas designated as enterprise zones. Location-dependent business activities are those that require operations to occur in distinct geographic regions due to resource or infrastructure requirements. This includes activities such as railroads, agriculture, and oil and natural gas development for which the location of the investment is more likely to be driven by businesses' needs, rather than tax incentives. We found that 2,321 (51 percent) of all businesses certified for enterprise zone credits in Fiscal Years 2017 and 2018, operate in industries that tend to be location-dependent, including the following: cell phone towers, railroads, agriculture, oil and gas production, oil and gas pipelines, airlines, mining and quarrying, and gas stations. These businesses accounted for about \$1.1 billion (37 percent) of all investments associated with the Enterprise Zone Tax Expenditures during Fiscal Years 2017 and 2018. In addition, 148 of the 3,100 businesses (5 percent) certified to claim one or more Enterprise Zone Tax Expenditures during Fiscal Year 2018 indicated that they relocated from another location or started a new business since 2017, which demonstrates that most investments associated with the credits were made by businesses already operating in the area. Therefore, although the tax expenditures may encourage businesses already established within enterprise zones to increase investments, their impact on business location decisions appears limited.

Though our review of OEDIT and Department of Revenue data indicates that the Enterprise Zone Tax Expenditures provide a relatively small incentive to make investments within enterprise zones, enterprise zone administrators indicated that they may have a significant impact. Specifically, all of the zone administrators stated that the Enterprise Zone Program provided a positive influence for generating new business activity in their respective areas, though most indicated that they function as "one of the tools in our toolbox" when it comes to incentivizing

economic development and may not be the deciding factor for businesses. In addition, our review of reports prepared by enterprise zone administrators indicates that enterprise zones may be used for more targeted purposes, such as revitalizing particular business districts or encouraging growth within particular industries that are not necessarily captured in the statewide investment data included in our analysis. However, several enterprise zone administrators told us that it is often businesses' accountants or tax preparers who have knowledge of these tax expenditures and make the decision to apply for them and not the business owners themselves, which suggests that the expenditures may not be driving the investment decisions of these business owners.

We also interviewed members of the Commission and other economic development stakeholders in the state, and they generally told us that Enterprise Zone Tax Expenditures reduced investment risk and encouraged the revitalization of economically distressed areas, particularly in smaller, rural areas which might not have the financial resources to provide other business incentives for prospective and existing businesses. Several also said that the expenditures play a significant role in some investments. However, these stakeholders, similar to zone administrators, indicated that the expenditures were one factor among many that businesses consider when deciding where to locate and if they should expand.

In addition, we surveyed a sample of businesses that were certified for at least one Enterprise Zone Tax Expenditure in Fiscal Year 2018 and received responses from 243 businesses. Of the respondents who answered the applicable questions, 74 percent said that the Enterprise Zone Tax Expenditures had a meaningful impact on their company's operations in Colorado. However, 49 percent indicated that the Enterprise Zone Tax Expenditures either had no impact or only a minor impact on their business location and investment decisions, with 23 percent saying they had a moderate impact, and only 11 percent saying that they were a significant influence or deciding factor. Furthermore, many businesses that provided additional comments to the survey indicated that although the Enterprise Zone Tax Expenditures are

helpful, they are one factor among many that the businesses consider in making investment decisions.

PERFORMANCE MEASURE #2: *To what extent have the ENTERPRISE ZONE TAX EXPENDITURES incentivized businesses to provide more job opportunities for residents of enterprise zones?*

RESULT: Overall, we found that the Enterprise Zone Tax Expenditures have likely provided a relatively modest increase in job opportunities for residents of enterprise zones. Although a significant number of jobs in enterprise zones are provided by businesses that have been certified for these tax expenditures, our review of the available evidence indicates that it is likely that many of these jobs would exist even in the absence of the expenditures and most went to employees who live outside of enterprise zones.

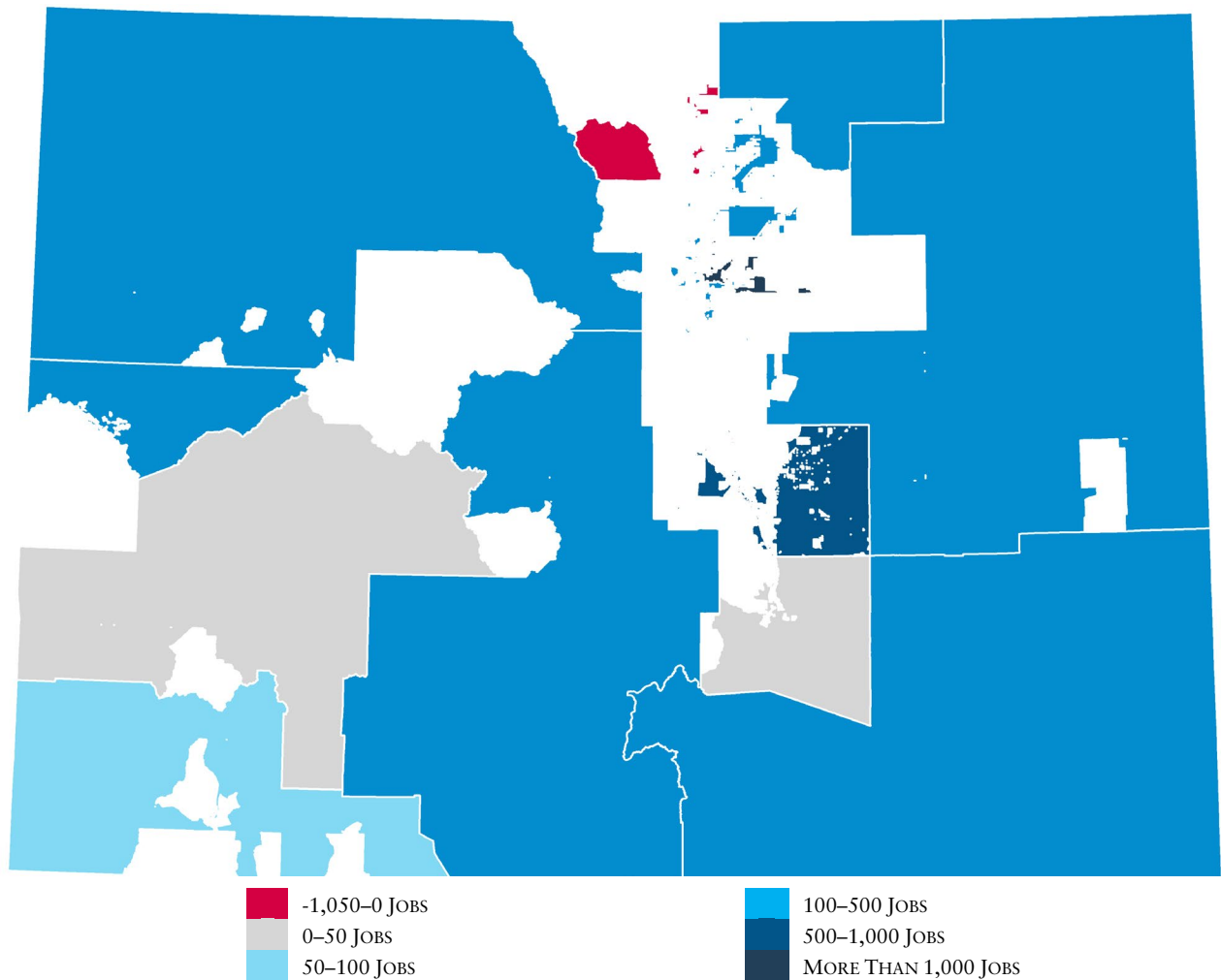
According to OEDIT data, businesses certified for one or more enterprise zone credits in Fiscal Year 2018 reported employing about 117,000 employees across the state, which comprises about 10 percent of the jobs in Colorado's enterprise zones and 4 percent of total jobs in Colorado during 2018. All participating businesses reported an average of 4,339 net new jobs (i.e., jobs created less jobs lost) in the state each year between Fiscal Years 2014 and 2018. EXHIBIT 1.8 provides the net new jobs reported by businesses certified for each of the Enterprise Zone Tax Expenditures in Fiscal Year 2018. Because businesses may claim several credits for the same activity, a substantial number of net new jobs are duplicated across the credit totals.

EXHIBIT 1.8. NET NEW JOBS REPORTED BY BUSINESSES CERTIFIED FOR ENTERPRISE ZONE CREDITS FISCAL YEAR 2018	
TAX EXPENDITURE ¹	NET NEW JOBS
New Employee Credit	4,767
Investment Tax Credit ²	3,799
Job Training Program Investment Tax Credit	1,709
Employee Health Insurance Credit	823
Research and Development Tax Credit	305
Agricultural Processing Employee Credit	301
Vacant Commercial Building Rehabilitation Tax Credit	57
SOURCE: Office of the State Auditor review of OEDIT data.	
¹ Does not include businesses exclusively claiming the Commercial Vehicle Investment Tax Credit, for which OEDIT did not have employment data available for Fiscal Year 2018, or businesses claiming the Manufacturing Machinery Sales Tax Exemption, for which taxpayers are not required to report job figures.	
² Includes the Renewable Energy Investment Tax Credit, which is included in OEDIT data for the Investment Tax Credit.	

