BEYOND AMAZON: DC AREA HIGH TECH TAX INCENTIVES

Leah Brooks and Caitlyn Valadez

Amazon’s search for its second headquarters home has led cities across the country to lay out what many contend are extravagant incentive packages. How big are these incentive packages? And how much of economic development inducements are run through the particularly opaque tax code? In this policy brief, we explore the tax incentives DC-area jurisdictions offer to retain or relocate high-tech firms. We find that almost all jurisdictions offer high-tech tax incentives, and that these incentives usually exempt firms from high-profile taxes.

For example, the education software company Blackboard was founded in the basement of a Dupont Circle row home in 1997 and is revered as Washington, DC’s first real tech start-up success story. In 2015, Blackboard considered moving out of DC and received offers from economic development officials across the DC metro area. Although Blackboard considered DC the most expensive jurisdiction under consideration, the financial incentives Blackboard received from the city convinced the firm to sign a 12-year lease on a new NoMa headquarters building (Bisnow).1

In this policy brief, we discuss what a tax incentive is, how we identified local high-tech tax incentives and their use in the region.

1. What is a Tax Incentive?

Tax incentives are benefits offered to firms or individuals through the tax code. Specifically, a tax incentive is an exception to regular tax rules designed to achieve a specific goal (Pew Trusts, 2018). Governments leverage economic tax incentives primarily to encourage businesses to undertake actions they would not have otherwise. For example, a property tax rebate offered to a specific firm is a tax incentive. Such incentives usually have a time limit, and sometimes require firms to create jobs; they are often coupled with a requirement that the firm stay in the local jurisdiction.

In contrast, a loan or grant is not a tax incentive. The form by which a government gives money to a firm has implications for the visibility, and therefore the political viability, of the decision. Loans or grants are direct expenditures by government, must be authorized, and are visible in budget documents. These expenditures are at least plausibly transparent.

Expenditures via the tax code – known as tax expenditures because they reduce the revenue the government raises – are more opaque. Tax expenditures occur when firms or citizens pay less money to the government than they would have without the special tax benefit. They are particularly difficult to account for because both the recipients and the value received may not be visible to tax authorities or other taxpayers.

Further, not all tax rules that help businesses economically are economic development tax incentives. For example, when a government creates tax credits, tax deductions, or tax exemptions to reduce the influence of the tax code on businesses decisions such actions may not be tax incentives. If the intent is to ensure the existing tax code does not impact firm decisions, this change is not a tax incentive (Pew Trusts). For example, Virginia’s Land Preservation Tax Credit is a tax incentive, but would not be considered an economic development tax incentive because its primary purpose is to preserve the environment (Pew Trusts).

In this policy brief, we focus not on state-sponsored tax incentives, but on those paid for by local governments. These tend to be much less well-documented than the state-sponsored ones. Of all the local jurisdictions in the greater Washington area, only the District of Columbia conducts evaluations of its tax incentive programs; these evaluations aim to document how much money is spent on tax expenditures and whether they achieve their stated goals.

2. How We Found Local Tax Incentives

In the fall of 2018, we set out to find whether tax incentives were available to create, retain or relocate high tech

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1 Blackboard benefited from the Creative and Open Space Modernization Tax Rebate program which can cover half of a company’s improvement costs, for a maximum amount of $5 million over five years (DC Office of the Deputy Mayor for Planning and Economic Development).
companies within the DC area. We focus on the region’s largest local jurisdictions: the District of Columbia; Maryland’s Montgomery and Prince George’s counties; and Virginia’s Arlington, Fairfax and Loudon counties.

To assess which incentives are available to high technology firms, we relied on information posted online and supplemented with phone calls where that information appeared inconclusive or incomplete.

We focus on two key questions:
(1) Which types of firms qualify for a high tech tax incentive?
(2) What do qualifying firms receive?

### 3. Which firms qualify for DC area high tech tax incentives?

We start with the first question: which firms are “high tech” for tax incentive purposes? One clear finding from our work is that there is no clear-cut definition of a high-tech firm. Table 1 below shows how our study jurisdictions classify firms as high tech. To make the data comparable, we aggregate qualifying firms into seven industry types: aerospace, defense, biotechnology/health, information technology, cybersecurity/computer science, data centers and e-commerce.

