FINAL
REPORT

Evaluation of the
Maine Seed Capital Tax Credit

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a report to the
Government Oversight Committee
from the
Office of Program Evaluation & Government Accountability
of the Maine State Legislature

GOVERNMENT OVERSIGHT COMMITTEE OF THE 130th LEGISLATURE

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Table of Contents

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Executive Summary

The Maine Legislature's Office of Program Evaluation and Government Accountability (OPEGA) completed an evaluation of the Maine Seed Capital Tax Credit program (MSCTC). We focused on:

- The extent to which the MSCTC is achieving the program's goals of increasing investment, increasing jobs, and increasing municipal tax bases;
- The extent to which the MSCTC is benefiting the intended beneficiaries of small businesses and jobseekers; and
- How the MSCTC fits within the State's larger economic goals.

The MSCTC is a long-standing tax expenditure program that seeks to incentivize private equity investment in small businesses by offering investors an income tax credit equal to a percentage of their investment in an eligible Maine business. In 2020, the annual cap for tax credits was tripled, from $5 million to $15 million, making this review timely. From 2010 to 2020, the Finance Authority of Maine (FAME) issued tax credit certificates to investors totaling $42.5 million in connection with $95.6 million of private equity investments made in 134 eligible businesses. The MSCTC is one piece of a statewide public-private system of supports for businesses in Maine – many early-stage businesses that receive MSCTC investment also receive funding and support from other programs.

We focused the evaluation on the extent to which the program design achieves the intended goals. We examined program data maintained by FAME and interviewed program stakeholders, including a sample of 10 participating businesses. We also considered research on incentivized investment programs and the design of other states' programs to provide context about the effectiveness of the design of Maine's program.

The MSCTC includes some businesses that described having grown substantially since their first MSCTC investment. However, the effectiveness of the program overall should not be assessed by anecdotal "success" stories only – reliable program data is necessary for ongoing assessment of the extent to which the program is meeting its goals.

Conclusions

OPEGA observed that the MSCTC is associated with substantial private equity investments in Maine businesses. However, OPEGA was unable to fully or reliably assess the effectiveness of the MSCTC in achieving the goals of increasing investment, increasing jobs, and increasing municipal tax bases. In particular, we found the following:

- The business annual report data collected and maintained by FAME is inconsistent and incomplete, rendering it not sufficiently reliable to make concrete assessments of program outcomes.
- Although a goal of the program is to create and retain jobs, there are no effective program design elements that drive towards this outcome. Participating businesses we spoke to described a range of experiences with job creation and retention but there is a lack of systematic program data to reliably measure this outcome.
- Another program goal is to increase investment, but we identified design features that permit credits to go to investors that may have invested anyway due to a connection with the business. The program also may not be maximizing opportunities to increase investment from out-of-State investors.

- Although MSCTC does benefit some businesses that appear to serve the program's intent and goals, OPEGA observed that the program also benefits some businesses that may not necessarily have the potential for rapid growth, such as film companies and businesses in the tourism and hospitality industries.
- The program design does not necessarily lead to an increase in municipal tax bases (another program goal) and no relevant data is collected to assess this, which raises the question of whether it is a core goal of the program.
- Finally, although the MSCTC is included in the "Maine Economic Development Strategy 2020-2029: A Focus on Talent and Innovation" as a tool to promote innovation, the program's design allows a broad range of businesses to benefit from the program, including those that do not appear to advance innovation, such as film companies and businesses in the tourism and hospitality sector.

Overall, we found that the program design is not well-aligned with the program goals, resulting in a situation where one cannot necessarily expect the program goals to be achieved. This suggests that the program goals or the program design or both should be adjusted.

Recommendations

- **OPEGA recommends that the Legislature, in consultation with FAME, the Department of Economic and Community Development (DECD), and other stakeholders as appropriate, re-evaluate and clearly define program goals and what "success" looks like in terms of outcomes. Thereafter, the program design should be adjusted, through amendments to statute or agency rules as appropriate, to ensure the program requirements align with the goals.**

- **OPEGA recommends that the Legislature, in consultation with FAME and DECD as appropriate, adjust the program's reporting requirements to allow for effective oversight of whether the program is meeting its goals.**

The recommended re-evaluation of program goals and design should include consideration of how the program is intended to fit within the public-private "eco-system" that exists to support early-stage businesses in Maine. After developing a clear definition of the MSCTC program goals, the program design should be adjusted to focus on meeting the defined goals. Different goals suggest different program design features, including different ways of defining the target businesses. With clear goals and a program design aligned with those goals, program data collection and reporting should be adjusted to align with the goals to allow for effective monitoring, oversight and continuous assessment of the extent to which the program is achieving its goals.

- **OPEGA recommends that FAME improve their processes for program data collection, analysis, and reporting.**

Whether or not changes are made to the program goals and design, OPEGA has identified areas for improvement by FAME in their approach to data collection, analysis, and reporting. Although the program was set up to be administered in a hands-off way, the substantial increase in the State's investment in the program over time, including the recent tripling of the annual cap on credits, may warrant reconsideration of this hands-off approach to ensure the State tax expenditure is a cost effective and efficient use of resources.

I. Introduction

The Maine Legislature's Office of Program Evaluation and Government Accountability (OPEGA) has completed a review of the Maine Seed Capital Tax Credit program ("MSCTC" or "Seed credit"). OPEGA performed this review as directed by the Government Oversight Committee (GOC) of the 129th Legislature, in compliance with 3 MRSA §999. The goal of the tax expenditure evaluation process is to assess the extent to which the tax expenditure is meeting its purposes in order to assist the Legislature in oversight and policy making. The GOC approved the evaluation parameters for OPEGA's review on January 24, 2020, including statements of the program purpose, intended beneficiaries, evaluation objectives, and performance measures (see Appendix A for the approved evaluation parameters).

The Seed credit has recently received increased attention from both the Maine State Legislature and the Executive Branch. The Maine Economic Development Strategy 2020-2029: A Focus on Talent and Innovation ("Strategic Plan") issued by the Department of Economic and Community Development (DECD) references the MSCTC as a tool to promote innovation. The Strategic Plan included a proposed action to raise the annual program cap for the Seed credit from $5 million to $15 million, in order to assist startups and create new jobs.[1] In early 2020, the Legislature enacted that proposal within the State budget.[2] The tripling of the State's commitment to the Seed credit makes this an opportune time to evaluate the program and to identify opportunities to improve its efficiency and effectiveness.

To complete the evaluation of the Seed credit, OPEGA obtained program information and data from the Finance Authority of Maine (FAME), businesses and investors participating in the program, and information in the public domain. OPEGA's full evaluation methods are described in Appendix A.

The remainder of this report is organized in three key sections as follows:

- Program background and overview;
- Evaluation results, addressing program outcomes and design issues across 6 key areas:
  - Fiscal and economic impacts;
  - Private investment;
  - Business development;
  - Job creation and retention;
  - Municipal tax bases;
  - Innovation; and
- Opportunities for improvement and recommendations.

[1] Action C2 of the Strategic Plan states: "Every dollar of Seed Capital Tax Credit raises ten dollars of private investment. An increase in the ceiling from $5 to $15 million would help about 40 startups and create 2,300 new jobs."
[2] PL 2019, c. 616.

II. Program Background and Overview

The MSCTC is a long-standing tax expenditure program that seeks to incentivize private equity investment in small businesses by offering investors an income tax credit equal to a percentage of their investment in an eligible Maine business. The effect of the credit is to reduce the investment risk to investors by the State guaranteeing a return of a portion of their investment by way of an income tax credit. In our interviews with program participants and stakeholders, we heard that the program is popular with investors and businesses alike.

A. Program Administration

Under the enabling statute, FAME is authorized to issue tax credit certificates to eligible investors (10 MRSA §1100-T). As program administrator, FAME is responsible for processing applications, determining eligibility of businesses and investors, issuing tax credit certificates to investors, and collecting and reporting program data. In this evaluation, OPEGA spoke to a range of program participants and stakeholders, all of whom were complimentary about the accessibility and helpfulness of FAME staff in assisting businesses, investors, and interested parties in navigating the program requirements.

The Maine Revenue Service (MRS) processes the actual claims for the credit by investors as part of their income tax filings, but is not otherwise involved in the administration of the credit.

B. Program Design

Key aspects of the Seed credit design include:

Credit percent: The Seed credit provides a tax credit as a percentage of dollars invested in eligible businesses. For investments made on or after April 1, 2020, the tax credit is up to 40% of the amount invested.[3] From January 2014 to March 2020, the credit was up to 50% for both individual investors and private venture capital funds (PVCFs). Appendix F shows how Maine's credit level compares to other states with similar programs, the majority of which offer a credit of 20% to 35%.

Eligible investors: Eligible investors can be taxpayers or PVCFs. Individual investors cannot own 50% or more of the business. Principal owners of the business, their spouse, and specified family members with an existing ownership interest in the business are not eligible for the Seed credit.[4] Investors are not limited in the total amount of tax credit certificates they may be granted; however, there are limits on the amount of investment by a single investor in a single business over a consecutive three-year period.

Eligible businesses: An eligible business must:

- Be located in Maine;
- Have annual gross sales of $5,000,000 or less;

[3] 10 MRSA §1100-T(2)(A) & (2-C)(A).
[4] "Principal owner" means a person who controls the business, whether through majority ownership or direct involvement in the day-to-day management of the business.

- Be the full-time professional activity of at least one of the principal owners;
- Fit into one of five eligible business categories:
    - a manufacturer;
    - value-added natural resource enterprise;
    - provide a product or service that is sold or projected to be sold or rendered predominantly outside of the State;
    - be engaged in development or application of advanced technologies; or
    - is certified as a visual media production company; and
- Certify that the amount of the investment is necessary to allow the business to create or retain jobs in the State.

For businesses approved as eligible from April 1, 2020, the program has a $3,500,000 lifetime limit (reduced from $5,000,000) on Seed credit eligible investment.[5] This change is discussed further at Appendix D.

Investment requirements: Seed investments must be used on plant, equipment, research and development, or working capital for the business – the only prohibited use of funds is repayment of equity investments.[6] The investment must be at risk for five years, meaning that the investment must remain in the business and may be lost if the business is unsuccessful.

Claiming the credit: Starting with the year of investment, the investor may claim up to 25% of the credit over each of the first four years. For PVCF investors, the tax credit is received in the form of a refund. For other investors, it is received as a credit against the income tax due in a year. This credit cannot exceed 50% of the income tax due in a year - if this limitation prevents the credit from being taken over four years, the credit may be carried forward for up to 15 years.

C. Program History and Origins

The MSCTC became effective on January 1, 1988, making it the first of its kind in the nation.[7] In the enabling statute, the Legislature highlights that "small new businesses can provide significant economic benefits to the State provided that they can obtain sufficient seed equity financing to carry them from start-up through the initial development phases of a business" (PL 1987, c. 864).

Since enactment in Maine, 31 other states have enacted similar tax credit programs.[8] Some states have repealed or let their programs expire, resulting in current programs in 24 states (see Appendix F for a list of programs in other states).

[5] LD 229 ("An Act to Increase Investment Caps in the Maine Seed Capital Tax Credit Program") was passed to be enacted by the House and Senate of the 130th Legislature and signed by the Governor on July 8, 2021.
[6] Program Rules (94-457, Chapter 307), paragraph 3(B)(1).
[7] Program enacted by PL 1987, c. 854. Denes et al. (2020) published extensive research on angel investor tax credit programs and identified Maine as the first program in the United States and North Dakota as the next program implemented in 1993.
[8] Denes et al (2020, 6).

The specific type of businesses eligible for the MSCTC has evolved over time. At its inception, the program was limited to businesses that export their products or services out of the State. Over time, four additional business categories were added as eligible for the program, resulting in the current five eligible business categories listed below.

Table 1: Eligible business categories and implementing Public Law	
Eligible Business Category	**Enabling Law**
Businesses that export products and services from the State	PL 1987, c. 854
Manufacturers	PL 1991, c. 854
Businesses that are engaged in the development or application of advanced technologies	PL 1997, c. 774 & PL 1999, c. 504
Certified visual media production companies	PL 2009, c. 470
Value-added natural resource enterprises	PL 2013, c. 438
Source: OPEGA review of legislative history	

Over time, the Legislature has amended various other aspects of the program, including:

- The tax credit amount as a percentage of investment dollars, including adding a temporary provision that allowed an enhanced level of credit for investment in businesses in high unemployment areas;
- The percentage of the credit that can be taken per year;
- Business revenue limit; and
- Investment limit for businesses and investors.