Of those jobs that were reported by businesses certified for enterprise zone credits in Fiscal Year 2018, we found that they paid, on average, about \$44,000 annually, compared to the statewide average of about \$59,000. In addition, in Fiscal Year 2018, businesses qualifying for the Enterprise Zone Employee Health Insurance Credit reported providing jobs that included health insurance to about 1,200 employees and businesses qualifying for the Enterprise Zone Employee Training Credit reported providing qualified training programs to about 31,000 employees.

Although the businesses that reported new jobs associated with the Enterprise Zone Tax Expenditures are spread across all regions of the state, we found higher concentrations of reported net new jobs by businesses in and near urban areas of the state. EXHIBIT 1.9 provides the net new jobs reported by participating businesses in each enterprise zone during Fiscal Year 2018.

EXHIBIT 1.9. NET NEW JOBS REPORTED BY BUSINESSES CERTIFIED FOR
ENTERPRISE ZONE TAX EXPENDITURES
BY ENTERPRISE ZONE
FISCAL YEAR 2018



SOURCE: Office of the State Auditor review of OEDIT data.

As discussed, not all jobs associated with the Enterprise Zone Tax Expenditures can be attributed to the incentives provided by the Enterprise Zone Program, since many of the businesses may have made the same hiring decisions in the absence of these tax expenditures. Further, some of the new jobs likely went to employees who live outside enterprise zones and jobs reported by one business may be offset by losses of jobs at other competing businesses. Therefore, the net job gains reported by participating businesses do not necessarily represent an increase in total jobs available to residents of the enterprise zone. On the other hand, these tax expenditures may encourage businesses to

maintain employment within enterprise zones and support the viability of businesses within the zone, which could decrease the likelihood of job losses. However, businesses do not report information indicating the extent to which these effects have occurred and they are not included in the net jobs figures we report above.

Similar to our approach in PERFORMANCE MEASURE #1, we surveyed businesses that were certified for enterprise zone credits during Fiscal Year 2018, interviewed enterprise zone administrators, and reviewed the relative tax benefit provided by the credits to assess the proportion of jobs created due to the expenditures.

Our survey of businesses certified for the credits showed that of those businesses that were certified for job creation credits, 59 percent said that they would have created the same number of jobs without the Enterprise Zone Tax Expenditures and 41 percent said that they would have added fewer jobs without the Enterprise Zone Tax Expenditures or that they would not have created any new jobs if it were not for the Enterprise Zone Tax Expenditures. Similarly, most of the zone administrators we interviewed indicated that while the availability of Enterprise Zone Tax Expenditures can be a helpful incentive for attracting employers, they have a relatively small impact on hiring decisions. Furthermore, although the members of the Commission and other economic development stakeholders we interviewed generally told us that the tax expenditures reduced the cost of hiring, particularly for smaller businesses, they similarly indicated that the expenditures are one of many factors that influence hiring.

We also found that the tax credits available for hiring new employees are relatively small in comparison to the typical labor costs for businesses. For example, the annual average salary of employees hired by businesses that claimed credits was \$44,000, which indicates that including typical benefits equivalent to the national average reported by the Bureau of Labor Statistics, employers' total cost to hire each employee is about \$65,000 annually. In comparison, the New Employee Credit provides a \$1,100 credit for each qualifying new employee hired by a business, or about 2 percent of the typical annual costs, though this

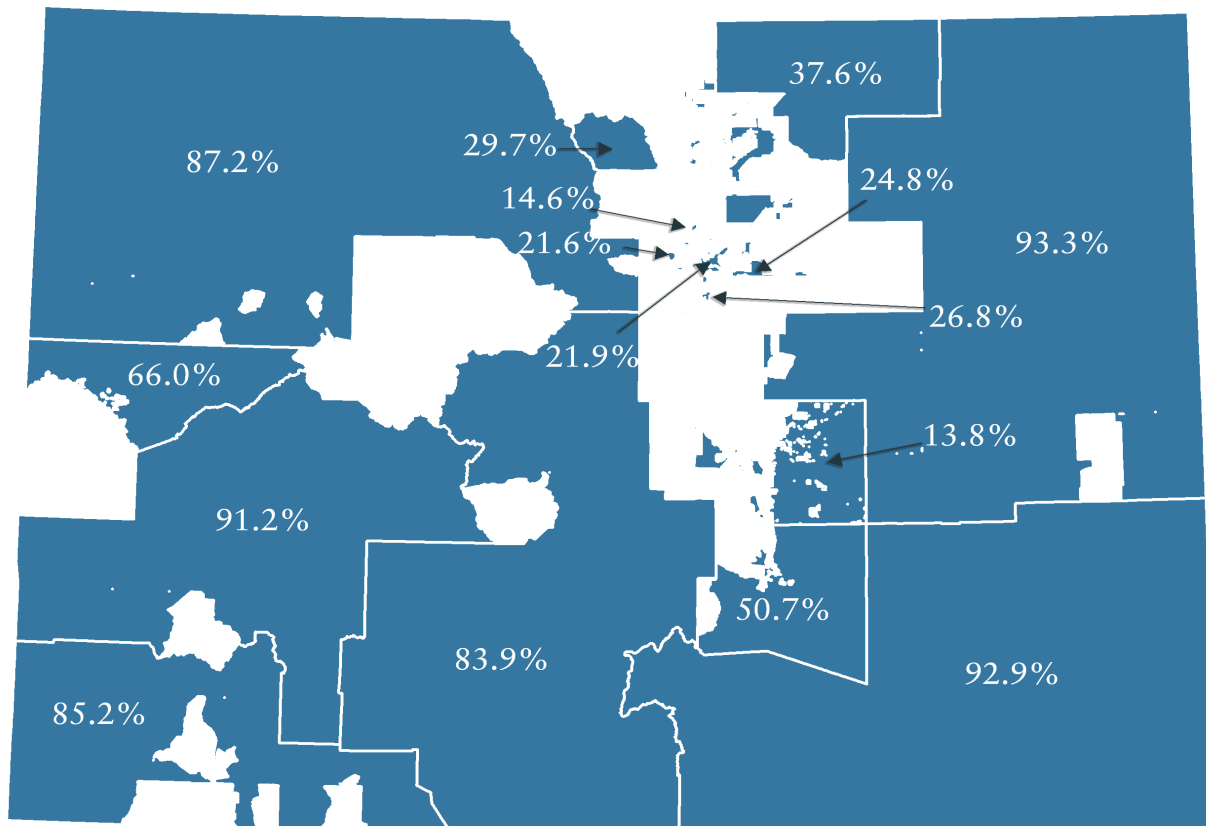
increases to \$3,100 (about 5 percent) in enhanced rural enterprise zones. While this benefit amount could influence some businesses' decision to hire additional employees within enterprise zones, economic studies on tax incentives similar to the Enterprise Zone Tax Expenditures indicate that while tax incentives can encourage businesses to create jobs within economically distressed areas, their effect is relatively small and they tend to be one factor among many that businesses consider when deciding the location and number of employees they hire. Specifically, other factors such as workforce education and availability, local wages, and the concentration of similar industries in the area can have a greater impact on businesses decisions.

In addition, we evaluated the likelihood that the jobs created by businesses certified to take the Enterprise Zone Tax Expenditures went to residents of enterprise zones. Because many of the net new jobs associated with these tax expenditures were created by businesses within urban enterprise zones, where zone boundaries tend to cover a patchwork of economically distressed areas within a larger urban core, it is likely that residents of areas not designated as enterprise zones received some of the new jobs. To the extent that this is the case, the Enterprise Zone Tax Expenditures will be less effective at reducing unemployment and increasing population within enterprise zones.

To assess this issue, we matched data from the Colorado Department of Labor and Employment, Department of Revenue, and OEDIT in order to map the home addresses of employees of businesses that claimed Enterprise Zone Tax Expenditures (other than the Enterprise Zone Manufacturing Machinery Sales Tax Exemption) for Fiscal Years 2016 through 2018, using geographic information software (GIS). We found that, statewide, 61 percent of employees hired by these businesses did not live within any enterprise zone. Further, enterprise zones in and near major urban areas of the state tended to have lower percentages of enterprise zone employees living within an enterprise zone. For example, in the enterprise zones near Denver and Colorado Springs we found that between 14 and 27 percent of employees of participating businesses lived within an enterprise zone. Due to inconsistencies

between data sources, we could not find matching employee records for about 22 percent of businesses and could not find matching addresses for about 11 percent of the employees for whom we obtained employment records. We excluded these businesses and employees from our analysis. In addition, to ensure consistent time periods for our analysis, we limited our analysis to businesses whose employee data corresponded to the tax year in which they planned to claim their credits. EXHIBIT 1.10 provides the percentage of employees of businesses within each enterprise zone that also reside in an enterprise zone.

