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Improve Transparency During Implementation of New Tax Abatement Reporting Standard

Taxpayers deserve greater transparency when it comes to state tax credits and, with the implementation of new accounting rules, Maryland has a chance to move in the right direction.

The Governmental Accounting Standards Board (GASB), an independent organization that establishes and improves standards of accounting and financial reporting for federal, state, and local governments, has established a new standard that will improve disclosure of tax-based economic development subsidies, also referred to as tax abatements.

Tax abatements reduce or exempt the taxes owed by a specific taxpayer, often allowing for reductions of extremely large amounts which have become quite burdensome on our economy; costing U.S. taxpayers an estimated $70 billion per year without being reflected in any budget. Because of the inconsistency in tax abatement reporting standards, to date, there has been limited evaluation of the cost that these expenditures impose on our economy.

The final GASB ruling, which was released in August 2015, requires all governmental entities to follow a newly developed set of criteria for reporting their tax abatements. [1] This change will make data on governmental expenditures publically accessible and expose the impact of tax abatements.

Tax Abatement

Tax abatements, as defined by GASB, are a reduction of or exemption from taxes, offered under an agreement between a government and a specific taxpayer, typically for the purpose of spurring economic development. [1] The expectation of a communal benefit, specifically in the form of economic development, is what makes tax abatement unique from other tax exemptions. The newly imposed GASB standard will not require all forms of tax expenditures to be reported (exempting corporate sales tax exemptions, for example).

Tax abatements are a popular and extremely costly subsidy. However, it is rare that governmental entities publicly disclose the totals of these expenditures. Prior to the ruling, tax abatement programs existed in 44 states, yet only six states require the release of such details to the public.

Beginning December 15, 2015, state and local governments will be required to report the costs of tax-based economic development subsidy programs (including those involving property, sales, income and other taxes) during the budget process.[2] This data will be publically accessible as early as 2017.

This standard will apply to 204 Maryland entities, including counties, municipalities, and school districts. Reports are submitted to the Department of Legislative Services (DLS), which has the ability to tell the Comptroller to withhold funds if an entity fails to submit its report.

Typically, the local school districts and the children they serve are the most negatively impacted by tax abatement agreements. For example, Baltimore City Schools are losing millions of dollars each year as a result of such deals. The cost of just one deal between Baltimore City and Marriott to build a hotel is $1.4 million next year for Baltimore City Schools because the agreement allows the company to pay $1 per year in lieu of property taxes on a $155 million piece of real estate for 25 years.[3] Generous agreements such as these legally exempt individuals and corporations from paying their fair share, while Baltimore students suffer from deep cuts to their schools, which has forced the termination of hundreds of staff members this school year.

Despite such problems, only a limited number of states give school boards the ability to protect themselves from the potential losses that these deals often result in. Maryland is not one of them.

Reporting Requirements

With the implementation of GASB's tax abatement standard, states and localities will now be required to report tax abatement spending in the notes of their Comprehensive Annual Financial Reports, which is a detailed report that government entities are required to produce about their finances. Specifically, the reports will have to include information regarding the direct and indirect costs of tax abatement economic development projects.

In addition, the new standard recognizes the costs economic development projects often impose on communities, such as infrastructure needs (roads, sewer and water lines, utility connections) and site preparation expenses (land acquisition and parceling, soil remediation, demolition). GASB notes that these are often contractually required in tax abatement project agreements, so the financial statement will need to disclose a government's commitment. [4]

Recommended Areas of Improvement

While the disclosure of information could be invaluable to policymakers and average citizens, neither GASB's final standard nor current Maryland law require the release of this information in a user-friendly manner. Those interested in the county-level data will have to go to each of the 204 jurisdictions individually and collect the information from the notes from financial statements.

To improve local transparency around these tax abatements, Maryland should:

- Require local governments to report their tax abatements in a standard way to a single entity
- Require that entity to aggregate, report and publish the local tax abatement data in an online searchable database, including the ability to break down the data by jurisdiction

Despite the improvements that the final GASB ruling will bring, there are still other areas of concern. For one, GASB's ruling does not mandate the full disclosure of the details of each tax abatement deal. This means that the public will only know the recipients of tax abatements if governments voluntarily release this information. Secondly, GASB does not include all tax expenditures in its definition of tax abatement, which will result in the omission of critical information. For example, Tax Increment Financing (TIF) and performance-based incentives are both costly tax subsidies that may not fall within the parameters of GASB's definition. Unfortunately this creates an incentive for governments to modify tax abatement programs so that they fall outside the reporting requirement. [2] Therefore, the need for tax expenditure reform will remain.

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[1] The Governmental Accounting Standards Board, Tax Abatement Disclosures. 2014.
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[4] Reese, Laurel & Sands, Gary. Land Policy Institute, Current Practices and Policy Recommendations Concerning Public Act 198 Industrial Facilities Tax Abatement. October, 2007. http://www.mml.org/advocacy/resources/lpi_pa198_policybrief.pdf