The requirement that businesses certify that the investment is necessary to create or retain jobs to be eligible was added in 2014.[9]

The program was enacted with an overall limit for available credits. This limit was initially $2,000,000 for up to and including calendar year 1996. The limit was increased gradually by successive Legislatures until it reached $30,000,000 for up to and including calendar year 2013.[10] From 2014, the program was changed to having an annual cap on available tax credits (see Table 2 for the annual tax credit caps). In 2020, the Legislature enacted several program changes, including:

- Raising the annual credit limit from $5 to $15 million for investments made in calendar years 2020-2026;[11]
- Reducing the credit from 50% to 40% of the amount invested in an eligible business;
- Reducing the aggregate investment in a business limit ($5 to $3.5 million and not more than $2 million in a calendar year);
- Expanding business reporting requirements; and
- Setting public policy objectives of the credit for the purpose of program evaluation.[12]

[9] PL 2013, c. 438.
[10] 10 MRSA §1100-T(4).
[11] In 2021, LD 229 (Senate Amendment to Committee Amendment A) changes the annual credit limit from $15 million to $13.5 million for calendar years 2021 and 2022.
[12] PL 2019, c. 616.

In this evaluation, we considered program amendments enacted in 2020 to the extent that we were able. For example, we included investment and credit data for the entirety of 2020 and commented on the expanded business reporting requirements.

D. Program Participation, Credits, and Investment

From 2010 to 2020, FAME issued tax credit certificates to investors totaling $42,541,781 in exchange for $95,673,690 of private equity investments made in eligible businesses (a ratio of 1:2.25), as shown in Table 2. The program is popular with both investors and businesses. From 2015 to 2019, the annual program cap was met each year. In 2019, the $5,000,000 limit on tax credits was met on the first day.

From 2010 to 2020, 134 unique businesses received MSCTC investment (see Appendix C for a list of businesses and associated investments and credits). Because many businesses benefit from MSCTC investment in multiple years, the total number of businesses receiving investment exceeds the number of unique businesses over the period. Table 2 shows the total number of businesses receiving investment each year, broken down by the number that received their first MSCTC investment that year and the number that received subsequent (or "follow-on") MSCTC investment each year.

Table 2: 2010-2020 MSCTC investments, credits, cap, and breakdown of businesses

Calendar year	MSCTC investment	MSCTC tax credits issued	MSCTC annual cap	Number of businesses receiving investment	Number of businesses receiving first investment	Number of businesses receiving follow-on investment
2010	$8,255,943	$3,363,344	n/a	24	17	7
2011	$4,130,165	$1,381,066	n/a	22	10	12
2012	$4,670,030	$2,744,014	n/a	24	10	14
2013	$380,000	$202,400	n/a	3	1	2
2014	$729,999	$525,000	$675,000	4	1	3
2015	$7,596,920	$3,948,460	$4,000,000	32	17	15
2016	$10,104,691	$4,994,943	$5,000,000	29	16	13
2017	$10,009,388	$4,999,994	$5,000,000	27	14	13
2018	$9,991,423	$4,995,711	$5,000,000	33	13	20
2019	$10,212,821	$4,999,902	$5,000,000	20	6	14
2020	$29,592,309	$10,386,948	$15,000,000	46	18	28
Total	**$95,673,690**	**$42,541,781**	-	264	123	141

Notes: From 1988-2013, the program cumulative cap was $30,000,000.
2020 credit and investment figures are as of May 2021.
To determine whether a business received a first or follow-on investment in 2010, we considered investment and credit data from 2007-2009 - some businesses may have received a first investment prior to 2007.
Source: OPEGA analysis of investment and credit data provided by FAME.

E. Program Context and the Challenge of Attribution

In any discussion or analysis of MSCTC and its effects, it is important to consider the broader context and environment in which this program operates. The MSCTC is one piece of a statewide public-private system of supports to assist businesses in Maine.[13] This system has grown and evolved over time since the enactment of the MSCTC and currently consists of entities created by the State, such as the Maine Technology Institute (MTI)[14] and the Maine Venture Fund (MVF)[15], along with individuals and groups of private equity investors and PVCFs.

An individual business might seek financial support from multiple parts of this system (often more than once) in the course of the business's development. For example, of the 29 businesses that received MSCTC investment in 2016, 21 also received funding from MTI, MVF or both between 2010-2020. Additionally, some businesses are likely to be eligible to participate in the Pine Tree Development Zones (PTDZ) and the Employment Tax Increment Financing (ETIF) programs and/or receive funding through federal research and development grants.

One stakeholder described the system of supports as being like a three-legged stool, where each leg is necessary - two legs consist of MTI and MVF, and the third leg is private investment (supported by the MSCTC). One business that we interviewed described MTI, MVF, and the private investment community (as encouraged by the MSCTC) as the three major cornerstones to the success of their business.

This context is important and makes it particularly challenging to attribute outcomes to one particular program, such as MSCTC. This impacts our ability to assess:

- Whether any increased tax revenue was caused by the MSCTC or may have happened without the program;
- Whether jobs would have been created or retained but for the MSCTC (and any attempt to provide a cost per job analysis, particularly where multiple State programs may be reporting the same jobs); and
- Whether business outcomes were caused by the MSCTC.[16]

Although assessing causation is challenging, gathering information and data on an ongoing basis about the extent to which MSCTC businesses also receive funding from other State economic development programs would provide the Legislature with valuable context to consider alongside business and program outcomes. This could provide a fuller picture of the extent to which State funds (from multiple programs) are used to support individual businesses, which could be considered alongside business outcomes.

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[13] This system is often referred to by stakeholders and participants as an "eco-system".

[14] MTI was created by the Legislature in 1999 (5 MRSA, Chapter 407). It offers grants, loans, equity investments and services to support Maine's innovation economy. https://www.mainetechnology.org/

[15] MVF was created by the Legislature as the Small Enterprise Growth Fund in 1996 (10 MRSA, Chapter 13). It invests in businesses that have the potential for significant growth and impact in Maine. https://www.maineventurefund.com/

[16] The State of Washington Joint Legislative Audit and Review Committee noted the general difficulty with determining causality: *"Determining whether the behavior of private individuals and organizations was caused by a tax preference is an extremely complicated exercise…. Measuring a change in a certain factor, such as employment, may reveal little about what caused this change. A myriad of factors can play into why decisions are made by individuals and organizations. Isolating whether or how much a tax preference influenced these decisions, in an objective and evidence-based manner, is rarely possible."* (Legislative Auditor Report to the Legislature: Guidance for Drafting Performance Statements in Tax Preference Legislation, January 2, 2014)

III. Evaluation Results

OPEGA's evaluation results address program outcomes and design issues across 6 key areas:

- Fiscal and economic impacts;
- Private investment;
- Business development;
- Job creation and retention;
- Municipal tax bases; and
- Innovation.

Each section begins with identifying relevant evaluation objectives, intended beneficiaries, and performance measures as approved by the GOC for the purposes of OPEGA's evaluation.

A. Fiscal and Economic Impacts

Relevant evaluation parameters approved by the GOC
Performance measure: • "Measures of fiscal impact and overall economic impact to the State."

> **From 2010-2020, FAME issued \$42.5 million in tax credit certificates under MSCTC.**

From 2010-2020, FAME issued investors with tax credit certificates totaling \$42,541,781 in exchange for investments made in eligible businesses.[17] The program is designed so that the amount of tax credits issued by the State in a given year is incurred as an actual cost to the State over multiple future years following the issuance of the certificate, ranging from a minimum of four years to a maximum of 15 years. When the State adjusts the overall program cap, the impact to the State budget is not immediate, but rather is spread over future years.[18]

As of May 2021, there continues to be \$4.6 million in available tax credits that could be claimed for investments made in 2020, as neither statute nor rules set a time limit from when the investment is made to when the investor can apply for the credit. This has arisen in 2020 (but not previous years) after the tripling of the annual program cap – in previous years, the annual cap was met during the allocated year. The lack of a time limit to apply for the credit causes some fiscal uncertainty for the State, as there is the potential for credits to be claimed months or years after the investment was made. Additionally, in the event that a credit is claimed by an investor for an investment made months or years prior, it raises the question of whether the credit was a significant driver in the decision to make the investment, or whether it is in effect a windfall. Some states have imposed time limits – for example, the InvestOhio program requires that applications be filed within 60 days of the date of the qualifying investment and within the same state biennium. Colorado's Advanced Industries Investment Tax Credit requires credit applications to be made within 90 days of the investment date.

17 The annual breakdown of issued tax credits is set out in Table 2.
18 The Maine State Tax Expenditure Report 2022-2023 estimates General Fund revenue loss for FY22 of \$6.9 million and for FY23 of \$8.4 million.

The administrative costs for the program are largely cost-neutral, as FAME's administrative costs are offset by program application fees and MRS' administrative costs are absorbed into efforts to process annual tax returns.[19]

- **Existing program data was not adequate to support an estimation of broader economic impacts for the State.**

Economic modelling to estimate broader economic impacts requires accurate data, at a minimum, about direct, permanent jobs and business spending inside the State. OPEGA concluded that the employment data collected as part of the business annual report process for MSCTC are not reliable (see Appendix B for a detailed explanation of employment data concerns) and no data are collected from participating businesses about how investment funds are spent. If the Legislature considers it worthwhile to conduct economic modelling, it would be necessary to collect data on: business sector (identification of North American Industry Classification System, or NAICS, code), reliable direct employment data by year, and direct in-state spending. Additional data, such as wages and revenue, would provide a more precise economic impact estimate.

As described on pages 7-8, an additional challenge would be determining the extent to which any economic impacts are caused by the Seed program, particularly in the context of businesses accessing multiple sources of financial support. Collecting specific data about the extent to which each MSCTC participating business has accessed funding from other State or federal sources would provide additional useful data for analysis.

B. Private Investment: Outcomes and Design Issues

Relevant evaluation parameters approved by the GOC
Program purpose: • "To increase private investment in small new and existing businesses, especially those that experience significant difficulty in the absence of investment incentives in obtaining equity financing to carry the businesses from start-up through initial development."[20]
Performance measures: • "The amount of qualified investment in eligible businesses during the period being reviewed." • "The amount of total investments made in eligible businesses leveraged by the tax credit eligible investments."

19 FAME estimates its annual administrative costs to be about $55,000 per year and that the application fees from 2020 will bring in $64,000 per year.

20 OPEGA focused on the extent to which the program increases investment.

- **From 2010-2020, MSCTC eligible businesses received almost $96 million of qualified investment.**

From 2010-2020, eligible businesses received $95,673,690 in private equity investment from individual investors and PVCFs through the MSCTC program, for a cost of $42,541,781 in foregone tax revenue (see Tables 2 & 3). The table below shows the number of MSCTC investments each year, along with the minimum, average, and maximum amount invested by a single investor in a single business. In 2020, eligible investments ranged from $1,500 up to $1.4 million.

Table 3: MSCTC investment statistics by year 2010 - 2020

Calendar year	Number of investments	Total investments	Minimum investment	Average investment	Maximum investment
2010	95	$8,255,943	$750	$86,905	$1,014,906
2011	69	$4,130,165	$5,000	$59,857	$1,000,000
2012	106	$4,670,030	$4,079	$44,057	$300,000
2013	7	$380,000	$25,000	$54,286	$70,000
2014	13	$729,999	$12,500	$56,154	$106,021
2015	143	$7,596,920	$1,667	$53,125	$500,000
2016	162	$10,104,691	$1,809	$62,375	$1,320,000
2017	89	$10,009,388	$2,500	$112,465	$2,442,500
2018	89	$9,991,423	$5,000	$112,263	$2,000,000
2019	100	$10,212,821	$1,374	$102,128	$2,000,000
2020	307	$29,592,309	$1,500	$96,392	$1,407,041
All Years	**1,180**	**$95,673,690**	**$750**	**$81,079**	**$2,442,500**

Notes: Individual investors might invest in multiple businesses or invest in the same business multiple times in a year.
Source: OPEGA analysis of investment and credit data provided by FAME.