EXHIBIT 1.10. PERCENTAGE OF PARTICIPATING BUSINESSES' EMPLOYEES WITH HOME ADDRESSES WITHIN ANY ENTERPRISE ZONE.



SOURCE: Office of the State Auditor analysis of OEDIT Enterprise Zone Certification data, Colorado Department of Labor and Employment employee data, and Department of Revenue taxpayer data using ArcMap GIS software.

In addition, as discussed, most of the Enterprise Zone Tax Expenditures are not limited to particular business types and they are used by a broad range of industries in the state. To assess the cost and job creation benefit provided by the Enterprise Zone Tax Expenditures within each industry sector, we compared the investment and net new jobs reported by

businesses within each industry sector that were certified for enterprise zone credits (we lacked data to include the Enterprise Zone Manufacturing Machinery Sales Tax Exemption in this analysis) to the total amount of credits they were certified to receive from Fiscal Year 2014 through 2018. EXHIBIT 1.11 summarizes the results of this analysis.

EXHIBIT 1.11. CREDIT AMOUNT CERTIFIED PER NET NEW JOB CREATED BY INDUSTRY FISCAL YEARS 2014 THROUGH 2018 ¹					
INDUSTRY SECTOR	VALUE OF CREDITS CERTIFIED (MILLIONS)	PERCENTAGE OF TOTAL CREDITS CERTIFIED	NET NEW JOBS	PERCENTAGE OF NET NEW JOBS	CREDITS CERTIFIED PER JOB REPORTED
Manufacturing	\$62.6	20%	5,254	24%	\$11,915
Transportation and Warehousing	\$49.3	16%	2,976	14%	\$16,566
Mining, Quarrying, and Oil and Gas Extraction	\$46.7	15%	720	3%	\$64,861
Utilities	\$38.6	12%	-29	>-1%	NA
Agriculture, Forestry, Fishing and Hunting	\$27.2	9%	466	2%	\$58,369
Information	\$15.6	5%	-470	-2%	NA
Retail Trade	\$14.9	5%	4,499	21%	\$3,312
Other ²	\$55.8	18%	8,278	38%	\$6,741
TOTAL	\$310.7	100%	21,694	100%	\$14,322

SOURCE: Office of the State Auditor review of OEDIT data.

¹ Figures include the Enterprise Zone Renewable Energy Credit, which is included within OEDIT data on the Investment Tax Credit.

² Includes the following industry sectors: construction, wholesale trade, finance and insurance, real estate and rental and leasing, professional, scientific and technical services, management of companies and enterprises, administrative support and waste management and remediation services, educational services, health care and social assistance, arts, entertainment and recreation, accommodation and food Services, other services and certifications that did not include an industry sector designation. Also includes a small number of businesses that did not indicate their industry sector.

As shown, businesses within some industry sectors, such as agriculture, forestry, fishing and hunting; utilities; mining, quarrying, oil, and gas extraction; and information, have created fewer jobs relative to the amount of credits certified, in some cases claiming credits for investments during the same year they reported reducing employment. Most of the credits certified for businesses in the sectors listed above were for the Enterprise Zone Investment Tax Credit, which does not

require any new jobs to be created in order to qualify and is based on capital investments within enterprise zones. Across all industry sectors in Fiscal Year 2018, we identified 637 of the 4,703 credit certifications (14 percent) for businesses that reported reducing jobs in the state. In total, these businesses were certified for about \$9.6 million in credits and reported decreasing employment by a total of 5,489 jobs. It is possible, however, that the businesses that did not report net job increases may have made investments that lead to job growth at other related businesses. For example, a business undertaking a large capital investment project may stimulate businesses that manufacture the equipment and supplies needed for the project, as well as construction and contract workers necessary to install it. Because businesses do not report these indirect job gains, we lacked data to assess the extent to which this effect has created jobs within enterprise zones or statewide.

Furthermore, we found that some businesses claiming the New Employee Credit and/or the Agricultural Processing Employee Credit, which are the two credits that require businesses to hire new employees in order to qualify, reported job gains at a specific location in order to qualify for the credits, but did not report any overall net job gains across all their business locations in the state. Specifically, in Fiscal Year 2018, of the 769 business locations certified for one or both of these credits, 131 of the business locations (17 percent) reported decreasing their employment numbers statewide during the year, and an additional 99 (13 percent) reported no net gain in jobs. These businesses were certified for \$2.4 million in credits in Fiscal Year 2018.

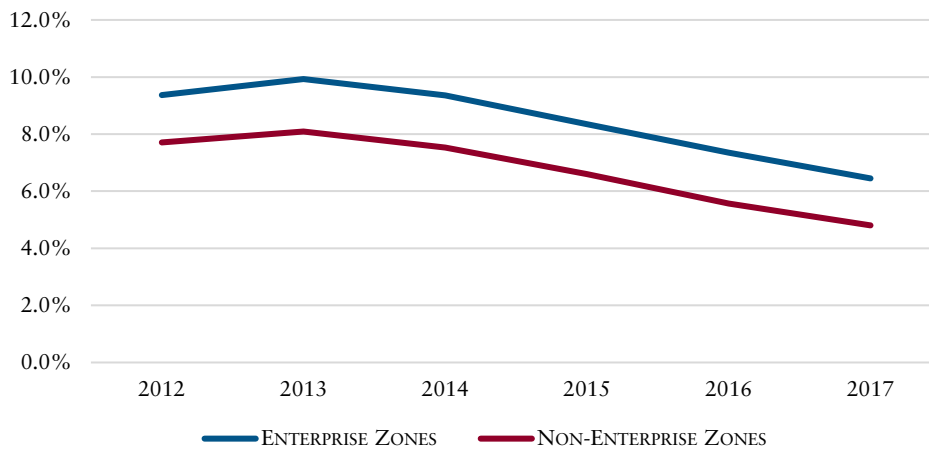
In addition, some sectors such as retail, accommodation and food services, and health care and social assistance reported relatively higher numbers of new jobs compared to the value of the credits certified. However, based on our review of academic research on tax incentives, incentives that target businesses that sell most of their goods and services locally, such as businesses in these sectors, tend to be less effective at increasing employment within an economically distressed area because they compete with other businesses in the same area, thereby causing corresponding job losses in other businesses.

PERFORMANCE MEASURE #3: *To what extent did the ENTERPRISE ZONE TAX EXPENDITURES have a measurable impact on improving the economic conditions within enterprise zones?*

RESULT: We found that the Enterprise Zone Tax Expenditures have generally not had a measurable impact on improving the economic conditions in the designated enterprise zones, as measured by unemployment rate, population growth, and per capita income (the metrics statute identifies for consideration when establishing enterprise zones). Specifically, data indicates that these economic indicators in enterprise zones did not improve relative to non-enterprise zones during Calendar Years 2012 through 2017.

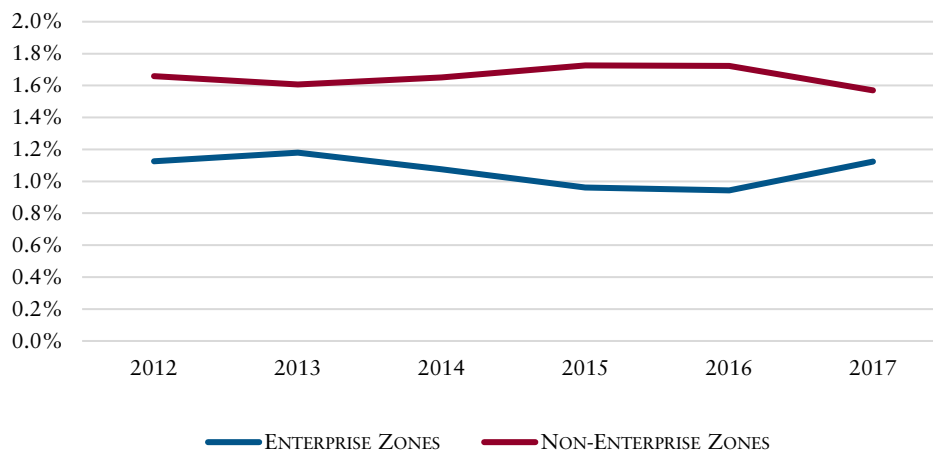
To evaluate the economic performance of enterprise zones compared to non-enterprise zones, we performed a two-part analysis. First, we compared the economic conditions in enterprise zones to non-enterprise zones using U.S. Census Bureau American Community Survey data on unemployment, population growth, and per capita income for Calendar Years 2012 through 2017. Based on this data, we found that the economic conditions in enterprise zones did not improve relative to non-enterprise zones during this time. As shown in EXHIBITS 1.12 through 1.14, enterprise zones' economic performance followed the same trends as non-enterprise zones, but the relative difference in their performance remained similar from Calendar Years 2012 through 2017. Although the boundaries of most enterprise zones remained substantially the same during our review period, there were significant changes to some boundaries during our review period, in particular in 2016. For example, in that year areas of the Lower Highland, Lowry, River North, and Stapleton neighborhoods in Denver were removed from the enterprise zone because of improved economic conditions. Therefore, some fluctuations in the enterprise zones' performance may be caused by new economically distressed areas being added to the zones.