<table>
<thead>
<tr>
<th>Industries Eligible for High Technology Tax Incentives</th>
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<tbody>
<tr>
<td>Aerospace</td>
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<tr>
<td>Arlington County, VA</td>
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<tr>
<td>District of Columbia</td>
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<tr>
<td>Fairfax, VA</td>
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<tr>
<td>Loudon County, VA</td>
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<tr>
<td>Montgomery County, MD</td>
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<tr>
<td>Prince Georges County, MD</td>
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Table 1
SOURCE: CENTER FOR WASHINGTON AREA STUDIES FALL 2018 SURVEY.

We find that most local jurisdictions do specialize in a particular high tech industry. Of the local governments we researched, none offers incentives in all of the seven categories. Montgomery County specializes in biotech and cybersecurity. Loudoun County offers incentives to all industries except cybersecurity. Interestingly, Fairfax County offers no tax incentives for high-tech firms.
To put these choices in context, Table 2 shows the total number of employees in 2007 and 2016 by our study jurisdictions, as well as the share of employment in a few specific high-tech categories: biotechnology (we observe only in 2016), computer programming and software installation. Fairfax County has far and away the largest proportion of its workforce in the high-tech industries on which we focus. Fully one in 20 workers in Fairfax County is in the computer programming industry. One interpretation of Fairfax’s lack of incentives is that they are not required: Fairfax is a market leader without them. Fairfax’s share of high tech workers in our categories is three times the share of employees working in computer programming in Arlington, Montgomery or Prince George’s counties — all of which do offer tax incentives for cybersecurity/computer science firms (Table 1 & 2). However, no area county has more than six percent of workers in the three high tech categories we investigate. Among the remaining industries, Montgomery County stands out for the consistently high share of workers in biotech. In contrast, the employment of software installation is much more evenly distributed.

4. What do qualifying firms receive?

Given a definition of “high tech,” we now consider what eligible firms can receive. It is useful to recall that local jurisdictions’ authority to levy taxes or set licensing rates is dictated by state law. For instance, Maryland counties cannot modify sales taxes. Maryland state law sets the state sales tax and prohibits counties from changing it. Furthermore, just because a county offers a specific tax incentive does not necessarily mean that all high technology industries within that jurisdiction are eligible for it. For example, Loudon County offers a tax credit on its business license tax, but only businesses in aerospace and information technology are eligible to receive it.
We now describe some of the specific types of incentives local jurisdictions offer.

**BOPL Tax Credit**
Virginia’s Business, Professional and Occupational License Tax, also referred to as the BOPL tax, is required to conduct business within Virginia jurisdictions. It has evolved over time from a state license tax to a local license fee (tax.virginia.gov).

**Who it Affects:**
- In Arlington County, 50% reduced BPOL rate for 10 years (Arlington County Economic Development).
- As previously stated, only Aerospace and Information Technology companies are eligible for a reduced BOPL tax rate in Loudon County.

**Property Tax Reduction**
A reduction of the property tax paid on property used by the high technology business.

**Who it Affects:**
- In Washington, DC, high technology companies receive a partial exemption from the personal property tax and a “five year freeze on real property taxes for office improvements” (Office of the Deputy Mayor for Planning and Economic Development).
- In Loudon County, aerospace companies manufacturing aircraft and flight simulators and satellite imaging technology companies are eligible for a reduced BOPL tax rate in Loudon County.
- In Prince George’s County companies in manufacturing, fabricating or assembling facilities that are primarily involved with the “engineering, life sciences, computer sciences, research and development, or the production of materials, parts or equipment” used in these industries are eligible for a Property Tax Credit that is phased in over a five year-period, beginning with a 100% exemption on the increased assessment in year one (Prince George’s County Economic Development Corporation).