- **Program design provides credits to investors who may already be likely to invest in a business, such as business founders.**

The program design permits business founders to claim the credit for investments in their own business. Individual investors cannot own more than 50% of the business and principal owners, their spouse and specified family members with an existing ownership interest are not eligible. However, this permits business founders, significant minority owners, and employees to receive the tax credit for their investments if they do not meet the definition of a principal owner (see footnote 4 for the definition of 'principal owner').

In two of the businesses receiving MSCTC investment that we interviewed, all investment in the business came from the business founders and no outside investment was sought – this accounted for almost $1.4 million in tax credits over several years. Although permitted, it is unclear whether policymakers intend to incentivize founders to invest in their own businesses, as business founders have an interest in investing in their own businesses whether or not a tax credit is available. Although some business founders might suggest that the MSCTC allows them to invest more in their business than they would have without the tax credit, the Legislature may wish to consider whether this is the type of investment that it intends the MSCTC to target, or whether the intention is to incentivize investment from "arms-length" investors, who are not already closely associated with the business. Some states impose more strict requirements on investors – for example, Kentucky, Wisconsin, Minnesota and Delaware prohibit investors (and their family members) who hold a 20% or more interest in the eligible business, while in New York, the limit is 10% ownership interest. Some states also prohibit employees or contractors of the business from receiving the credit.

➢ **Program design may limit opportunities to attract out-of-State investment.**

We heard from businesses, investors and stakeholders that there is a finite pool of available investment from within the Maine investment community. When a business outgrows in-State funding and intends to continue to grow, it may be necessary to seek investment from out-of-State sources. As the MSCTC is available as a refundable credit to PVCFs, but not to out-of-State individual investors, some businesses and stakeholders that we spoke to suggested that the MSCTC may not be maximizing the opportunity to attract individual investors from out-of-State. We also heard from one business that limiting out-of-State investment to PVCFs can create an artificial barrier, as a group of out-of-State investors formed a qualified PVCF for the sole purpose of getting the credit when investing in the Maine business. If accurate, this suggests that some savvy investors have found ways to access the credit, but it raises the question of whether the limitation of refundability to PVCFs is operating as intended. The Legislature may wish to consider whether the program should specifically target and encourage investment from out-of-State sources, which could be a way to bring additional investment into the State.

➢ **Anecdotal information from interviews with MSCTC businesses suggests that there may be a disincentive to invest in businesses if the credit is not available.**

In some interviews OPEGA conducted with MSCTC businesses, we heard that the existence of the credit may serve as a disincentive to continue to invest in businesses after the credit is no longer available.[21] In years where the annual credit cap was reached, we heard that investors delayed investing until the MSCTC was again available – this results in investments only being available to businesses when it coincides with the timeline of credit availability, rather than the timeline of business need.

In our interviews, we also heard from several businesses that were no longer eligible for the MSCTC (either because they reached their overall investment limit or they exceeded the revenue limit) that their investors who previously used the MSCTC were reluctant or unwilling to invest when the credit was no longer available. One business participant described it as "impossible" to raise money from local investors after the business was no longer eligible for the program. Another business described that the first question investors ask is if the business is still eligible for MSCTC; when the business explains that they are no longer eligible, "it is like throwing a wet blanket over the deal".

Another business reported that the private investment community in Maine thinks of the MSCTC as "half-price investing"; when the credit is no longer available, an investment costs twice as much, which

[21] See Appendix A for more information about the business interview methodology.

can be challenging for a growing business to overcome. Although these comments from businesses were based on experiences when the credit was 50%, the current credit rate of 40% is still at the higher end of credit percentages compared to other states (see Appendix F for a list of other state programs and their credit rates). Participants suggested possible solutions to these challenges, including introducing a phased reduction of the credit to avoid the sudden apparent doubling of the cost of an investment that may act as a disincentive for further investment in a developing business.

➢ **The data used to support a leveraging ratio of 7.7:1 is not reliable.**

On February 18, 2020, FAME provided testimony to the Taxation Committee that stated: "through 2017, participating companies were able to raise almost $271 million of capital using just under $35 million of the credit, producing an impressive leveraging ratio of 7.7 to 1." OPEGA concluded that the data used to determine this leveraging ratio were not sufficiently reliable to warrant concrete conclusions about leveraging.

FAME collects program data on additional investment on the business annual report form.[22] The program data include all businesses that file an annual report, whether or not the business received any eligible MSCTC investments that year, or in any year.[23] In 2018, 31% of the annual reports submitted to FAME (and included in the data) came from businesses that had not yet received any MSCTC investments or the investments had been received more than 5 years prior. In 2017, this number was 46% (see Appendix B for more detail about our concerns with the reliability of the program data).

In our review of the data and comparison with information gained through business interviews, OPEGA identified several concerns regarding the investment data collected by FAME and how the data were presented including:

- The data included investments that came before the MSCTC investment, which indicates that the MSCTC investment could not have caused that investment.
- The data included investment and funding from public or quasi-public sources, such as grants and loans from MTI and equity investment from MTI or MVF.[24]
- The data included investments by principal owners and ineligible family members. This suggests that at least some of the reported investments may have happened regardless of the existence of the credit, rather than being additional investment that was leveraged because of the MSCTC investment.

OPEGA did hear from businesses that the MSCTC investment played a role in meeting matching funding requirements for MTI, MVF, and federal grants. It was not clear whether the businesses would have found a way to meet those requirements through some other means if the MSCTC did not exist.

22 The form asks: "What is the total dollar amount of private investments (whether or not made in connection with the Maine Seed Capital Tax Credit Program) received in [year]?"

23 According to FAME rule, eligible businesses must submit annual reports for the year the business is approved under the program and continuing until four years following the last eligible investment. The reported program data is inclusive of all businesses that returned an annual report, whether or not they received any eligible MSCTC investment that year, or ever.

24 Although the business annual report form asks about "private investments", we observed that some businesses provided figures that included funds from public sources and funds that were not equity investments.

To the extent the MSCTC plays a role in allowing a business to access MTI or MVF funding, it plays a role in leveraging public or quasi-public money. This may be the intention, but it is important for policymakers to have clear and reliable information about the extent to which the funding leveraged is private investment or other public money.

C. Business Development: Outcomes and Design Issues

Relevant evaluation parameters approved by the GOC
Program beneficiaries: • "Small new and existing businesses, especially those that experience significant difficulty in the absence of investment incentives in obtaining equity financing to carry the businesses from start-up through initial development." Legislative findings set out in statute also suggest that the program is intended to target businesses that have the potential for rapid growth and bring capital into the State.[25]
Performance measures: • "The change in the number of businesses created or retained in the State as a result of the credit."

➢ **Program design targets small businesses with annual revenues under $5 million.**

The program design targets small businesses by requiring participating businesses to have annual revenues of less than $5 million. FAME monitors this requirement through the business application process and business annual reporting. OPEGA did not identify any concerns from stakeholders or businesses about this revenue maximum.

An annual revenue limit as a business eligibility criterion appears common amongst other states with similar programs. The $5 million annual revenue limit is within the range used by other states, which have ranges from $500,000 at the lowest end up to $10 million at the highest end. If policymakers wish to consider setting more criteria to further refine the definition of "small" businesses, other criteria that some states have used in various combinations include setting a maximum number of employees (ranging from 20-225) and a cap on business age (ranging from a maximum of 5-10 years up to 20 years for businesses working in a medical field).

➢ **Program design does not address whether the business experiences significant difficulty in obtaining equity financing.**

Despite the program intending to target businesses that experience significant difficulty in obtaining equity financing, there is nothing in the program design that requires businesses to demonstrate this feature. By including this in the program goals, it suggests that the Legislature wants the MSCTC to target businesses that would not have been able to raise equity investment without the availability of the credit. If this is an important or necessary criterion for program participation, consideration should be given to incorporating relevant and meaningful program requirements. Examples of requirements

[25] 10 MRSA §1100-T(1).

imposed by other states include the Delaware Angel Investor Tax Credit and the Minnesota Angel Tax Credit, which both require businesses to not have previously received private equity investment of more than $4 million. The Kansas Angel Investor Tax Credit includes a requirement that funding be otherwise not available on commercially reasonable terms.

- **Program design allows some businesses to benefit that may not be considered to have the potential for rapid growth.**

The program benefits some businesses that appear to be the types that policymakers want to promote, such as renewable energy and aquaculture; however, the program also benefits businesses that it is unclear to OPEGA whether policymakers consider it worth the cost of a tax credit to incentivize.

Published research suggests that programs such as the MSCTC may not effectively target the types of businesses and sectors that are most likely to have strong positive impacts for local economies. The research suggests that although many state programs attempt to limit the program to "high-growth industries", the implementation of the programs allows participation of businesses that do not appear to meet that definition, which can impact the extent to which the program achieves the desired economic outcomes.[26] This accords with OPEGA's observation of how the eligible business categories have been used in the MSCTC, in particular, the categories of visual media production companies, export businesses, manufacturing, and natural resource businesses.

> Visual media production companies: Although visual media production companies are an eligible business category, they do not appear to be businesses that have the potential for rapid growth. The available program data on businesses that were identifiable as film companies suggest they are temporary projects rather than continuing businesses. The business annual reports suggest that they largely employ independent contractors (rather than full-time permanent employees) and report these contracted positions as created jobs. For example, one such business received over $300,000 in tax credits and reported "creating" 123 new jobs; however, it had no ongoing employees and its annual report form described all reported jobs as independent contractors.

> Export businesses: The export category appears intended to support businesses that export products and services out of the State.[27] However, the category is defined in rules and interpreted more broadly. FAME rule defines export businesses as: "*a seller of goods or a provider of services, 60% or more of the customers of which are located or are from out of the State and the employment functions are carried out predominantly within the State.*"[28] OPEGA observed examples of this definition being used by businesses in the tourism/hospitality industry to become eligible for the MSCTC, as they provided evidence of projected sales to customers who are "from out of

[26] Denes et al (2020); Howell and Mezzanotti (2019).
[27] Legislative findings note: "Businesses that export their products or services out of the State bring capital into the State and help to develop export markets for Maine products." 10 MRSA §1100-T(1).
[28] FAME MSCTC Rules, paragraph 3(A)(1)(b).

State," even though the transaction takes place in State.[29] This approach does not appear to align with the intention of exporting products and services out of the State.

Manufacturing and natural resources: Beyond the expected business types that manufacture products or natural resources such as forestry or marine resources, approved MSCTC businesses in these categories include breweries and distilleries. Similar to the export category, OPEGA observed the manufacturing and natural resources categories to be interpreted broadly to include businesses in the hospitality and service industry. This broad interpretation raises questions about whether these are the type of businesses that policymakers consider worth the cost to subsidize investment in, particularly as the businesses in the hospitality and service industries appeared to largely use hourly wage employees.

Although MSCTC benefits some businesses that appear to serve the program's goals, OPEGA observed that the program also benefits some businesses that may not necessarily have the potential for rapid growth, such as film companies and businesses in the tourism and hospitality industries.

- **Business outcome data is not tracked or held on businesses that received MSCTC investment.**

Business outcomes, such as whether a business continues to operate or not, and if so, how well it is performing, are a reasonable metric for monitoring the performance of businesses that have received State support by way of MSCTC investment. FAME does not actively monitor the portfolio of MSCTC businesses to identify if they are still operating. In some cases, a business might return the annual reporting form with a note that it ceased to operate, which FAME notes in its records. In other cases, the business may simply stop returning the annual report form and it cannot be determined from the data whether the business is operating but not returning the form, or whether it has ceased to operate.[30]

Business outcomes are also an area that the Legislature has indicated that it wants more information about, as statute was amended in 2020 to require investors to notify FAME if a business that they invested in using the MSCTC ceases to operate and the likely reasons for the cessation of business.[31] However, this approach relies on investors to report this information and has no effective enforcement mechanism. OPEGA questions whether this will be an effective tool to gather the information that the Legislature appears to be seeking about business outcomes within the portfolio of businesses benefitting from this program.

Caution should be used when seeking to attribute business outcomes (whether positive or negative) to the MSCTC, particularly where a business is accessing multiple sources of State or federal funding programs. Nonetheless, it would be valuable for Legislators to have a better understanding of both

[29] Examples include a hotel franchise and a golf course.
[30] In one instance, OPEGA sought to interview a business that had received investment in 2016; however, the contact information held by FAME was not current and the last successful communication FAME had with the business was when they returned their 2016 annual report. Although the business received eligible investment resulting in over $100,000 of tax credits being issued, neither OPEGA nor FAME were able to contact a representative of the business.
[31] PL 2019, c. 616 (effective March 18, 2020).

business outcomes and other programs that the business has accessed to be able to consider the performance of the overall portfolio of businesses receiving investment through the MSCTC.