EXHIBIT 1.12. WEIGHTED UNEMPLOYMENT RATE IN ENTERPRISE ZONES AND NON-ENTERPRISE ZONES CALENDAR YEARS 2012 THROUGH 2017



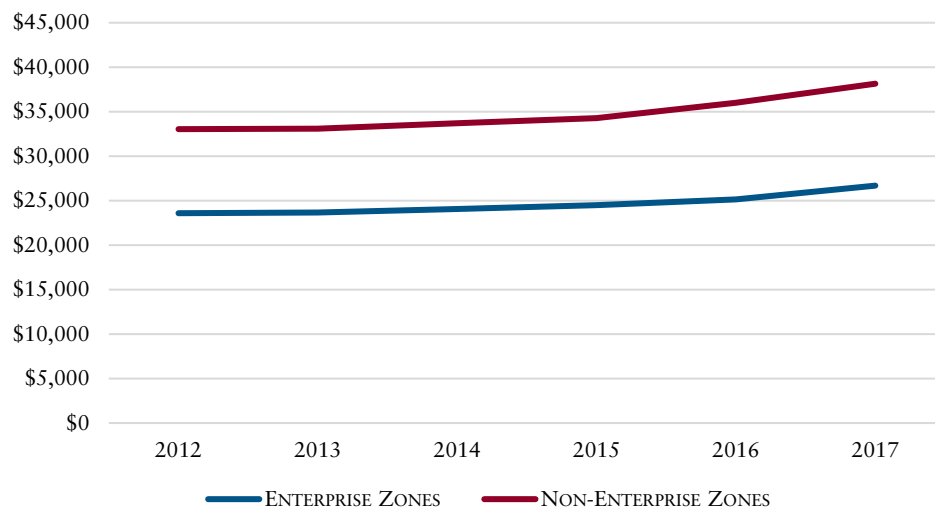
SOURCE: Office of the State Auditor analysis of OEDIT and U.S. Census Bureau American Community Survey data.

EXHIBIT 1.13. WEIGHTED POPULATION GROWTH RATE IN ENTERPRISE ZONES AND NON-ENTERPRISE ZONES CALENDAR YEARS 2012 THROUGH 2017



SOURCE: Office of the State Auditor analysis of OEDIT and U.S. Census Bureau American Community Survey data.

EXHIBIT 1.14. WEIGHTED PER CAPITA INCOME IN ENTERPRISE ZONES AND NON-ENTERPRISE ZONES CALENDAR YEAR 2012 THROUGH 2017



SOURCE: Office of the State Auditor Analysis of OEDIT and U.S. Census Bureau American Community Survey data.

For the second part of our analysis we performed a statistical analysis to measure the impact of enterprise zone designation on the economic performance in enterprise zones from Calendar Years 2012 through 2017 by comparing the performance of areas included within enterprise zones to economically similar areas outside of the zones.

Overall, though we lacked data to include all areas within enterprise zones in our review, we found that for the areas included, being designated within an enterprise zone had no measurable impact on areas' unemployment rates, population growth rates, or per capita income. Specifically, we found that the economic performance in enterprise zones was the same as the performance of areas that were not included within enterprise zones, but that had similar economic conditions as of 2012. Although the Enterprise Zone Tax Expenditures may still provide economic benefits to the state as a whole, this analysis indicates that they have not likely improved these measures of economic performance within enterprise zones relative to areas outside of enterprise zones.

To conduct this analysis we used a statistical method called “propensity score matching” to identify census tracts outside of enterprise zones that would be most suitable for comparison with census tracts located within the enterprise zones. Using data from the U.S. Census Bureau’s American Community Survey, we matched census tracts located entirely inside enterprise zones to census tracts located entirely outside enterprise zones that shared similar economic conditions in 2012. We used the same three economic indicators as the basis for our matching. For each indicator, we used two types of measurement: static and dynamic. Static indicators measure economic performance at a point in time (e.g., unemployment rate as of 2012) and dynamic indicators measure the rate of change in economic performance (e.g., the change in unemployment rate from 2011 to 2012). We included both types of measurement to match census tracts based on both their economic conditions as of 2012 and relative change in economic conditions from 2011 to 2012. Additionally, we included population density in determining the matches to account for the inherent economic differences between rural and urban areas that might not be captured by the other measures.

Based on these measures, we then applied a statistical algorithm to match enterprise zone census tracts with the closest possible match of those census tracts not located in the enterprise zones. Overall, we were able to identify matches for 68 of the 134 census tracts located completely within enterprise zones. Due to a lack of a suitable match, we excluded 66 census tracts, most of which came from the most economically distressed areas of the state. Furthermore, because our analysis only included census tracts that were either fully inside or fully outside an enterprise zone, dense urban areas, where partial zone boundaries are common, were less likely to be included in our analysis. As a result, our conclusions cannot be extended to the most distressed census tracts or dense urban areas.

Once we created our two comparable groups, we assessed the difference in outcomes of the three economic measures in each of the two groups over a 5-year period from Calendar Year 2012 to 2017. We quantified

this comparison using “p-values,” which range from zero to one and, in our analysis, are a way of determining whether differences in each of the three economic measures between enterprise zone census tracts and non-enterprise zone census tracts are likely a result of the enterprise zone designation. P-values provide a measure to identify statistically significant differences, but cannot be used to establish the “percent chance” that enterprise zone designation is causing a difference in economic performance. Based on standard practices for this statistical analyses, p-values of 0.05 or less are needed to establish a potentially statistically significant difference in economic performance based on an area being within an enterprise zone. Our analysis resulted in p-values for each of the economic metrics we used, as follows:

- Rate of population change: 0.93
- Unemployment rate: 0.54
- Per capita income: 0.49

Because the p-values were well above 0.05 for each economic measure, we determined that there is no statistically significant difference in outcomes for enterprise zone census tracts based on the economic metrics we evaluated.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURES?

Based on Department of Revenue data, we estimate that the Enterprise Zone Tax Expenditures had a revenue impact to the State of about \$23.5 million in Tax Year 2016. EXHIBIT 1.15 provides the amount claimed for each of the Enterprise Zone Tax Expenditures for Tax Year 2016. Because the credits can be carried forward for multiple years, they may have been for business activities certified during prior years.

EXHIBIT 1.15. TAX YEAR 2016 REVENUE IMPACT AND CLAIMS PER ENTERPRISE ZONE CREDIT		
	REVENUE IMPACT / CLAIMS	
	AMOUNT	CLAIMS
Investment Tax Credit	\$16,397,000	3,201
New Employee Credit	\$3,583,000	815
Qualified Job Training Program Investment Credit	\$1,598,000	478
Manufacturing Machinery Sales Tax Exemption	\$370,000 ¹	N/A ²
Research and Experimental Activities Credit	\$643,000	249
Employee Health Insurance Credit	\$504,000	122
Vacant Commercial Building Rehabilitation Credit	\$268,000	107
Agricultural Processing Employee Credit	\$91,000	33
Commercial Vehicle Investment Tax Credit	\$21,000	15
TOTAL	\$23,475,000	5,020³
SOURCE: Office of the State Auditor analysis of Department of Revenue data and estimate of Manufacturing Machinery Sales Tax Exemption.		
¹ Estimated by the Office of the State Auditor based on Department of Revenue sales tax information. Estimate is based on Tax Year 2017 data. For the purposes of our estimated total, we assumed this amount remained unchanged from Tax Year 2016.		
² Data was not available to determine the number of claims.		
³ Includes multiple claims by some businesses, so the total does not reflect the number of unique taxpayers.		

For all of these tax expenditures, except the Enterprise Zone Manufacturing Machinery Sales Tax Exemption, we based our revenue impact on figures provided by the Department of Revenue's 2018 Tax Profile and Expenditure Report. However, the Department of Revenue does not separately track or report the revenue impact for the Enterprise Zone Manufacturing Machinery Sales Tax Exemption. Instead, because taxpayers report the amount exempted for this exemption on the same reporting line on the Department of Revenue Retail Sales Tax Return (Form DR 0100) as the broader Manufacturing Machinery Sales Tax Exemption, which is not limited to enterprise zones, data for the two exemptions are aggregated. According to Department of Revenue data, the total combined amount exempted for these two exemptions in Tax Year 2017 was \$3.6 million. Because the Enterprise Zone Manufacturing Machinery Sales Tax Exemption has the effect of expanding the broader Manufacturing Machinery Sales Tax Exemption to cover purchases of mining and oil and gas extraction machinery within enterprise zones, we reviewed the State's Gross Domestic Product (GDP) attributable to the manufacturing, mining, and oil and gas extraction industries in 2017 and found that the mining, and oil and gas extraction sectors comprise 10 percent of the GDP for all of these categories combined. We then

multiplied this by the \$3.6 million reported as exempt for both exemptions to arrive at our estimate of \$370,000 million for the Enterprise Zone Manufacturing Machinery Sales Tax Exemption.