**Sales Tax Reduction**
A reduction of the sales tax paid on items and services that are not eligible for resale.

**Who It Affects:**
- In Washington, DC, high technology businesses are eligible for a sales tax exemption of “intangible property or services… including internet-related services and sales, website design, maintenance, hosting or operation” (DC Code §47-2001).
- In Loudon County, these are available only to Data Centers that “invest $150 million or more, hire 50 or more employees, pay at least 1.5 times the average local wage, and enter into an MOU with the Virginia Economic Development Partnership” and include data center equipment, such as “servers, routers, generators” and other enabling hardware (Loudon Virginia Economic Development Center).

**Corporate Franchise Tax**
A tax paid on the taxable income of a corporation.

**Who It Affects:**
- In Washington, DC, for “taxable years beginning after December 31, 2017, a tax at the rate of 8.25%” is levied on the taxable income of a corporation (DC Code § 47–1807.02). High technology businesses are entirely exempt from the tax for the first five years. The total amount that each company may receive in exemptions cannot exceed $15 million. After the five-year period or the $15 million limit is reached, the company will still have a reduced tax rate of 6%. (DC Office of Tax and Revenue).
Table 3 summarizes the type of incentives by jurisdiction offered by jurisdiction and gives high-level information on what the requirements are to receive the incentive. Across jurisdictions, DC offers the most types of incentives. Virginia’s jurisdictions—with the exception of Fairfax—offer reductions in the BOPL. Both Maryland jurisdictions offer only one type of incentive. This is an income tax credit in Montgomery County and a property tax rebate in Prince George’s County.

<table>
<thead>
<tr>
<th>Types of Tax Incentives Offered</th>
<th>BOPL Tax Credit</th>
<th>Property Tax Reduction</th>
<th>Sales Tax Reduction</th>
<th>Corporate Franchise Tax Reduction</th>
<th>Income Tax Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arlington County, VA</td>
<td>50% reduction, 10 years</td>
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<tr>
<td>District of Columbia</td>
<td>Partial exemption from the personal property tax &amp; 5-year freeze on real property taxes for office improvements</td>
<td>On intangible property</td>
<td></td>
<td>0% Corporate Tax for first 5 years</td>
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<tr>
<td>Fairfax County, VA</td>
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<tr>
<td>Loudon County, VA</td>
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<td>Data Centers only</td>
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<tr>
<td>Montgomery County, MD</td>
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<td></td>
<td>Income tax credit equal to 50% on eligible investment up to $250,000</td>
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<tr>
<td>Prince Georges County, MD</td>
<td>Phased in over 5 year period</td>
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</tbody>
</table>

Table 3

*If the box is shaded this means that the respective tax incentive is offered in the jurisdiction but not necessarily that every type of high tech industry qualifies for each of these incentives.

*This table does not include all tax incentives offered by each jurisdiction.

SOURCE: CENTER FOR WASHINGTON AREA STUDIES FALL 2018 SURVEY.
5. Why Incentives?

Since DC is the only local jurisdiction to estimate the costs of tax incentives—it is mandated to do so by law—we cannot easily compare the costs of these incentives and their potential benefits. However, Table 4, which shows total payroll in an industry divided by employees in that industry (as a proxy for compensation), shows why jurisdictions find these industries desirable employers. In almost all cases, payroll per employee for targeted high-tech industries is about five times higher than that of the average industry.

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Total Payroll per Employee in All Industries (2018 Dollars)</th>
<th>Payroll per Employee (2018 Dollars)</th>
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<tbody>
<tr>
<td></td>
<td></td>
<td>Biotech</td>
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<tr>
<td>DC</td>
<td>$ 19,439 $ 19,249</td>
<td>-</td>
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<tr>
<td>VA</td>
<td></td>
<td>Arlington</td>
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<td>Loudon</td>
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<td>Fairfax</td>
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<td>MD</td>
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<td></td>
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<td>Prince Georges</td>
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</tbody>
</table>

Table 4


Tax incentives are a powerful tool for local governments, and an important lever for jurisdictions to attract high paying jobs. However, they are not easily discoverable by the public. Our policy brief finds that they are widely offered by DC area governments. As suggested by the Pew Research Center, we encourage local jurisdictions to both publish and formally evaluate their incentives.
References