D. Job Creation and Retention: Outcomes and Design Issues

Relevant evaluation parameters approved by the GOC
Program goal: • "To increase job opportunities for residents of the State in businesses that export products or services from the State."
Program beneficiaries: • "Jobseekers in the State."
Performance measures: • "The number and geographic distribution of full-time employees added or retained during a period being reviewed who would not have been added or retained in the absence of the credit." • "The amount of the tax revenue loss for each year being reviewed divided by the number of jobs created or retained."

- **Program design does not drive the program goal of increasing job opportunities in <u>export</u> businesses.**

Although a stated program purpose is to increase job opportunities in businesses that export their products and services from the state, exporters are currently only one of five permitted business categories (see Table 1). Of the 29 businesses that received MSCTC investment in 2016, only two were qualified under the export category only and three were qualified under multiple categories, one of which was export. If the Legislature intends for the program goals and design to align, one or both should be changed.

- **Program design does not require creation or retention of employees for businesses to benefit.**

Although MSCTC investments in businesses may contribute to their ability to create or retain jobs, there are no meaningful program requirements around employment. The amount of value a business can derive from the program is not linked to evidence of job creation and retention. As part of the business application process, businesses are required to certify that the amount of investment is necessary to allow the business to create or retain jobs in the State.[32] This is achieved by the business signing a pre-written one sentence statement attached to the investment application. After FAME approves the investment, the investor is granted the tax credit certificate and there are no consequences to the investor or the business if jobs are not created or retained. As the requirement is for the business to make the certification, rather than to actually create or retain jobs, the statutory

[32] PL 2013, c. 438 added the statutory requirement that the business must certify that the amount of investment is necessary to allow the business to create or retain jobs in the State.

requirement does not meaningfully drive employment. It therefore should not be assumed that the program drives increased employment without supporting data.[33]

- **Available program data is inadequate to assess the extent to which businesses create or retain jobs.**

Based on the available program data, OPEGA was not able to assess the extent to which businesses receiving MSCTC investments created or retained jobs. Program data on employment is gathered by way of the business annual report form.[34] In considering the data and comparing the data to the business interviews, OPEGA observed the following concerns with the data:

- The business annual report data about employment contains inconsistencies because there is no common understanding of what constitutes a job that should be reported. Examples of inconsistencies include the following being included in job counts:
    - Independent contractors;
    - Seasonal staff;
    - Individuals working without pay (such as founders); and
    - Vacancies, including positions that are vacant by the employer's choice.
- The business annual report data is incomplete. OPEGA observed that in 2018, 27% of businesses that were required to submit an annual report because they had received a Seed eligible investment did not do so. In 2017, 42.6% of businesses that received a Seed eligible investment did not provide an annual report. (See Appendix B for more information about the data concerns.)

Additionally, while FAME collects employment data at the time of the business application, no additional data is collected at the time of the first MSCTC tax credit – this may contribute to inconsistencies in businesses attempting to identify what is a "created" or "retained" job in their annual reporting. OPEGA concluded that the business annual report data could not be used to provide a reliable measure of employment changes in businesses that received MSCTC investment.

- **Insufficiently reliable data has been used to inform Legislative oversight.**

Having concluded that the business annual report data could not be used to provide a reliable measurement of employment changes, OPEGA evaluated the program data that FAME has provided to the Legislature in the past and concluded that the employment data reported by FAME to the Legislature has not been sufficiently reliable to make concrete assessments of program efficacy.

33 The program is designed to rely on investor decisions. The interests of individual investors might, but not necessarily, align with the State's interests to create jobs. A good investment for an investor could be a business that creates high-quality jobs in Maine or it could be a business that uses few full-time employees in Maine and contracts production outside the State or country.

34 The form asks: "What was the total number of Maine jobs created in [year]?", "What was the total number of Maine jobs retained in [year]?", and "What was the total number of Maine employees employed as of 12/31/[year]?"

For example, in 2020, FAME provided testimony that stated that, through 2017, participating MSCTC businesses created over 3,200 jobs and retained 7,500 jobs, and that in 2018, the program helped to create and retain 870 Maine jobs.[35] OPEGA identified the following concerns with these figures:

- The figures reported included all businesses that returned an annual report, whether or not they received any eligible MSCTC investments that year, or ever.
- The figure cited of MSCTC participating businesses retaining 7,500 jobs is based on a cumulative total of reported retained jobs each year. This approach inflates the number of jobs retained; for example, a single job that is retained and reported each year for 5 years is counted as 5 retained jobs (when the reality is that it is a single job retained for 5 years). It also obscures job losses over time; for example, if a business starts with five jobs and employment declines over the years to zero employees, only the cumulative positive number of jobs is reported (explained in more detail in Appendix B).
- Additionally, OPEGA compared the reported figures to the raw data, which showed 300 fewer "created jobs" (a difference of over 10%) and 1,000 fewer "retained jobs" (a difference of over 13%) than were presented in the testimony. FAME explained that they could not determine how they arrived at the published figures and that it could have been an error in analysis.

Taken together, these three concerns show that the data that has previously been published in support of the program is not sufficiently reliable to conclude as to program outcomes.

➢ **FAME has not consistently complied with statutory reporting requirements.**

Although FAME has provided program information and data as part of testimony around program changes, FAME has not consistently provided the Legislature with annual reports on the MSCTC as required by statute. Statute sets out that businesses are required to report to FAME specified information annually.[36] In turn, FAME is required to report annually to the Taxation Committee on "activity under this section". OPEGA asked FAME for copies of previous annual reports; however, FAME explained that they had not provided a report to the Taxation Committee for several years and were unable to confirm when they last did provide such a report. In October, 2020, FAME wrote to the Chairs of the Taxation Committee and enclosed a spreadsheet with information on program years going back to 1989. OPEGA asked FAME why the report did not include the information that the businesses are required to report to FAME, such as employment, payroll and revenue information. FAME explained that they do not interpret statute as requiring them to report this information to the Legislature. OPEGA notes that this interpretation results in the Legislature not being provided with any ongoing information about program outcomes.

In 2020, the business reporting requirements were expanded and the requirement for FAME's annual report to the Legislature is required to include identification of businesses receiving investments eligible for the MSCTC and FAME's determination as to whether the investments would have been made in the absence of the credit.[37] If the Legislature expects to also receive information and data

[35] Testimony in support of LR 3206 to the Joint Standing Committee on Appropriations and Financial Affairs and the Joint Standing Committee on Taxation (2/18/2020).
[36] See Appendix B for a summary of the business annual reporting requirements.
[37] PL 2019, c. 616.

regarding business outcomes, such as data reported by businesses to FAME, the Legislature should make this expectation clear.

- **Anecdotal information from interviews with MSCTC businesses suggests variable outcomes around job creation and the associated tax credit cost; the Legislature would benefit from more active monitoring and reporting.**

In our limited interviews of businesses, we heard a range of outcomes related to employment following MSCTC investment. This includes both the extent to which jobs are created or retained in participating businesses and the amount of tax credits issued in respect of investments in those businesses. These variable experiences demonstrate that policymakers may benefit from more active monitoring and reporting of business employment outcomes, along with the associated program cost on a per business basis.

The information below is <u>not</u> from a representative sample and should not be used to generalize outcomes across the program, rather it provides examples to show that there is a wide range of employment outcomes (and cost of associated tax credits) amongst businesses receiving MSCTC. Among the eleven businesses we sought to interview:[38]

- Three businesses lost employees, having started with a combined total of 14 employees at the time of their first investment and currently each have zero employees. This represents a net loss of 14 jobs from the time of first investment and a cost to the State of $443,705 in tax credits.
- Two businesses maintained their employment levels at a combined total of 9 jobs.[39] This represents a retention of 9 jobs and a cost to the State of $1,656,166.
- Six businesses increased employment, starting with a combined total of 36 jobs and currently report a combined total of 170 full-time employees. This represents a net increase of 134 jobs and a cost to the State of $7,764,304 in tax credits.

These variable outcomes in a small sample demonstrate the value of policymakers having more systematic information about employment outcomes and costs in businesses receiving investment. This is also supported by recent research that raises concerns about whether investor tax credits achieve their goals of promoting high-growth entrepreneurship – although the authors found that investor tax credits did increase investment, the investment seemed to go to lower-growth businesses and the tax credits often went to inexperienced investors and investors tied to the businesses.[40]

[38] We sought to interview eleven businesses and ultimately spoke to ten. One of the businesses did not appear to be operating in the State of Maine and could not be located.
[39] One of the businesses' employment remained steady; one described having more employees prior to the Covid-19 pandemic and an intention to increase employment in the coming year.
[40] Denes et al (2020); Howell and Mezzanotti (2019).

➢ **Program design does not focus on increasing average wages and no relevant data is collected to allow assessment of this outcome.**

In addition to there being nothing in the program design that requires a business to create or retain jobs to benefit from the program, there is also nothing in the program design that directs program funding towards businesses that are more likely to pay a higher wage.

The MSCTC legislative findings state that the jobs created by the businesses that MSCTC targets "*tend to pay higher wages and offer more benefits than other businesses,*" suggesting that this is a goal of the MSCTC.[41] However, the program does not have any effective design elements that direct investment to businesses that are more likely to create new jobs, or that any jobs created should be at a particular salary or skill level. Currently, the data that businesses are required to report to FAME only relates to the number of jobs and does not include any additional information on the quality of jobs, such as whether they are full-time or part-time, permanent or temporary, salaried or hourly, or include benefits.

From interviews OPEGA conducted with 10 businesses receiving MSCTC investment during the course of 2016, six reported having new positions that still exist. These six described a significant variation in types of jobs:

- The businesses working in science, technology, engineering and mathematics ('STEM') related fields described having a majority of their full-time employees on salaries and a smaller number of hourly employees.[42] These businesses described recruiting early stage engineers from Maine, including those that have completed engineering programs at the University of Maine. They also described actively recruiting mid-career or specialist engineers from out-of-State, who relocated to Maine. Both the salary ranges and the source of employees appears to align with the State's Strategic Plan around increasing wages, growing local talent and attracting new talent to Maine.
- The MSCTC businesses in the hospitality industry, such as a hotels, breweries and distilleries, or other businesses in the tourist or service economy had lower salaries than those businesses that we spoke to specializing in STEM fields – these businesses had largely hourly employees and smaller number of salaried employees.[43]

These observations support the suggestion that using business eligibility requirements for MSCTC could be used to specifically target industries and business sectors more likely to create or retain particular types of jobs. However, the five eligible business categories currently used in the MSCTC are not effective for this purpose, as they include industries that do not appear to support full-time employment (such as film businesses) and the export, manufacturing and natural resources categories are so broad that they allow businesses that pay lower wages to be eligible.

[41] 10 MRSA §1100-T(1).
[42] Engineering or other STEM related positions had annual salaries ranging from $50,000 to $200,000 and hourly wages ranging from $15 to $28 per hour.
[43] Hospitality management positions had annual salaries ranging from $42,000 to $100,000 and hourly employees earning $13 to $20 per hour.

Some states with similar programs include program requirements related to wages. The Minnesota Angel Tax Credit requires businesses to pay employees annual wages of at least 150% of poverty level for a family of four, which for 2021 is $46,375 per year or $22.03 an hour. The Arkansas Equity Investment Incentive program includes a criterion on businesses that they pay 150% of the county or state average wage.

E. Municipal Tax Bases: Outcomes and Design Issues

Relevant evaluation parameters approved by the GOC
Program goal: • "To increase municipal tax bases."

➢ **MSCTC does not have design features which would be expected to increase municipal tax bases and is not set up to collect data to measure such an impact.**

There is nothing in the design of the MSCTC that drives a direct increase to municipal tax bases. To increase municipal tax bases, one would expect a program to include requirements for funds to be used for taxable expenditures, such as:

- purchase of taxable business equipment; [44] or
- make improvements to land or buildings that impact property taxes.