Additionally, insurers who are eligible for credits against their insurance premium tax report them to the Division of Insurance and so these credits are not included in Department of Revenue's 2018 Tax Profile and Expenditure Report. However, according to the Division, no insurers claimed the credits in Tax Year 2016.

According to Department of Revenue and OEDIT data, the number of credits actually claimed by taxpayers has been substantially less than the amount of credits certified by OEDIT in recent years. As shown in EXHIBIT 1.16, for Tax Years 2012 through 2016, taxpayers have only claimed 34 percent of the value of the credits certified by OEDIT during this period. Although taxpayers may claim some of these credits in future years, because the Enterprise Zone Tax Expenditures have been available since 1986, these figures likely account for taxpayers carrying forward credits. As discussed previously, each enterprise zone credit has a specific carry forward period established in statute.

EXHIBIT 1.16. ENTERPRISE ZONE CREDITS CLAIMED VS. CERTIFIED TAX YEARS 2012 THROUGH 2016						
	2012	2013	2014	2015	2016	TOTALS
Department of Revenue Claimed (Millions)	\$28.9	\$25.7	\$25.7	\$24.8	\$23.1	\$128.2
OEDIT Certified (Millions)	\$112.9	\$62.2	\$70.0	\$60.2	\$75.0	\$380.3
Difference (Millions)	\$84.0	\$36.5	\$44.3	\$35.4	\$51.9	\$252.1
Claimed credits as a percentage of Certified Credits	26%	41%	37%	41%	31%	34%
SOURCE: Office of the State Auditor analysis of OEDIT Data and Department of Revenue data.						

While there could be many reasons for taxpayers not claiming the full value of credits, it is likely that many of these taxpayers did not have enough tax liability to use the available credits. This may be especially true for taxpayers who qualify for a credit based on a capital investment within an enterprise zone, since large capital investments may generate net operating losses that can be deducted as investments depreciate

under a separate tax expenditure provision—Section 39-22-504, C.R.S. Further, some taxpayers who are eligible for the credits may not claim them because they are not profitable or discontinue operations before incurring taxable income.

To assess the economic impact of the Enterprise Zones Tax Expenditures that were claimed, we conducted an economic impact analysis using IMPLAN to estimate the economic impact of the tax expenditures as currently applied and the impact if the State refunded the same amount to taxpayers. As discussed in our analysis above, it is likely that much of the investment and hiring associated with these tax expenditures would have occurred regardless of the incentive provided by these tax expenditures. Although we could not quantify the percentage of investments and hiring that were caused by the Enterprise Zone Tax Expenditures, economic reports, such as *A New Panel Database on Business Incentives for Economic Development Offered by State and Local Governments in the United States*, prepared in 2017 by Timothy Bartik for the Pew Charitable Trusts (which also cites studies by Michael Wasylenko, Kevin Hollenbeck, Enrico Moretti, and Daniel Wilson), indicate that business incentives that provide a tax benefit similar to the Enterprise Zone Tax Expenditures increase long-term business activity between 2 and 12 percent, though there can be some variation depending on the economic conditions in the areas targeted. Furthermore, the Enterprise Zone Tax Expenditures provide a smaller relative tax benefit than programs evaluated in these studies. For this reason we performed our analysis based on the assumption that between 1 and 10 percent of the businesses that claimed Enterprise Zone Tax Expenditures would not have gone forward with the associated business activity (i.e., making capital investments, creating new jobs) if the expenditures had not been available.

EXHIBIT 1.17 shows the estimated economic impact of the Enterprise Zone Tax Expenditures, assuming a range of incentivization levels. We used OEDIT data on investments and job creation reported by businesses for credits certified in Fiscal Year 2018 to conduct this analysis. Furthermore, we estimated the revenue impact to the State, assuming that

34 percent of the credits certified will be claimed, consistent with our above analysis on the percentage of certified credits in Fiscal Years 2012 through 2016 that have been claimed. We then assumed that 75 percent of the tax savings would be spent in the state on general business operations, regardless of whether the businesses were incentivized to conduct additional business activities because of the credits or not.

EXHIBIT 1.17. STATEWIDE ECONOMIC IMPACTS OF ENTERPRISE ZONE TAX EXPENDITURES IN FISCAL YEAR 2018¹

PERCENTAGE INVESTMENT/NEW JOBS INCENTIVIZED	COMBINED IMPACT	
	JOBS SUPPORTED	ECONOMIC VALUE-ADDED (MILLIONS)
1%	253	\$26.9
5%	1,265	\$134.6
10%	2,530	\$269.3

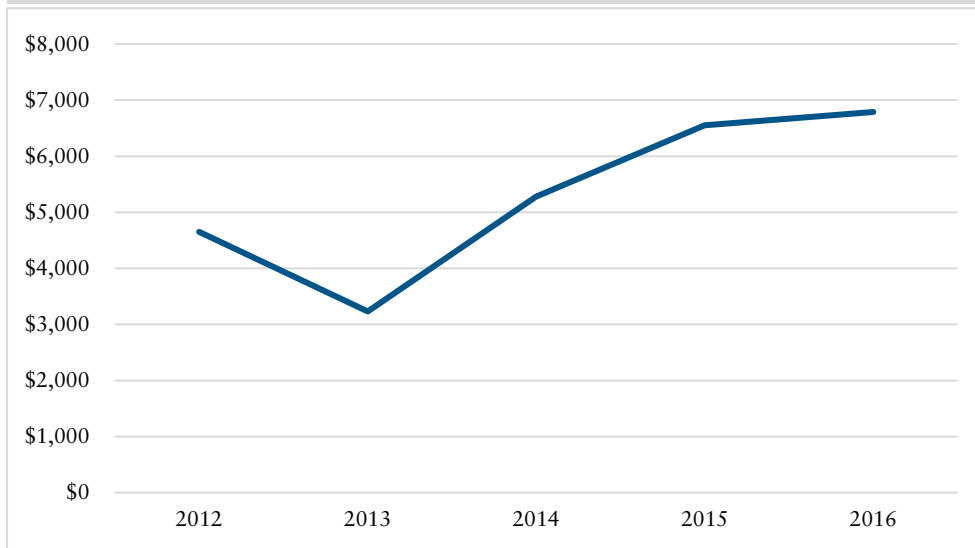
SOURCE: Office of the State Auditor analysis of Department of Revenue and OEDIT data.

¹ Includes amounts for the Enterprise Zone Renewable Energy Credit which is included within OEDIT data on the Investment Tax Credit.

As shown, even at relatively low incentivization rates, the tax expenditures appear to provide a substantial economic impact. For comparison, we used IMPLAN to estimate the economic impact if instead of offering the credits, the State collected the amounts claimed for the Enterprise Zone Tax Expenditures and issued a general refund to taxpayers and found that this would result in 134 jobs supported and \$11.9 million in economic value added within the state. However, these models do not reflect the lost economic activity as a result of the State receiving less revenue and spending less due to the Enterprise Zone Tax Expenditures because we lacked data to provide a comparable model showing the impact of state spending. Additionally, some of the job growth reported by participating businesses may have come at the expense of job losses at non-participating businesses. However, we could not quantify this potential impact and did not include it in our analysis above; therefore, it is possible that our analysis overstates the cost effectiveness of the tax expenditures to some extent. In addition, this impact is not limited to the enterprise zones themselves, and based on our analysis showing that there is no measurable difference in the economic performance of enterprise zones relative to non-enterprise zones, it appears likely that the economic impact is spread throughout the state.

In addition, to further assess the Enterprise Zone Tax Expenditures' cost effectiveness, we reviewed the amount of credits claimed during Tax Years 2012 through 2016 to the total number of net new jobs reported by participating businesses for Fiscal Years 2012 to 2016. As shown in EXHIBIT 1.18, we found that the amount of credits claimed by participating certified businesses for every new net job they reported has increased from \$4,649 in 2012 to \$6,789 in 2016, a 46 percent increase. This may indicate that the Enterprise Zone Tax Expenditures have become less cost effective in creating new jobs in the state during this period. However, because we lacked data on the percentage of new jobs businesses reported that would not have occurred in the absence of these expenditures, we could not determine the cost to the state for every net new job that was caused by them, which would likely show a substantially higher cost to the State per job and provide a clearer measure of their cost effectiveness over time.

EXHIBIT 1.18 CREDIT AMOUNT CLAIMED PER NET NEW JOB REPORTED BY PARTICIPATING BUSINESSES 2012 THROUGH 2016



SOURCE: Office of the State Auditor analysis of Department of Revenue and OEDIT data.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURES HAVE ON BENEFICIARIES?