The MSCTC does not require invested funds to be used in these ways. Statute permits MSCTC invested funds to be used broadly, including to cover any business operating expense.[45] If policymakers consider increasing municipal tax bases to be a core goal of the program, the design could be adjusted to align with this goal. Some programs in other states have relevant requirements: the Delaware Angel Investor Tax Credit requires invested funds to be expended on real property, personal property or intangible property; InvestOhio requires the business to have, within 6 months of investment, incurred costs for tangible personal property, motor vehicles, real property, leasehold improvements, or compensation for new employees hired after the date of qualifying investment.

We note that MSCTC may also have indirect impacts on the municipal tax base through increases and decreases in employment, if those changes cause residents to improve properties or purchase items that may be subject to municipal taxation; however, any potential increases to municipal property taxes may also be offset by increased costs that are driven by a greater demand for services by residents.

F. Innovation: Role of MSCTC in State Economic Development Strategy

In addition to assessing the MSCTC program design against its own goals, OPEGA considered how the program fits within the State's larger economic goals.

44 The business would likely be exempt under the Business Equipment Tax Exemption (BETE) from paying personal property tax to the municipality, the municipality may receive a partial reimbursement from the State. Although this represents an increase in revenue for the municipality, it is an increase in cost to the State.

45 The only express prohibition is on using the investment to repay equity investments. 10 MRSA §1100-T(2)(F) and paragraph 3(B)(1) of FAME rules. Of the businesses interviewed by OPEGA, several described using investment funds for the purchase of business equipment and one described using the investment funds for improvements to land.

- **The MSCTC is included in Maine's Statewide Strategic Plan under the strategy related to promoting innovation; however, the program's design does not effectively focus on promoting innovation.**

In November 2019, DECD published the "Maine Economic Development Strategy 2020-2029: A Focus on Talent and Innovation" ('Strategic Plan'). This sets out 10-year goals and strategies to meet the State's economic needs. The goals are:

1. Grow the average wage by 10% to the benefit of all workers at all income levels;
2. Increase the value of what Maine sells per worker by 10%; and
3. Attract 75,000 people to Maine's workforce from within and outside the State.

In order to achieve these goals, the Strategic Plan sets out seven strategies. The MSCTC is specifically mentioned as a tool under the strategy to promote innovation in areas of Maine strength and the Strategic Plan proposed an increase to the MSCTC ceiling from $5 to $15 million with the aim of helping about 40 startups and creating 2,300 new jobs. This increase was implemented by the Legislature and took effect in 2020.

The Strategic Plan identifies Food/Marine, Forest Products, Making/Manufacturing, and Technical Services as areas of Maine strength that will provide a focus for all of Maine's public research and development programs. In contrast, the MSCTC design allows a broad range of businesses to benefit from the program, including those that do not appear to advance innovation, such as film companies and businesses in the hospitality sector.

Other than determining whether a business fits into one of the five eligible business categories in the MSCTC statute, there is nothing in the MSCTC application process that assesses the extent to which a business would contribute to the goal of promoting innovation. There is also no information or data that businesses are required to report that could help to assess the extent to which participating businesses are promoting innovation, such as the number and type of patents that have been applied for and granted to the business.[46]

- **There are opportunities for the MSCTC to more effectively target businesses that promote innovation.**

If the Legislature considers the MSCTC as a tool to promote innovation, there are opportunities to adjust the program design to drive towards this goal. Policymakers may wish to consider whether the eligible business categories (and types of business approved under those categories) align with the State's economic priorities. OPEGA observed that the MSCTC eligible business categories are broader than the seven technology sectors that MTI targets[47] – this suggests an opportunity for more strategic thinking to ensure that State-sponsored supports for start-ups and entrepreneurs works together effectively. Although a broad approach may allow a wide range of businesses to access the

[46] Of the 10 businesses that OPEGA interviewed, two described having patents.
[47] The seven technology sectors that MTI focuses on are: biotechnology, composites and advanced materials, environmental technologies, forest products and agriculture, information technology, marine technology and aquaculture, and precision manufacturing.

program, it may not deliver the results the State seeks, such as jobs with higher wages, greater innovation in Maine businesses, or developing the sectors prioritized in the Strategic Plan. Alternative approaches could include adjusting the business categories to:

- Create a more specific framework for included and excluded business sectors (see Appendix E for examples of how other states have targeted their programs);
- Better align the sectors with other state-sponsored partners, such as MTI and MVF;
- Better align the sectors with the sectors highlighted in the Statewide Strategic Plan.

IV. Opportunities for Improvement and Recommendations

A. Recommended Legislative Action: Goals, Design, and Oversight

The MSCTC tax credit is three decades old and has been amended by successive Legislatures, which may have contributed to the areas of misalignment identified in this evaluation between the program design and the program goals. The areas of misalignment described in Section III are re-capped in the table below.

Table 4: Summary of areas of misalignment between program goals and program design	
Program goals	**Description of misalignment in program design**
Increasing investment	• Program design provides credits to investors who may already be likely to invest in a business. • Program design may limit opportunities to attract out-of-State investment.
Intended business beneficiaries	• Program design does not address whether the business experiences significant difficulty in obtaining equity financing. • Program design allows some businesses to benefit that may not be considered to have the potential for rapid growth.
Increasing employment	• Program design does not drive the program goal of increasing job opportunities in export businesses, or require creation or retention of employees for businesses to benefit. • Program design does not focus on increasing average wages.
Increasing municipal tax bases	• MSCTC does not have design features which would be expected to increase municipal tax bases.
Promoting innovation	• Program design does not effectively focus on the strategy of promoting innovation.
Source: OPEGA analysis.	

With the program cap for annual tax credits having recently been tripled from $5 to $15 million, there is value in taking a strategic look at the program's goals at this juncture. Clearly identifying program goals and desired outcomes provides a framework within which to consider program design changes.

In our discussions with participating businesses, investors and stakeholders, we heard a diverse range of expectations and goals for the program, including that the program is intended to:

- Assist businesses to scale by attracting outside capital and filling the gap between friends, family and founder investment and PVCF investment;
- Attract capital investment from out-of-State;
- Grow businesses to create good quality jobs in the State in order to raise the average wage;
- Facilitate private investment to meet matching fund requirements for MTI and MVF;
- Increase research and development in Maine and help to bring new products to market;
- Increase the number and diversity of private investors in Maine, with a view to building wealth in communities; and
- Improve the perception that Maine is a good place to start a business.

The misalignments between program design and program goals, and the diversity of expectations for the program, suggest that a fresh look at the program goals would be beneficial.

➢ ***Recommendation*: OPEGA recommends that the Legislature, in consultation with FAME, DECD, and other stakeholders as appropriate, re-evaluate and clearly define program goals and what "success" looks like in terms of outcomes. Thereafter, the program design should be adjusted, through amendments to statute or agency rules as appropriate, to ensure the program requirements align with the goals.**

The recommended re-evaluation of program goals and design should include consideration of how the program is intended to fit within the state-funded "eco-system" that exists to support early stage businesses and economic development in Maine. Areas for particular consideration include:

1. **Increasing investment.** Consider the source of investment sought and whether investment is intended to be used for a particular purpose. In particular:
    a. Consider whether a time limit should be placed on when the investor may apply for the credit to allow for better defining of program costs after year-end and to exclude those investments where the passage of time suggests that the credit may not have been a driving factor in the decision to invest;
    b. Consider whether business founders, significant minority owners, and employees should be permitted to receive the credit or whether the intention is to focus on investors who are not already associated with the business;[48]
    c. Consider whether it is a goal of the program to attract out-of-state investment and if so, how opportunities to achieve this can be maximized; and
    d. Consider whether it is a goal of the program to leverage later, non-MSCTC private equity investment and/or public or quasi-public investment through meeting matching funding requirements for programs such as MTI, MVF, or federal research and development grants.

2. **Job creation**: Consider whether there are particular types of jobs that MSCTC is expected to help create, such as jobs in particular sectors, at specific skill levels, or above an identified salary. Although there is a tension in identifying how requirements can be enforced because the credit is given to the investor, rather than the business, some states have found ways to design their programs to be more likely to meet employment goals (see page 22). More focused targeting on particular business sectors may also impact jobs.

3. **Municipal taxes**: Consider whether increasing municipal taxes is a core goal of the program and if so, how it is expected to achieve this (possible approaches are discussed on page 22). If it is not a core goal of the program, adjust the identified program goals to reflect this.

4. **Promoting innovation**: Consider whether promoting innovation is a program goal and if so, how this can be meaningfully assessed as part of the business application process. This could

[48] Consideration could also be given as to whether additional qualifications should be imposed on investors to participate. For example, a number of other states require that investors be accredited by the Securities and Exchange Commission to participate.

be addressed through more focused targeting of eligible businesses and sectors. Possible approaches are discussed in Appendix E.

Following developing a clear definition of the program goals, the program design should be adjusted to focus the design on meeting those goals. Different goals suggest different design features, including different ways of defining the target businesses. For each goal, thought should be given to what success for this program looks like, including what margin of loss is acceptable – as this program targets early-stage businesses that are higher risk and may not succeed, there should be an understanding that loss is an expected part of this program. After the goals are re-defined and the program design is adjusted to align with those goals, the program would benefit from ongoing, pro-active monitoring and oversight to continuously assess whether it is meeting expectations to advance the program's and the State's economic goals.

- ***Recommendation*: OPEGA recommends that the Legislature, in consultation with FAME and DECD as appropriate, adjust the program's reporting requirements to allow for effective oversight of whether the program is meeting its goals.**

Program data collection and reporting should be adjusted to allow for effective oversight of the extent to which the program is achieving its goals. The type of data and information gathered and reported, both by businesses and FAME, should specifically align with the MSCTC's goals. Areas of adjustment could include:

1. **Business outcomes**: Requiring FAME to monitor and report to the Legislature on business "exits", such as when a business has ceased to operate in State or whether it was purchased by a larger entity, including whether that purchase results in operations staying in Maine (and for how long) or moving out of State.

2. **Employment**: Requiring businesses to report more specific information about the types of jobs created after MSCTC investment. This information could include: salary ranges, skill level, and benefits information.

3. **Other State or federal funding received**: Requiring businesses to report on the source and amount of funding received from parts of the "eco-system" and other economic development programs, including MTI, MVF, PTDZ/ETIF, FAME loans, federal research and development grants, private bank loans, and non-MSCTC investors (in and out-of-state).

4. **Indicators of innovation**: Requiring business to report data on measures of innovation, such as pending or granted patents.

In addition to improving monitoring and oversight of MSCTC, this recommended approach to enhanced data collection and reporting requirements could provide the foundation for a more comprehensive approach to tracking the costs and benefits of State investments in businesses through tax incentive and economic development programs and associated outcomes.

B. Recommended Management Action: Data Collection, Analysis, and Reporting

Due to issues with the available MSCTC program data, OPEGA was not able to use these data to provide a quantitative evaluation of program outcomes. In summary, these issues are:

1. The MSCTC business annual report data relating to employment, payroll, and additional investment is reported inconsistently because there is no common understanding, or definitions, of what should be reported for these metrics.
2. The business annual report data is incomplete. We found that businesses fail to report annual report data to FAME and there is no effective enforcement mechanism in place to compel businesses to report.
3. The analysis and presentation of program data by FAME to the Legislature in recent years has been flawed. More attention to data analysis and reporting is needed to ensure the program information reported to the Legislature is more reliable and consistent.
4. Transparency and Legislative oversight of MSCTC has been relatively low. A contributing factor is the lack of ongoing reporting of program data to the Legislature by FAME.

Our specific concerns about the quality and usefulness of the business annual report data collected and reported by FAME is described in more detail in Appendix B.

- ***Recommendation*: OPEGA recommends that FAME improve their processes for program data collection, analysis and reporting.**

OPEGA has identified the following areas for attention and improvement by FAME:

1. **Data collection:** FAME should collect consistent and complete program data from participating businesses, by:
   a. Creating specific guidance for businesses about what information and figures should be included and excluded for each data point required in the annual report. For example, for employment and payroll, the guidance could specify which job-types (full-time, part-time, seasonal, or contractors) should be included or excluded, and for additional investment amounts, guidance could specify which funding sources should be included or excluded;
   b. Gathering baseline data on employment, payroll, revenue and any other relevant metrics at the time of investment for each business; and
   c. Establishing and implementing effective enforcement mechanisms to ensure businesses submit the required annual reports.