If the Enterprise Zone Tax Expenditures were eliminated, businesses operating in Colorado would no longer have the added incentive

provided by these expenditures to hire and make investments within enterprise zones. However, the results of our evaluation indicate that the Enterprise Zone Tax Expenditures have provided a relatively small tax benefit and incentive for businesses, so if they were eliminated, the impact to businesses would likely be relatively small statewide, though the impact to specific taxpayers would vary significantly. In Fiscal Year 2018, OEDIT data shows that about 3,100 taxpayers were certified for between \$9 and \$3,100,000 in enterprise zone credits, with the average taxpayer certified for about \$18,000 in credits and the median taxpayer certified for about \$1,600. For some businesses, these amounts may not be enough to have a significant impact, especially considering that in recent years, only about 34 percent of certified credits have been claimed; however, for businesses that operate on smaller profit margins, the impact could be more substantial. For example, many agricultural businesses are certified for enterprise zone credits and these businesses tend to operate on smaller profit margins, which indicates that eliminating the Enterprise Zone Tax Expenditures could have a more substantial effect on these businesses.

In addition, some economic development stakeholders we spoke to indicated that, without the Enterprise Zone Tax Expenditures, businesses would grow more slowly in many distressed parts of the state. Moreover, for some businesses, it might also reduce the attractiveness of locating or expanding their businesses in Colorado due to a perception that the State is less “business-friendly” than other states. However, stakeholders also indicated that the availability of tax credits is one factor among many that companies consider when deciding whether to go forward with a decision to locate, expand, invest, and/or increase hiring in a particular location and they are not typically the deciding factor.

We also surveyed businesses currently in an enterprise zone and asked how their business would be impacted if the enterprise zone credits were eliminated. Just over half who responded to the applicable question (69 of 135) said that eliminating the Enterprise Zone Program would result in negative impacts to their business, including an increase in taxes,

which would result in less capital to invest in growing their business and adding additional employees. Further, 40 percent of respondents stated that they did not know what the impact would be if the program were eliminated, while 9 percent reported that there would be no impact on their business.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

In addition to Colorado, 38 other states and the District of Columbia currently offer tax expenditures similar to Colorado's Enterprise Zone Tax Expenditures, although there is variation in how the tax expenditures work, including the size of each state's zones, whether pre-qualification is required, how the tax expenditures are structured, and their annual revenue impact. For example, in Arkansas, Georgia, Mississippi, and North Carolina, virtually all of the states' land areas have been designated as enterprise zones, while Michigan and Indiana restrict their enterprise zones to small parcels of land. Besides Colorado, only eight other states require pre-qualification before a business' operations begin or are substantially increased in order for the business to claim enterprise zone tax expenditures, including Alabama, Connecticut, Delaware, Iowa, Maine, Ohio, Rhode Island, and Texas.

In addition, we performed a more detailed review of similar tax expenditures in the states bordering Colorado. As shown in EXHIBIT 1.19, eligibility requirements and benefits vary widely from state-to-state. Although three of the seven states bordering Colorado do not offer enterprise zone tax expenditures, all of them provide some type of economic development incentives. As shown, each of the four bordering states with enterprise zone tax expenditures similar to Colorado target both employment and investment, though the credit amounts tend to be generally lower than Colorado's or capped at a certain amount.

EXHIBIT 1.19: SUMMARY OF NEIGHBORING STATES' ENTERPRISE ZONE TAX EXPENDITURES

STATE	SUMMARY
Oklahoma	<p><i>Qualifications:</i></p> <ol style="list-style-type: none"> 1 Counties that have experienced population decreases. 2 Counties that rank in the lowest third by per capita income. 3 Urban areas where poverty exceeds 30 percent or per capita income is 15 percent or more below state average. <p><i>Benefits:</i></p> <p>Provides manufacturers a tax credit based on either an investment in depreciable property OR on the addition of full-time equivalent employees. The credits are available statewide, but additional amounts are provided within enterprise zones equivalent to the greater of an additional 2 percent per year of investment in qualified property or a credit of \$1,000 per new job and may be claimed for 5 years.</p>
Kansas	<p><i>Qualifications:</i></p> <p>Economically distressed areas located within cities.</p> <p><i>Benefits:</i></p> <ol style="list-style-type: none"> 1 Tax credit on qualified employees equal to \$350 per \$100,000 in salary, and \$500 when a qualified targeted employee. 2 Tax credit available for business investment statewide, but additional amounts are provided in enterprise zones equal to \$1,000 per \$100,000 on investments, \$1,500 per \$100,000 in salary on qualified employees in metropolitan areas, and \$2,500 per \$100,000 in salary in nonmetropolitan areas.
Nebraska	<p><i>Qualifications:</i></p> <ol style="list-style-type: none"> 1 Areas with high unemployment, poverty, and declining populations. 2 Zones within a single county, not to exceed area of 16 square miles. <p><i>Benefits:</i></p> <ol style="list-style-type: none"> 1 Variable grant amounts based on number of new jobs created or workers trained. 2 A variety of grants made available for research and development, new businesses, innovation, and businesses that make capital investments. There is also a tax credit for residents who contribute to startups.

EXHIBIT 1.19: SUMMARY OF NEIGHBORING STATES' ENTERPRISE ZONE TAX EXPENDITURES

STATE	SUMMARY
Utah	<p><i>Qualifications:</i></p> <p>Counties with population of less than 70,000 or municipalities with populations less than 20,000, with “clear evidence of the need for development.”</p> <p><i>Benefits:</i></p> <ol style="list-style-type: none"> 1 \$750 credit for each new full time position plus \$500 if the new position pays 125 percent of the county average monthly wage for the industry, plus \$750 if position is in agricultural processing, plus \$200 if the position has an employer sponsored health plan. 2 Contribution credit of 50 percent (capped at \$100,000) for contributions to nonprofits engaged in economic development. 3 Vacant/rehabilitated buildings credit for 25 percent of first \$200,000 spent to rehabilitate. 4 Investment tax credit of 10 percent of the first \$250,000, and 5 percent of the next \$1 million in capital investment.
Wyoming	No enterprise zones, although other economic development tax credits, grants, and loans are available.
New Mexico	No tax benefits unique to enterprise zones, though other economic development tax credits available.
Arizona	No enterprise zones, although other economic development tax credits available.

SOURCE: Office of the State Auditor review of Bloomberg BNA information on tax provisions in states bordering Colorado.

ARE THERE TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

Statute provides several additional tax expenditures similar to the Enterprise Zones Tax Expenditures, including the:

- **OLD INVESTMENT TAX CREDIT** [Section 39-22-507.5, C.R.S.], which provides corporations with an income tax credit for Colorado investments in historic buildings; alternative energy projects; certain “advanced” coal energy projects; and “gasification” projects, which convert organic materials into carbon monoxide, hydrogen, and carbon dioxide. This credit is equal to varying amounts of the eligible investment based on federal income tax criteria, up to \$5,000 plus 25 percent of the taxpayer’s tax liability in excess of \$5,000. Taxpayers without sufficient tax liability are generally allowed to carry their credits back up to 3 tax years and forward up to 7 tax

years. However, taxpayers are not allowed to claim the Old Investment Tax Credit for the same investment in which they are also claiming the Enterprise Zone Investment Tax Credit.

- **NEW INVESTMENT TAX CREDIT** [Section 39-22-507.6, C.R.S.], which provides a broader corporate income tax credit for similar types of Colorado investments allowable under the Enterprise Zone Investment Tax Credit, except without the restriction that the investment must be used within an enterprise zone. Such investments include tangible personal property; other tangible property used in manufacturing, extraction, production, transportation, communications, or energy; agricultural structures; oil and gas storage facilities; and livestock, but exclude real estate, buildings, or building components. The maximum credit allowed is \$1,000 per taxpayer, reduced by the amount of any Old Investment Tax Credit claimed. Taxpayers without sufficient tax liability can generally carry them forward for up to 3 tax years with no carry back allowed. Taxpayers are allowed to claim both the New Investment Tax Credit and the Enterprise Zone Investment Tax Credit for the same investment.
- **GENERAL MANUFACTURING MACHINERY SALES TAX EXEMPTION** (General Exemption) [Section 39-26-709, C.R.S.], which provides for a statewide sales and use tax exemption covering many of the same types of machinery and equipment as the Enterprise Zone Manufacturing Machinery Sales Tax Exemption. However, the General Exemption does not include purchases of property used for refining, mining, and oil and gas extraction, which are included in the Enterprise Zone Manufacturing Machinery Sales Tax Exemption. Further, the General Exemption is limited to purchases of machinery that can be capitalized and depreciated, whereas this limitation does not apply to the Enterprise Zone Manufacturing Machinery Sales Tax Exemption.
- **HISTORIC PROPERTY PRESERVATION CREDIT** [Section 39-22-514, C.R.S.], which provides a tax credit for taxpayers who perform preservation projects on eligible properties, with the intent of encouraging economic development and renovation of properties.

However, a taxpayer who is allowed to claim the Enterprise Zone Rehabilitation of a Vacant Building Credit, as allowed by Section 39-30-105.6, C.R.S., may not claim the Historic Property Preservation Credit for the same rehabilitation project.

- **REGIONAL HOME OFFICE RATE REDUCTION** [Section 10-3-209(1)(b)(I)(B), C.R.S.], which provides a 50 percent insurance premium tax rate reduction for insurers who maintain a home office or regional home office in Colorado.

OEDIT also administers several other programs and tax expenditures aimed at incentivizing business location, growth, investment, and hiring in Colorado including the:

- **COLORADO STRATEGIC FUND**, which provides cash incentives to qualified businesses located in Colorado based on net new full-time jobs created above the county average annual wage. Eligibility is determined based on factors such as fund matching commitments from local governments; the potential for economic “spinoff” benefits, such as expansion initiatives or attracting suppliers; and interstate competitive factors. The amount of cash incentive provided by the Colorado Strategic Fund depends on whether the business is located in an enterprise zone and the degree to which the average annual wage of the business’ net new jobs exceeds the county average wage, ranging from \$2,500 to \$5,000 per net new job. During Fiscal Year 2018, the Commission approved 16 Strategic Fund projects for up to \$11.3 million in performance-based cash incentives.
- **JOB GROWTH INCENTIVE TAX CREDIT**, which provides a tax credit for businesses that undertake job creation projects and documents that they would not otherwise occur in Colorado. Businesses must create 20 or more jobs to qualify or five or more within enhanced rural enterprise zone counties. During Fiscal Year 2018, the Commission approved 34 projects for up to \$156.7 million in future Job Growth Incentive Tax Credits.

- **RURAL JUMP START**, which provides an income tax credit equivalent to 100 percent of businesses' income tax liability and a sales tax exemption for businesses that locate in a rural jump start zone. Qualifying employees of the business also receive an income tax credit. To qualify, businesses must demonstrate that they will not compete with businesses currently operating in the state, coordinate with a local institution of higher education, and create new jobs. Currently, eight Colorado businesses have begun operations and met the requirements to remain in the Rural Jump Start Program, which had a 2018 state revenue impact of \$143,000.

THE COLORADO RURAL ECONOMIC DEVELOPMENT INITIATIVE, administered by the Department of Local Affairs, also provides a variety of grants intended to help rural communities diversify their economy. Types of grants available through the initiative include:

- Local government economic planning grants, such as for engineering plans and studies on land use feasibility or marketing.
- Infrastructure grants, such as for facility expansion, business incubators, and industrial park infrastructure.
- Grants that support the development of rural entrepreneurial businesses.

Colorado counties, municipalities, school districts, and special districts often also provide incentives for business location, expansion, and hiring through local sales and property tax expenditures. Sections 30-11-123, 31-15-903, 32-1-1702, and 39-30-17.5 C.R.S., allow counties, municipalities, and special districts, to negotiate employment-based property tax incentives with taxpayers who are establishing new business facilities, expanding existing business facilities, or have existing business facilities that are at risk of being relocated outside the state.

There are also several federal programs and tax expenditures aimed at improving economic conditions in economically distressed areas, including:

- **FEDERAL NEW MARKET CREDITS.** These provide credits for individuals and corporations who make equity investments in domestic corporations or partnerships that provide loans, investments, or financial counseling in low-income and rural communities. Over a 7-year period, investors can claim credits equal to 39 percent of the cost of their investments.
- **FEDERAL WORK OPPORTUNITY TAX CREDITS.** These provide credits for businesses that hire individuals from certain groups, such as veterans, recipients of the Supplemental Nutrition Assistance Program (SNAP) between the ages of 18 and 39, and residents of federally-designated “rural renewal counties” between the ages of 18 and 39. Businesses are allowed to claim credits equivalent of 20 to 40 percent of the new hires’ qualified wages, up to \$2,400 per employee, per year.
- **FEDERAL OPPORTUNITY ZONES.** These zones were created with the federal 2017 Tax Cuts and Jobs Act to support economic development in economically distressed areas of the country. Taxpayers investing in a qualified opportunity fund, the investment vehicle through which funds are made available for economic development in distressed areas, are eligible for a deferral of federal capital gains taxes on the investment. Of Colorado’s 1,249 census tracts, 126 have been approved as designated Federal Opportunity Zones.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURES?

We were unable to match OEDIT and Department of Revenue data for businesses that claimed the Enterprise Zones Tax Expenditures. As a result, we could not conduct a complete analysis of these taxpayers’ actual credits claimed as compared to the amount for which they were certified and the amount they carried forward. Department of Revenue staff reported that data for partnerships are the primary reason why Department of Revenue and OEDIT data do not match for these taxpayers. Specifically, when a partnership elects to claim the Enterprise Zones Tax Expenditures and passes the credits through to its partners,

it is supposed to file the Enterprise Zone Credit and Carryforward Schedule (Form DR 1366), calculate the credit available for its partners, show the credits being passed through to the partners on its tax return, and then use the Pass-through Entity Enterprise Zone Credit Distribution Report (Form DR 0078A) to report the credit amounts being distributed to each partner. The partners must then also complete and file a DR 1366 with their respective income tax returns to claim the credits and indicate the partnership name and account number, and their percentage of ownership in the partnership.

According to the Department of Revenue, not all partnerships are filing partnership returns and partners are instead claiming the credits on their individual returns. For these taxpayers, the Department of Revenue does not have data to show the business entity from which the credit originated. Since OEDIT data only tracks certifications at the business entity level, it is difficult to match the credits claimed by partners to the businesses that were certified for a credit. Furthermore, when taxpayers claim any of these credits, they are required to attach the certificate provided by OEDIT to their tax returns. However, GenTax, the Department of Revenue's tax processing system, does not capture the certificates, and Department of Revenue staff reported that it is possible that some taxpayers do not submit their OEDIT certificates with their income tax returns.

Because this data constraint is largely driven by taxpayers not following the Department of Revenue's reporting requirements, addressing it would require more stringent review of taxpayer returns. According to the Department of Revenue, due to resource constraints, its staff do not review all returns for taxpayers who claim the credit and therefore, cannot enforce this reporting requirement in all cases.

In addition, the Department of Revenue's Retail Sales Tax Return (Form DR0100) does not have a separate line for vendors to report the value of their exempt sales due to the Enterprise Zone Manufacturing Machinery Sales Tax Exemption. Instead, the line combines this exemption with the general Manufacturing Machinery Sales Tax Exemption. As a result, we could not disaggregate these exemptions and

had to estimate the revenue impact of the Enterprise Zone Manufacturing Machinery Sales Tax Exemption. If this data were available, we would be able to provide a more reliable estimate of the exemption's revenue impact. Therefore, if the General Assembly determined that a more accurate figure is necessary, it could direct the Department of Revenue to add additional reporting lines on its Retail Sales Tax Return and make changes in GenTax to capture and pull this information. According to the Department of Revenue, this type of change would require additional resources to develop the form and complete the necessary programming in GenTax (see the Tax Expenditures Overview Section of the Office of the State Auditor's *Tax Expenditures Compilation Report* for additional details on the limitations of Department of Revenue data and the potential costs of addressing the limitations).

Also, although we were able to draw reliable conclusions regarding the extent to which the enterprise zone distinction had an impact on alleviating economic problems within some areas of the state, data limitations prevented us from providing a reliable analysis of dense urban areas. Specifically, statute does not require that enterprise zone boundaries conform to the boundaries between census tracts and we found that enterprise zone boundaries in dense urban areas frequently cut across census tracts, resulting in many tracts that are partially inside and partially outside the enterprise zones. For this reason we could not use U.S. Census Bureau American Community Survey census tract data to perform our analysis in these areas. Although the American Community Survey does report data by block group, which are smaller areas within census tracts, this more granular data comes at the cost of increased margins of error, which we determined were too large to provide for our analysis. Furthermore, enterprise zone boundaries also frequently cut across block groups, so this would not have fully resolved the issue of partial census tracts. Although there are some methods of estimating the data for partial census tracts based on data available for the whole census tract, we found that these methods were either insufficiently accurate for our purposes or would take too much time to be feasible.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER WHETHER THE ENTERPRISE ZONE TAX EXPENDITURES ARE MEETING THEIR INTENDED PURPOSE AND ESTABLISH PERFORMANCE MEASURES TO CLARIFY ITS INTENT FOR EVALUATING THEIR EFFECTIVENESS. As discussed, we found that these tax expenditures have likely encouraged some additional business investment and job opportunities within enterprise zones, though the extent of these benefits seems to have been relatively modest. In addition, we found that the Enterprise Zones Tax Expenditures likely have had a positive economic impact statewide. Stakeholders indicated that the tax expenditures were helpful for encouraging economic growth, although most also reported that they are likely not the primary driver of businesses' decisions regarding investment and hiring in enterprise zones. For these reasons, we concluded that the expenditures are meeting their purpose, at least to a limited extent. However, we also found that the economic conditions in enterprise zones, as measured by the metrics provided in statute for establishing them—unemployment rate, per capita income, and population growth—have not improved relative to non-enterprise zones. Specifically, our statistical analysis of economically comparable enterprise and non-enterprise zone census tracts showed no measurable difference in economic performance for areas designated as enterprise zones relative to non-enterprise zones. Based on this evaluation, and because statute does not include performance measures or goals for these tax expenditures, we were unable to determine whether the Enterprise Zone Tax Expenditures fully achieve the General Assembly's intent. Therefore, the General Assembly may want to review their effectiveness and amend statute to provide performance measures and goals for these tax expenditures, which would aid future evaluations.