2. **Data analysis:** FAME should ensure data analysis provides reliable results and information, by:
   a. Removing from the analysis those businesses that have qualified for MSCTC, but have not yet received eligible investment, so as to ensure that only participating businesses are included in the analysis and reported results; and

b. Analyzing changes (up or down) in reported business outcomes to identify changes to business outcomes following their first MSCTC investment. For example, rather than relying on a business to identify whether jobs were "created" or "retained", a more reliable approach would be for FAME to analyze changes to total employment.

3. **Data reporting:** At a minimum, FAME should consistently comply with the annual reporting requirements to the Legislature as set out in statute and follow-up to ensure that the Legislature has the information it needs to provide effective oversight of the program.

Although the program was set up to be administered in a hands-off way, the substantial increase in the State's investment in the program over time, including the recent tripling of the annual cap on credits, may warrant reconsideration of this hands-off approach to ensure the State tax expenditure is a cost effective and efficient use of resources.

Acknowledgements

OPEGA would like to thank the Finance Authority of Maine for their cooperation throughout this review. OPEGA would also like to thank the Maine Revenue Service, Maine Department of Economic and Community Development, Maine Technology Institute, Maine Venture Fund, along with program stakeholders, investors, and businesses for their cooperation and assistance.

Agency Response

In accordance with 3 MRSA §997(1), OPEGA provided the Finance Authority of Maine and the Maine Revenue Service an opportunity to submit additional comments after reviewing the report draft. The agency response letter can be found at the end of this report.

Appendix A. Evaluation Scope and Methods

Evaluation Scope

On January 24, 2020, the GOC voted to approve the following evaluation parameters, pursuant to 3 MRSA §999(1)(A), which set forth the scope of the evaluation.

Program purpose
(1) To increase job opportunities for residents of the State in businesses that export products or services from the State; (2) To increase private investment in small new and existing businesses, especially those that experience significant difficulty in the absence of investment incentives in obtaining equity financing to carry the businesses from start-up through initial development; and (3) To increase municipal tax bases.
Program beneficiaries
(1) Small new and existing businesses, especially those that experience significant difficulty in the absence of investment incentives in obtaining equity financing to carry the businesses from start-up through initial development; and (2) Jobseekers in the State.
Evaluation objectives Each objective will be addressed to the degree possible based on its relevance, the level of resources required and the availability of necessary data.
(a) The fiscal impact of the tax expenditure, including past and estimated future impacts; (b) The extent to which the design of the tax expenditure is effective in accomplishing the tax expenditure's purposes, intent or goals and consistent with best practices; (c) The extent to which the tax expenditure is achieving its purposes, intent or goals, taking into consideration the economic context, market conditions and indirect benefits; (d) The extent to which those actually benefiting from the tax expenditure are the intended beneficiaries; (e) The extent to which it is likely that the desired behavior might have occurred without the tax expenditure, taking into consideration similar tax expenditures offered by other states; (f) The extent to which the State's administration of the tax expenditure, including enforcement efforts, is efficient and effective; (g) The extent to which there are other state or federal tax expenditures, direct expenditures or other programs that have similar purposes, intent or goals as the tax expenditure, and the extent to which such similar initiatives are coordinated, complementary or duplicative; (h) The extent to which the tax expenditure is a cost-effective use of resources compared to other options for using the same resources or addressing the same purposes, intent or goals; and (i) Any opportunities to improve the effectiveness of the tax expenditure in meeting its purposes, intent or goal.

Performance measures
(1) The number and geographic distribution of full-time employees added or retained during a period being reviewed who would not have been added or retained in the absence of the credit; (2) The amount of qualified investment in eligible businesses during the period being reviewed; (3) The change in the number of businesses created or retained in the State as a result of the credit; (4) Measures of fiscal impact and overall economic impact to the State; (5) The amount of the tax revenue loss for each year being reviewed divided by the number of jobs created or retained; and (6) The amount of total investments made in eligible businesses leveraged by the tax credit eligible investments.

Evaluation Methods

To complete the evaluation, OPEGA obtained program information and data from FAME, businesses and investors participating in the MSCTC program, and information in the public domain. No confidential taxpayer data was obtained for this review.

Data collection and analysis methods included:

- Extensive review of relevant statute and rules, including the history of changes made since the program was enacted, along with testimony and Committee files associated with significant changes;
- Consideration of all program materials and forms;
- Consideration of published research about angel investment and incentivized angel investment programs;
- Research of programs in other states;
- Interviews with FAME, Maine Revenue Services, Maine Department of Economic and Community Development, Maine Technology Institute, Maine Venture Fund, a representative of Maine Angels, and other stakeholders;
- Interviews with a selection of participating businesses covering: business history from creation to date; MSCTC program investments and how the funds were used; other sources of funding, investment and support; changes in business revenue and employment since first MSCTC investment; details of employment, including types of positions and salary ranges. Eleven of the 29 businesses that received investment in 2016 were selected for interview based on a range of factors, including: the nature of the business, whether the current status of the business could be ascertained, amount of MSCTC investment received and the number of years over which it was received, content of business annual reports (if available), and whether the business had received financial support from MTI or MVF or both. Contact was made with 10 businesses and one business could not be located;
- Analysis and summary of program data held by FAME from 1989 to 2020, including comparing the raw data to information presented to the Legislature in testimony;

- Review of a small selection of FAME files, including business and investor applications, business annual reports, and correspondence;
- Research of a sample of participating businesses, including the nature and status of the business, publicly available information and data, all available MSCTC program data about the businesses, and public data and information from other programs, such as MTI and MVF. This research focused on the 29 businesses that received investment in 2016 in order to allow for sufficient time to have passed since that year of investment; and
- Obtaining program costs and offsets from FAME and MRS.

Research cited in this report

- Denes, M., Howell, S., Mezzanotti, F., Wang, X., and Xu, T. (2020). Investor Tax Credits and Entrepreneurship: Evidence from U.S. States. *NBER Working Paper.*
- Howell, S. and Mezzanotti F. (2019). Financing Entrepreneurship through the Tax Code: Angel Investor Tax Credits. NBER Working Paper

Appendix B. Program Data Reliability

The law governing MSCTC requires eligible businesses to submit an annual report to FAME regarding their activities in the State over the calendar year in which the investment occurred and for such additional years as may be required by FAME. In 2020 (PL 2019, c. 616) the Legislature expanded these reporting requirements. Below is a summary of the statutory reporting requirements before and after the 2020 changes.

Table B.1. Summary of business reporting requirements

Business annual reporting requirements before March 18, 2020	Business annual reporting requirements, effective March 18, 2020
• Total amount of private investment received; • Total number of persons employed as of December 31st; • Total number of jobs created and retained; • Total annual payroll; and • Total sales revenue.	• Total amount of private investment received by the eligible business from each investor eligible to receive a tax credit; • Total number of persons employed by the eligible business as of December 31st; • The total number and geographic location of jobs created and retained by the eligible business stated separately for all jobs in the State and for those jobs that would not have been created or retained in the absence of the credit; • Total annual payroll of the eligible business stated separately for all employees in the State and for those employees who would not have been employed in the absence of the credit; and • Total sales revenue of the eligible business stated separately within and outside the State.

Source: OPEGA review of statute.

Given the timing of this evaluation, OPEGA considered the business annual report data gathered by FAME prior to the 2020 statutory expansion of reporting requirements.

The process by which FAME collects and compiles the annual report data from businesses is as follows. Each year, FAME sends out a short annual report form to each approved business, whether or not they have received any MSCTC eligible investment. Once a business returns the completed form, FAME staff enter the data into an Excel spreadsheet. For this evaluation, FAME provided OPEGA with the Excel spreadsheet recording annual report information from 2003 to 2018.

Below we provide additional information and details on the data concerns identified in this evaluation and discussed in the body of the report.

Data Concern 1: MSCTC program data is inconsistent and incomplete

OPEGA identified the following problems with the data:

1. The business annual report data about employment and payroll is inconsistently reported because there is no common understanding of what constitutes a "job" that should be reported to FAME or included in the analysis by FAME. OPEGA observed the following:
    a. Businesses reported independent contractors as "created jobs" and included them in "payroll". For example, one business reported 45 "created" jobs but zero total employees, along with $82,000 in annual payroll, with a note that all payroll payments were "1099 vendor" related.
    b. Businesses reported seasonal staff as "created jobs" and included them in "payroll". For example, one business reported 30 created jobs, 30 retained jobs, and seven total jobs, but noted that the jobs created were seasonal employees in peak season.
    c. Businesses reported individuals working without pay (such as founders) in the count of jobs.
    d. "Created" plus "retained" did not equal "total" jobs, with some reports wholly inconsistent. For example, one business reported 64 "created jobs", two "retained jobs" but only two total employees.
    e. Businesses reported "vacancies" as "employees", some of which were due to the employer's choice. For example, one business reported 23 retained jobs and 23 total employees, but we learned that there were 7 full-time employees, 4 part-time employees and 11 vacancies, 9 of which were by the employer's choice due to economic conditions.

    OPEGA notes that the annual report data is self-reported by businesses and there is no guidance for businesses about what to include or exclude. The result is that businesses are interpreting the reporting requirements differently, resulting in inconsistent data that cannot be reliably used to provide a meaningful analysis of changes in full-time employment over time.

2. The business annual report data (for all requested data fields) is incomplete due to lack of reporting and no effective enforcement mechanism to compel businesses to submit the annual reports. OPEGA observed that in 2018, 27% of businesses that were required to submit an annual report because they had received a Seed eligible investment did not do so. In 2017, 42.6% of businesses that received a Seed eligible investment did not submit an annual report.

    Although the program statute permits FAME to revoke credits from investors for the failure of a business to provide an annual report, FAME explained to OPEGA that it has not used this enforcement mechanism because it would punish the investor for the actions of a business over which the investor does not have control. FAME described that, instead of revoking credits, they do not allow a business to obtain further investment if the business has not met the annual reporting requirements; however, OPEGA observed instances where businesses had not returned a report but still received investment in a future year. FAME explained that they may consider adopting a clear internal policy that creates a hard and fast last deadline for reports after which no credits will be processed; however, FAME also noted that the fact that most investment applications are received at the start of the calendar year makes it more difficult to accurately and fairly enforce this approach.

Data concern 2: FAME analysis and presentation of program data has been flawed

OPEGA identified several problems with the way FAME analyzed and reported MSCTC data to the Legislature in its February 18, 2020 testimony to the Taxation Committee:

1. FAME reported figures about investment, jobs, payroll and revenue included data from businesses that had not yet (or, in some cases, ever) received MSCTC investment. In 2018, 31% of reports were from businesses that had not yet (or ever) received MSCTC investments or the investments had been received more than 5 years prior. In 2017, this number was 46%.

   According to FAME rule for MSCTC, eligible businesses must submit annual reports for the year the business is approved and continuing until four years following the year the last tax credit certificate is issued. Businesses often apply for program eligibility years before they receive their first Seed eligible investment. Some businesses never receive an eligible investment. Approved businesses complete and return annual reports with the required information about investment, jobs, payroll and revenue. FAME adds every annual report received into the same spreadsheet, which is used to add up cumulative figures and report program data. The reported program data is based on all businesses that returned an annual report, whether or not they received any eligible MSCTC investment that year, or ever.

2. FAME reported figures on retained jobs in a way that did not disclose that there are redundancies that lead to overstating the number of jobs actually retained. OPEGA identified that the figures cited of MSCTC participating businesses retaining 7,500 jobs is based on a cumulative total of reported retained jobs each year. Counting each retained job each year has the following effects:
   a. It suggests a much higher number of retained jobs than reflects the number of unique jobs. For example, if a business has one job and retained it for five years, this method of calculation would show 5 "retained" jobs. This is demonstrated with the following hypothetical example.

Table B.2: Business A example	
Report year	Reported retained jobs
2013	1
2014	1
2015	1
2016	1
2017	1
Total	5

This approach suggests 5 "retained" jobs, when it is more accurately described as one job retained for five years.

b. It does not disclose job losses that appear over time. For example, if a business has five jobs and gradually losses employees over time, these losses are not identified and only positive numbers are counted and presented as part of the cumulative total. This is demonstrated with a hypothetical example below.

Table B.3: Business B example	
Report year	Reported jobs retained
2013	5
2014	4
2015	3
2016	2
2017	1
Total	15

This approach suggests 15 retained jobs, when the business has lost four jobs.

3. In addition to the previously identified concerns, the data FAME reported on created and retained jobs was higher than what OPEGA found in the raw data (even taking into account the calculation methods described above). Using the cumulative total approach (which is described in paragraph 2 above) OPEGA's calculations of the reported figures showed 300 fewer created jobs and 1,000 fewer retained jobs. FAME was asked to explain how they arrived at the figures provided in the testimony and they said they could not determine how they arrived at the figures and that it could have been an error in analysis.

Oversight concern: FAME has not consistently complied with statutory reporting requirements

FAME has not consistently provided the Legislature with annual reports on the program as required by statute. Statute sets out that businesses are required to report to FAME specified information annually and, in turn, FAME is required to report annually to the Taxation Committee on program activity. OPEGA asked FAME for copies of previous annual reports; however, FAME explained that they had previously provided the reports, but had mistakenly not provided a report to the Taxation Committee for the past several years and were unable to confirm the last year they did provide such a report.

In October, 2020, FAME wrote to the Chairs of the Taxation Committee to explain that they had not provided reports for several years and enclosed a spreadsheet with information on program years going back to 1989. For each year, the following information was provided:

- Amount of tax credits issued;
- Amount of eligible investment;
- Number of businesses with investments;
- Number of investors;
- Number of credits issued; and
- Number of venture capital funds.

OPEGA noted that the report did not include information on businesses outcomes that the businesses are required to report to FAME, such as employment, payroll and revenue information and asked FAME why those were not included. FAME explained that they do not interpret statute (which requires a report on "activity under this section") as requiring them to report the employment, payroll and revenue information to the Legislature. OPEGA notes that this interpretation results in the Legislature not being provided with regular, ongoing information about program outcomes.

OPEGA also notes that the new reporting requirements enacted in 2020 (PL 2019, c. 616) may pose challenges to FAME providing the information sought. In particular, the new statute requires:

a. Businesses to report in the year in which the investment occurred <u>and</u> for each additional year for which a credit is claimed. FAME explained that they have no way of knowing how long an investor may be claiming a credit for a particular business and therefore it is not a feasible requirement to enforce.
b. FAME to include in its annual report to the Taxation Committee a determination as to whether the investments would have been made in the absence of the credit. FAME explained that they are likely to ask businesses as part of the annual reporting process to make this determination as FAME will have no basis upon which to assess this on their own.

Appendix C. Total Investments Between 2010 and 2020 by Business

This table lists the 134 businesses that received investment through the MSCTC program between 2010-2020.[49] It is sorted from largest cumulative investment to smallest and includes the amount of MSCTC credits that were issued to investors associated with these investments. Many businesses receive multiple investments from different investors across multiple years. Some of these businesses may have received MSCTC investment prior to 2010 – these figures are not included.

Table C.1: Investment and credits by business for 2010-2020

Business name	MSCTC investments	MSCTC credits issued
Pika Energy	$4,999,996	$2,529,998
Cerahelix	$4,434,772	$1,556,718
Madison ESS (fka New England Battery Storage)	$4,000,000	$1,998,400
Constant Energy	$3,835,000	$1,429,521
DAVO	$3,677,041	$1,518,455
STARC Systems	$3,342,500	$1,671,250
Lighthouse Imaging	$3,193,279	$1,440,138
My Health Math	$3,033,000	$1,292,144
NBT Solutions	$2,466,217	$1,042,318
OURLY Help	$2,427,510	$1,059,829
Ovation	$2,392,443	$656,977
Reconnect	$2,372,102	$923,578
Maine Fiber Company Equity, LLC	$2,309,696	$923,878
Kennebunk Port Hotel	$2,305,147	$1,095,221
GO Lab	$2,300,000	$860,535
Biovation (Grow-Tech / MCLH)	$2,152,360	$947,150
Peregrine Turbine	$1,735,483	$825,725
Polymer Labs	$1,730,993	$692,397
Ocean Approved	$1,617,283	$771,811
TrakTec, LLC	$1,605,000	$848,000
Academic Merit	$1,565,000	$732,500
Coastal Ventures III (20%)	$1,550,000	$620,000
Maine Craft Distilling	$1,494,601	$747,173
Wentworth Technology	$1,477,302	$708,451
Dream Local Digital	$1,276,571	$637,906
Amplify	$1,262,000	$439,655
Course Storm	$1,256,967	$611,728
Launch Security	$1,225,000	$532,356
Gelato Fiasco	$1,201,715	$660,427
R.e.d.d., Inc	$1,133,058	$566,529
Laboratory Feeds of Maine	$1,100,000	$550,000
American Unagi	$1,068,251	$388,740
Hyperlite Mountain Gear	$1,029,580	$514,790

49 This list is inclusive of at least one PVCF that received investment under prior rules permitting this.

Business name	MSCTC investments	MSCTC credits issued
Rainmaker Spring Water	$949,667	$403,467
Mobile Price Card	$877,798	$398,209
Direct Vet Marketing, Inc.	$694,106	$265,303
Nearpeer	$657,000	$249,631
Two Tides Entertainment	$645,000	$301,000
Junora	$640,000	$306,000
Math & Problem Solving	$610,000	$251,395
HighByte	$600,000	$222,531
Nu Holding, LLC	$600,000	$300,000
Mingle Analytics	$575,000	$287,500
AboGen	$571,309	$285,605
Zylo Media	$547,500	$317,500
Novia Products LLC (dba Scentovation)	$520,000	$270,000
PTT Distributed Energy	$500,000	$250,000
Standard Biocarbon	$500,000	$200,000
Maine Grains, Inc. (aka Somerset Grist Mill, LLC)	$480,000	$257,960
Kadabra, Inc. (fka Veebie; aka Minnow Technologies)	$450,000	$225,000
NorthStar Brand	$445,000	$214,813
RockStep Solution	$440,000	$180,438
Acadia Harvest, Inc.	$431,633	$215,817
Comfortable Waters	$425,000	$147,156
Forager	$406,123	$188,864
Oxbow Brewing	$405,000	$172,000
Farming Fungi	$391,000	$195,372
Dairy Forge	$355,000	$177,500
FPN, LLC	$353,429	$141,372
Sonic Blue	$302,788	$124,621
Entosense	$300,000	$149,760
Lifethereal, LLC	$300,000	$140,000
Maine Distilleries	$280,366	$117,047
Union Atlantic Electricity	$280,000	$142,400
MVP Aero	$270,000	$135,000
Pelletco, LLC	$255,000	$153,000
Maine Shellfish Technologies	$250,000	$125,000
Howell - MSI, Inc.	$247,900	$99,160
DMC	$245,500	$112,705
OpBox LTD	$242,092	$96,837
Bigelow Mountain Part.	$211,377	$88,564
Chimani	$210,000	$100,300
Wassail, LLC (dba Maine Mead Works)	$210,000	$91,000
Battery Steele Brewery	$205,000	$102,500
Sea Hag Seafood, Inc.	$200,000	$120,000
Demers Food Group	$195,000	$97,500
GLOBECo	$195,000	$92,888

Business name	MSCTC investments	MSCTC credits issued
The Witch Files, LLC	$178,000	$89,000
Med Rythms, Inc	$176,072	$80,536
Orono Sepectral Solutions	$170,100	$77,788
Montecito Roadhouse, Inc.	$160,800	$69,280
Newfield Design, Inc.	$154,997	$92,998
ArchSolar	$150,000	$75,000
Lil Squirts	$150,000	$75,000
Double Blue Sport	$145,000	$72,500
AMS, LLC (dba Gagne Foods)	$145,000	$58,000
Maine Lee Technology Group	$140,022	$70,011
Gladstone's Under The Sun	$137,500	$82,500
L&K Manufacturing	$135,000	$64,000
Sea Bags Holdings	$130,000	$65,000
Trundy Point	$130,000	$65,000
40 West, LLC	$127,500	$51,000
Pumpspotting	$125,000	$50,000
The Landing at Pine Point, LLC	$125,000	$50,000
Savilinx	$110,000	$55,000
Vertical Harvest	$105,124	$42,050
Blue Ox Malthouse	$100,000	$50,000
Cerealus	$100,000	$50,000
Northern Farms	$100,000	$50,000
Northern Girl	$100,000	$55,000
Ocean Renewable Power	$100,000	$50,000
Sustainability Metrics	$100,000	$50,000
Planetary Emissions Management, Inc.	$100,000	$60,000
Biofine Development	$100,000	$40,000
Businesses that each received MSCTC investments of less than $100,000 (with associated credits of less than $36,000) from 2010-2020:		
Maine Cedar Log Homes (dba MCL Corp) Abierto Networks, LLC Crushroom Gulf of Maine Sashimi Heightened Benevoltek Good To-Go Integrity Composites, LLC Concert Rat, Inc. Energy Circle, LLC Resilient Communications Corp. VitaminSea, LLC Onside Compliance Monopol Films Northern Maine Distilling Co.	Tootie's Tempeh Maine Scallop Co. American Whirlwind Pictures, LLC Maine Crisp Co. Energy By Waste, Inc. Starflight 4 Pure Lime Island Scallop Co. Maine Shellfish Developers Total Relations Management Solution, Inc. Holly Star Production Zeomatrix, LLC Green Ridge Partners S, LLC Indian Meadow Herbals, LLC Green Ridge Partners H, LLC	
Total	**$95,673,690**	**$42,541,781**

Source: OPEGA analysis of investment and credit data provided by FAME.

Appendix D. Consideration of Changes to Aggregate Investment Limit

In March 2020, the State reduced the maximum lifetime limit of MSCTC investment per business from $5 to $3.5 million (PL 2019, c. 616; effective March 18, 2020). In 2021 a bill was introduced that proposed increasing the per business maximum lifetime limit of MSCTC investment to $6 million. This bill, LD 229 ("An Act to Increase Investment Caps in the Maine Seed Capital Tax Credit Program"), was referred to the Taxation Committee. During deliberations on this bill in April 2021, the Taxation Committee invited OPEGA to consider the recently enacted and proposed changes to the maximum lifetime limit on MSCTC investment per business. This appendix responds to that request.[50]

Using data available from FAME, OPEGA looked at the number of businesses that would have exceed the $3.5 million cap per business investment cap had it been in place from 2010-2020. We found that five businesses out of 134 participating businesses (3.7%) received MSCTC investment of more than $3.5 million, but less than the $5 million cap in place during that period. Of these five businesses, OPEGA is aware that two businesses had a "successful exit", meaning that the business was acquired by another, larger entity. In addition to the five that exceeded $3.5 million, there were three businesses with investment amounts approaching the $3.5 million per business investment limit (see Appendix C).

OPEGA understands that the reasoning for the reduction of the per business investment limit in 2020 from $5 to $3.5 million was to spread the available investment dollars among a larger number of businesses. Whether this is an effective strategy largely depends on how the goals of the program are defined by policymakers. If a program goal is to give a larger number of businesses the opportunity to benefit from the credit, even if the amount of per business investment is less, then instituting a lower per business cap is logical. However, if a goal of the program is to increase the number of businesses that are able to scale up into larger entities and enterprises, it may be beneficial to have a larger per business investment cap (OPEGA heard from businesses that it takes a significant amount of funding to successfully scale a business). OPEGA notes that higher or lower per business investment limits each have risks and trade-offs. Spreading the credit and associated investment to many businesses in smaller amounts risks diluting the impact of the credit, while focusing a significant amount of State funding in a smaller number of individual businesses risks total loss if the businesses are ultimately unsuccessful.

In this report, OPEGA also notes some concerns expressed by businesses about the impact of not being able to access the MSCTC program upon hitting the investment limit. One business suggested that there be a more gradual decrease in the credits that could be made available to investors as a business reaches identified cut-off points such as the overall investment limit (see page 13).

[50] LD 229 (as amended by Senate Amendment A to Committee Amendment A) was passed to be enacted by the House and Senate and was signed by the Governor on July 8, 2021.

Appendix E. Targeting Credits to Business Categories - Examples from Other States

Below we provide examples of ways that some states have designed similar tax expenditure programs with regards to targeting types, or categories, of businesses. These examples are not presented as model programs, but rather presented to provide context around alternative approaches to targeting credits.