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER AMENDING STATUTE TO BETTER TARGET THE ENTERPRISE ZONE TAX EXPENDITURES AND IMPROVE THEIR EFFECTIVENESS. Specifically, we identified the following

issues that may make the tax expenditures less effective at meeting their purpose:

- **BROAD ENTERPRISE ZONE BOUNDARIES, WHICH ENCOMPASS 84 PERCENT OF THE STATE'S LAND AREA, MAY DILUTE THEIR IMPACT WITHIN DISTRESSED ECONOMIC AREAS.** Specifically, we found that because enterprise zones are within commuting range of all of the States' major population centers, individuals hired by participating businesses often do not live in an enterprise zone, but instead likely commute to the enterprise zone to work. Our evaluation found that, statewide, about 61 percent of employees hired by participating businesses within enterprise zones did not live in an enterprise zone themselves, indicating that the tax expenditures' impact on employment is likely spread throughout the state, as opposed to just economically distressed areas. This issue is more pronounced in urban enterprise zones, where there are typically significant population centers within closer commuting range. For some of these enterprise zones we found that up to 86 percent of the employees of participating businesses did not live in an enterprise zone. Our review of enterprise zone programs in other states indicates that most target the boundaries of enterprise zones more narrowly than Colorado, although the criteria for establishing boundaries varies significantly. In addition, our review of academic research related to place-based business tax incentives suggests that they are more effective when targeting a small number of geographic areas.
- **BUSINESSES CLAIM ENTERPRISE ZONE CREDITS DURING YEARS WHEN THEY REDUCE THE NUMBER OF JOBS.** Although many participating businesses reported creating new jobs, we found that for Fiscal Year 2018, about 14 percent of the business certifications were for businesses that reported reducing the number of jobs that they had. These businesses were certified for \$9.6 million in tax credits, most of which was for the Investment Tax Credit, which along with the Commercial Vehicle, Job Training Investment, Vacant Building Rehabilitation, Research and Development, and Employee Health Insurance Tax Credits, is tied to investments, not new jobs. However,

we also found that 230 of the 769 business locations certified for the New Employee Credit and/or the Agricultural Processing Employee Credits, both of which require increases in employment, also reported that they did not create any jobs or reduced the number of jobs on a statewide basis, but had qualified for the credits based on creating jobs at a particular location.

- **BUSINESSES DO NOT CLAIM THE MAJORITY OF CREDITS THEY ARE CERTIFIED FOR, WHICH MAY MAKE THE CREDITS A LESS EFFECTIVE INCENTIVE.** Specifically, we found that from Tax Years 2012 through 2016, businesses only claimed about 34 percent of the credits that OEDIT certified each year. Although there could be many reasons that taxpayers did not claim more of the credits, a significant factor for many businesses, especially new businesses and those making significant investments, is that they may not have sufficient tax liability to apply the credits. Although the credits can typically be carried forward between 5 and 14 years, our review of economic research related to business tax incentives indicates that businesses place much less value on benefits that occur in future years and that tax incentives that provide more benefits up front are more effective at incentivizing business decisions. Making the credits refundable would likely increase their effectiveness as an incentive for businesses that have not participated due to a lack of tax liability; however, this would also substantially increase the revenue impact of the Enterprise Zone Tax Expenditures. Specifically, in Tax Year 2016, about \$51.7 million of the credits certified were not claimed by taxpayers and it is likely that a substantial portion of this amount would have been claimed if the credits were refundable. Further, it is likely that additional taxpayers, who are eligible, but currently do not seek certification for the credits due to a lack of tax liability, would begin claiming credits, which would further increase the revenue impact, though we lacked data to estimate this impact.
- **CREDITS WENT TO LOCATION-DEPENDENT BUSINESSES THAT ARE LESS LIKELY TO BE INCENTIVIZED BY A CREDIT.** Our evaluation found that many participating businesses are in industry sectors, such as railroad

construction and maintenance, oil and gas development and pipelines, mining, cell phone towers, and agriculture that are already likely to make investments in enterprise zones, regardless of available tax incentives, because their business assets and necessary resources are located in enterprise zones. Many of these activities tend to be concentrated in rural areas and are eligible for the Enterprise Zone Tax Expenditures because most of the State's rural areas are included within an enterprise zone. Businesses in these sectors were certified for \$51 million in credits for Fiscal Years 2017 and 2018, which was 42 percent of the total amount of credits certified in those years. Moreover, stakeholders indicated that location-dependent businesses (primarily mining firms and oil and gas producers) claim the majority of the Enterprise Zone Manufacturing Machinery Sales Tax Exemption.

- **CREDITS PROVIDED TO SOME INDUSTRIES APPEAR LESS EFFECTIVE AT INCENTIVIZING THE CREATION OF NEW JOB OPPORTUNITIES.** Specifically, for Fiscal Years 2014 through 2018, we found that 41 percent of the total amount of credits certified for the Enterprise Zone Tax Expenditures went to industries that collectively reported creating only 4 percent of the net new jobs reported by all participating businesses. These industries included utilities, oil and gas extraction, mining, and agriculture industry sectors, which all reported a relatively lower number of net new jobs associated with their credits in comparison to the amount of credits for which they were certified. In addition, we found that the retail, food services, and health care and social service industry sectors accounted for about 32 percent of reported net new jobs and about 9 percent of credit amounts certified. Although these sectors tend to generate relatively more new jobs associated with the Enterprise Zone Tax Expenditures, our review of academic research related to business tax incentives indicates that businesses in these sectors are less likely to increase total employment within economically distressed areas because these businesses' customers tend to be concentrated in the same areas, causing the businesses to compete with each other, so

that job gains at one business often come at the expense of jobs lost at another.

- **THE 2-YEAR VACANCY REQUIREMENT OF THE VACANT COMMERCIAL BUILDING CREDIT MAY LIMIT ITS EFFECTIVENESS.** Specifically, statute [Section 39-30-105.6(1), C.R.S.] requires a building to be completely vacant for 2 years before it can qualify for the credit. Of the 19 zone administrators that we interviewed, four specifically mentioned that this 2-year vacancy requirement limits how often the Vacant Commercial Rehabilitation Credit can be used. According to these administrators, some businesses are unable to claim the credit for buildings that are mostly unused, but have had a temporary use such as storage of materials or being rented temporarily for a holiday themed attraction (e.g., Halloween haunted house). We found that this credit is the least frequently used of all the Enterprise Zone Tax Expenditures, with only 16 businesses claiming it for a total of \$338,000 in certified credits during Fiscal Year 2018, which may indicate few businesses have been able to qualify for it.

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER CLARIFYING THE CARRYFORWARD PERIODS FOR THE NEW EMPLOYEE CREDIT. Section 39-30-105.1, C.R.S., establishes both the New Employee Credit and the Agricultural Processing Employee Credit and generally provides a 5-year carry forward for both credits for taxpayers who lack sufficient tax liability to use the credits. Section 39-30-105.1(4)(a)(II), C.R.S., appears intended to provide for a longer, 7-year carry forward period for the credits for businesses in enhanced rural enterprise zones, in which the credit amounts are also increased. Statute provides that “credits claimed by a taxpayer pursuant to subsections (1)(a)(III) [emphasis added] and (3)(b) of this section” are eligible for the increase carryforward. However, subsection (1)(a)(III) does not refer to the enhanced rural enterprise zone credits, but instead provides additional requirements regarding employees that qualify for the New Employee Credit generally. This appears to be unintentional; instead subsection (1)(a)(II) refers to the enhanced rural enterprise zone credit and appears to be the provision that was intended to be referenced. OEDIT staff confirmed

that this appears to be a drafting error. In addition, the Department of Revenue has been interpreting the statute in the way it appears to be intended, with both credits receiving the equivalent extra 2-year carryforward only if they operate in an enhanced enterprise zone. However, a plain reading of statute could be interpreted by taxpayers to mean that the 7-year carryforward is available for all New Employee Credits, not just those in enhanced rural enterprise zones. Therefore, the General Assembly may want to revise statute to clarify its intent for the carry forward period.