- **Colorado Advanced Industries Investment Tax Credit.** This program includes a criterion that the business must manufacture an advanced technology and influence one or more of Colorado's advanced industries, which include advanced manufacturing, aerospace, bioscience, electronics, energy and natural resources, infrastructure engineering, and information technology. When determining if a business is in an advanced industry, the administering agency will look at the following factors:
  - Is the company advancing the industry or advancing the state of the art?
  - What is the company's intellectual property strategy?
  - Do they hold or are they applying for patents, or do they have trade secrets?
  - Does the company perform Research & Development?
  - What percent of employees are in STEM-related fields?

- **Tennessee Angel Tax Credit.** This program requires that businesses be an innovative small business with high-growth potential, received small business innovation research or small business technology transfer funding, or is commercializing technology developed at a Tennessee-based research institution. For the first criterion, the agency uses a variety of factors to determine whether a company is an "innovative small business with high growth potential," including:
  - Business model;
  - Ability to scale;
  - Nature of innovations;
  - Market size;
  - Nature of competition;
  - Management team; and
  - The likelihood of obtaining institutional capital for later funding.

  The business cannot be a professional service firm and cannot be primarily engaged in the provision of goods or services in any of the following industries: construction, leisure, hospitality, retail, real estate, insurance, banking, lobbying, consulting, alcohol or gambling.

- **Wisconsin Qualified New Business Venture Program.** This program requires businesses to be engaged in, or committed to engage in, innovation in any of the following:
  - Manufacturing, biotechnology, nanotechnology, communications, agriculture, or clean energy creation or storage technology.
  - Processing or assembling products, including medical devices, pharmaceuticals, computer software, computer hardware, semiconductors, any other innovative technology products, or other products that are produced using manufacturing methods that are enabled by applying differentiating technology.
  - Services that are enabled by applying differentiating technology.

  The business must be undertaking pre-commercialization activity related to differentiating technology that includes conducting research, developing a new product or business process, or developing a service that is principally reliant on applying a differentiating technology.

  The business must not be primarily engaged in real estate development, insurance, banking, lending, lobbying, political consulting, professional services provided by attorneys, accountants, business consultants, physicians, or health care consultants, wholesale or retail trade, leisure, hospitality, transportation, or construction, except construction of power production plants that derive energy from a renewable resource.

Appendix F. Credit Level for Similar Programs in Other States

In this appendix we provide contextual information for reference about the credit level, as a percentage of investment, in other states with similar programs to MSCTC. The level of the MSCTC has varied throughout the program's history and has been as high as 60%. From 2014 to March 2020, it was 50%. From March 2020, the credit was reduced to 40%. Below is a table showing a snapshot of information about the credit level of programs in States with active tax credit programs similar to MSCTC, based on research conducted by OPEGA in 2020-2021. We note that this is a point in time snapshot as states frequently amend these programs.

Table F.1: Credit level of other state programs

State	Program name	Credit percent
Arkansas	Equity Investment Incentive	33.3%
Arizona	Angel Investment Small Business Capital Investment	35% for small rural or bioscience company 30% for other qualified small businesses
Colorado	Advanced Industries Investment Tax Credit	25% standard or 30% if in an enterprise zone
Connecticut	Angel Investor Tax Credit Program	25%
Delaware	Angel Investor Tax Credit	25%
Illinois	Angel Investment Credit Program	25%
Indiana	Venture Capital Investment Tax Credit	20%
Iowa	Angel Investor Tax Credit	25%
Kansas	Kansas Angel Investor Tax Credit	50%
Kentucky	Kentucky Angel Investment Act Program	40% or 50%, depending on the county
Louisiana	Angel Investor Tax Credit	25%
Massachusetts	Angel Investor Tax Credit	20% or 30%, depending on the municipality
Maryland	Biotechnology Investment Incentive Tax Credit	50%
Minnesota	Angel Tax Credit Seed Capital Investment Credit Program	25% 45% (targets border cities)
New Jersey	Angel Investor Tax Credit Program	20% (plus 5% for a business in a qualified opportunity zone, low-income community, or minority or woman owned business)
New Mexico	Angel Investment Credit	25%
New York	Qualified Emerging Technology Company Capital Tax Credit	10% if investment not disposed of within 4 years 20% if not disposed of within 9 years
North Dakota	Seed Capital Investment Tax Credit Program Angel Investor Investment Credit	45% 25%-35% (pooled angel funds)
Ohio	InvestOhio	10%
South Carolina	High Growth Small Business Job Creation Act	35%
Tennessee	Angel Tax Credit	33% or 50%, depending on the county
Utah	Technology and Life Science Investment Tax Credit	Up to 35% over a 3 year term (year 1 - 10%, year 2 - 10%, year 3 - 15%)
Virginia	Qualified Equity and Subordinated Debt Investments Credit	50%
Wisconsin	Qualified New Business Venture Program	25%

Source: OPEGA research.

Appendix G. Extracts from Maine Economic Development Strategy 2020-2029

<table>
<tr><th colspan="2">10 Year Goals</th></tr>
<tr><td colspan="2">(1) Grow the average wage by 10% to the benefit of workers at all income levels</td></tr>
<tr><td colspan="2">(2) Increase the value of what Maine sells per worker by 10%</td></tr>
<tr><td colspan="2">(3) Attract 75,000 people to Maine's workforce from within and outside the State</td></tr>
<tr><th>Major Needs</th><th>Strategies</th></tr>
<tr><td rowspan="4">(1) Draw More Workers to Workforce</td><td>Private sector, non-profits, tourism industry and State will work together to brand Maine as a great place to live</td></tr>
<tr><td>Draw foreign immigrants to Maine with programs that support credential acceptance and support housing and transportation needs</td></tr>
<tr><td>Programs to move 100,000 Mainers of working age who are not in the workforce into the workforce</td></tr>
<tr><td>Expand and simplify debt relief programs such as the Educational Opportunity Tax Credit</td></tr>
<tr><td rowspan="5">(2) Increase Innovation for Economic Growth</td><td>Capitalize on growth of renewable energy sources</td></tr>
<tr><td>Pursue opportunities for sustainable fishing, such as aquaculture</td></tr>
<tr><td>Grow the support services for the aquaculture industry including fish vaccines, testing for exports, and veterinary support</td></tr>
<tr><td>Continue growth of bio-based alternative products</td></tr>
<tr><td>Invest in research and development using existing entities such as the Maine Venture Fund, Maine Technology Institute, and the Finance Authority of Maine</td></tr>
<tr><th colspan="2">Opportunities
Chosen based on Maine's current strengths, global demand, and the potential for job creation</th></tr>
<tr><td rowspan="3">Bio-Based Alternatives (using Forest Products and Manufacturing)</td><td>Advanced Building Materials</td></tr>
<tr><td>Bioplastics</td></tr>
<tr><td>Biofuels</td></tr>
<tr><td rowspan="4">Create Solutions for Climate Change (using Technical Services and Manufacturing)</td><td>On/Offshore Wind Power</td></tr>
<tr><td>Tidal Power</td></tr>
<tr><td>Battery Development</td></tr>
<tr><td>Solar Development</td></tr>
<tr><td rowspan="4">Safe, Climate-Responsible Food Source (using Food Systems and Marine Resources, Manufacturing and Technical Services)</td><td>Aquaculture</td></tr>
<tr><td>Finfish Veterinary Services</td></tr>
<tr><td>Shellfish Vaccines</td></tr>
<tr><td>Testing for Exports</td></tr>
</table>

<table>
<tr><th colspan="2">Strategies</th></tr>
<tr><td rowspan="4">Strategy C: Promote Innovation in Areas of Maine Strength*</td><td>Action C1: Increase R&D Investment Levels in Maine
Create a combination of public subsidies, tax incentives, and higher education investments to partner with the private sector and lift R&D expenditures and investments</td></tr>
<tr><td>Action C2: Raise the Investment Cap of the Maine Seed Capital Credit
Increase ceiling from $5 to $15 million to help about 40 startups and create 2,300 new jobs</td></tr>
<tr><td>Action C3: Revitalize the Maine Innovation Economy Advisory Board
Board brings together major private, nonprofit and public research organizations in Maine; will provide oversight and coordination to State's overall effort to ensure that funds are targeted to areas that translate into new and profitable business growth</td></tr>
<tr><td>Action C4: Promote Exports in Order to Strengthen the Climate for Startups
Expand the work of the existing Maine International Trade Center; develop a domestic exports program</td></tr>
</table>

*The Strategic Plan identifies Food/Marine, Forest Products, Making/Manufacturing, and Technical Services as areas of Maine strength that will provide a focus for all of Maine's public research and development programs (14 & 28).

Appendix H. Performance Measures

OPEGA has integrated the consideration and discussion of identified performance measures (see Appendix A) throughout this report. For references, we provide a summary table documenting the extent to which OPEGA was able to quantify specific performance measures.

Table H.1: MSCTC performance measures as set by the GOC

Performance measure	Result (where available)	Additional information
The amount of qualified investment in eligible businesses during the period being reviewed.	Qualified investment: $95,673,690 (2010-2020)	See Table 2 (page 7) and Table 3 (page 11) for additional information.
The number and geographic distribution of full-time employees added or retained during a period being reviewed who would not have been added or retained in the absence of the credit.	Insufficient reliable data available to calculate jobs-related measures.	Information on the difficulty with attributing job creation or retention to this program is on pages 7-8.
The amount of the tax revenue loss for each year being reviewed divided by the number of jobs created or retained.	Tax credit certificates issued: $42,541,781 (2010-2020)	Information and context about jobs obtained through interviews with individual businesses are on pages 20-21.
The change in the number of businesses created or retained in the State as a result of the credit.	Numbers of unique businesses receiving qualified investment: 134 (2010-2020) Insufficient data available to identify how many businesses continue to operate.	Information on the difficulty with attributing business outcomes to this program is on pages 7-8. The full list of businesses and their associated MSCTC credits and investments is listed at Appendix C.
Measures of fiscal impact and overall economic impact to the State.	Tax credit certificates issued: $42,541,781 (2010-2020). Administration costs: neutral. Insufficient data available to conduct economic modelling.	Information on the difficulty with attributing economic impacts to this program is on pages 7-8 and the information required for economic modelling is on page 10.
The amount of total investments made in eligible businesses leveraged by the tax credit eligible investments.	Insufficient reliable data available to calculate this measure.	Information on this measure is on page 13.

Source: OPEGA analysis.

FINANCE AUTHORITY OF MAINE

July 27, 2021

Lucia A. Nixon, Ph.D, Director
Office of Program Evaluation & Government Accountability
Maine State Legislature
82 State House Station
Room 104, Cross State Office Building
Augusta, ME 04333-0082

Dear Ms. Nixon:

Thank you for providing us with the opportunity to review and comment on your office's report on the Maine Seed Capital Tax Credit Program. We enjoyed working with Ms. Ricci and other members of your staff over the past year and one-half and hope you found FAME to be cooperative, responsive, and helpful in sharing information regarding the program and our association with it over many years.

The report's findings and recommendations are gratefully appreciated, and we look forward to working collaboratively to improve the program. We believe the credit is an invaluable program in Maine's economic development offerings and have often received such feedback from both the benefitting companies and investors alike. The program has meant a great deal to their companies' growth and success.

As noted in the report, with economic development incentives it can be very difficult to attribute a particular investment directly to a specific incentive versus the overall collective offering of various incentives, such as those offered by our partner organizations, the Maine Department of Economic and Community Development (DECD), the Maine Technology Institute (MTI), and the Maine Venture Fund (MVF), all of which may collectively help to drive investor activities. Further, as we consider possible modifications to the program, we should bear in mind the desired precision of data and results may impose additional burdens on the companies and investors involved, as well as serve as potential disincentives for them to participate at all.

FAME takes seriously its role as administrator of the program and welcomes suggestions for improvement. While we believe there are many positive things to say about the program and our customers who have benefitted from it, this important review has exposed deficiencies and shortcomings on our end which we must and will address going forward. The program has grown and evolved over the years and clearly would benefit from additional staff resources and attention to data collection and reporting details. If the various recommendations for improving our record-keeping and reporting are implemented, we likely will require additional resources to perform these duties.

We look forward to working with you, the Legislature, our economic partners such as DECD, Maine Revenue Services, MTI, and MVF, as well as members of Maine's business community and angel investor and venture capital communities, to improve and strengthen the program.

We welcome the opportunity to discuss further with the Government Oversight Committee the report and our experiences over the years in administering the Maine Seed Capital Tax Credit Program.

Sincerely,

Carlos R. Mello

Carlos R. Mello
Acting Chief Executive Officer

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