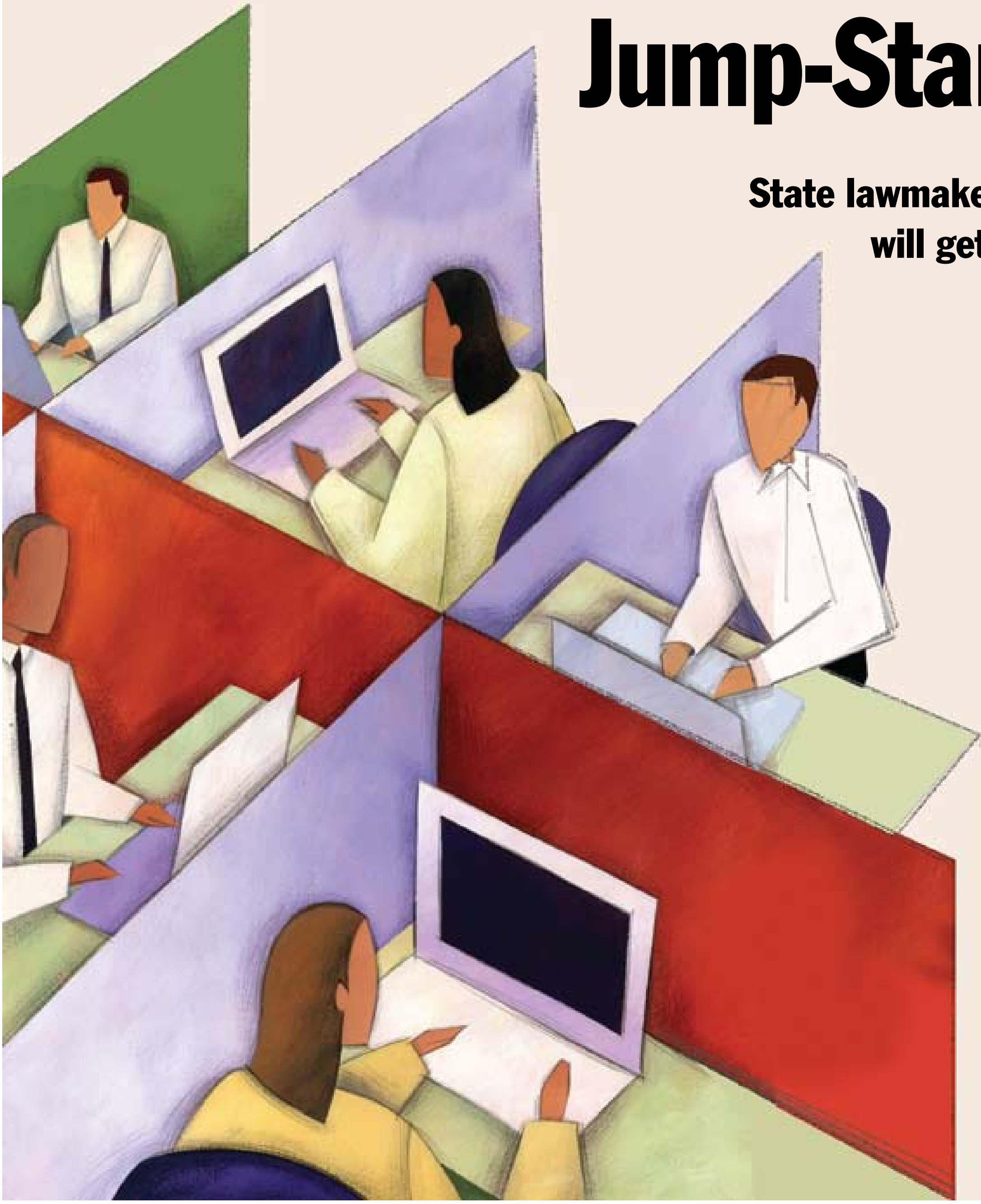
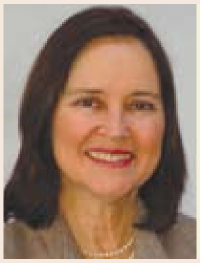


Jump-Starting Jobs

State lawmakers are hoping tax credits will get small businesses hiring.

"We weren't going to become the center of innovation by having an economic development strategy that focused on luring one big box store at a time. Instead, we focused on supporting the human talent that we already have and investing in entrepreneurs."

—CONNECTICUT MAJORITY LEADER DENISE MERRILL



MAJORITY LEADER
DENISE MERRILL
CONNECTICUT

BY LUKE MARTEL

The recession ended 18 months ago, but you wouldn't know it by looking at the jobless numbers. The national unemployment rate is nearly 10 percent, and a handful of states are facing jobless rates of 12 percent or higher.

"We're not Europe," says economist William Strauss of the Federal Reserve Bank of Chicago. "We're not comfortable being in this position."

Luke Martel tracks economic development issues for NCSL.

Across the nation, economists agree that job creation is the key component to a sustained economic recovery. And there's the obvious benefit to state economies from more workers—but the stakes are even higher.

Job creation can be costly—either in direct expenditures to companies for creating jobs or foregone revenues from tax credits—so passing any legislation with a price tag is challenging in an era of scarce fiscal resources. And is it a good return on investment?

The hope that the return exceeds the investments has led to support for new programs, especially job creation tax credits for businesses. Employers receive these credits when they create and fill a new job, so the programs offer tangible benefits. States also expect that the return—in terms of the new employee's income taxes and renewed spending—will at least meet or exceed what the state loses in revenue directed to the credits.

The tax credit programs differ, but they all provide a tax benefit to an employer for hiring someone in a newly created position. Other features can include the following:

◆The employer must hire someone who is, or has been, drawing unemployment benefits.
◆The position is full time, pays a specified

HOW THE CREDITS WORK

At least nine states started new job creation tax credit programs in 2010.

◆ **Alabama:** Businesses can deduct up to 50 percent of the wage of each new hire who stays at least a year, was drawing unemployment or whose benefits had expired.

◆ **California:** Small businesses that show a net increase in full-time employees from the previous year can deduct up to $3,000 for each new employee hired in 2009 and 2010. There is a cap of $400 million on the total amount of credit available.

◆ **Connecticut:** Small business can claim a tax credit up to $200 a month for each new employee who is a state resident. Businesses that hire residents with physical or mental impairments also can claim a tax credit. There is a cap of $11 million on the total amount of credit available.

◆ **Florida:** Manufacturing, financial and service industries can receive a $1,000 corporate income tax credit for every employee hired who earns at least 185 percent of the federal poverty rate. Most retail and food service industries are excluded. There is a cap of $5 million on the total amount of credit available over the next two years.

◆ **Illinois:** Small businesses can receive a $2,500 credit against withholding taxes if they create a new, full-time position filled by a state resident for at least a year that pays no less than $13.75 an hour. There is a cap of $50 million on the total amount of credit available.

◆ **Indiana:** Businesses relocating or incorporating in the state are eligible for a credit equal to 10 percent of wages paid to full-time employees during a 24-month period. Existing businesses qualify if they hire at least 10 new employees.

◆ **Maryland:** Businesses are eligible for a $5,000 tax credit for each employee hired full-time in a newly created position or one that has been vacant for six months, and who was drawing unemployment benefits or whose benefits had expired. There is a cap of $20 million on the total amount of credit available.

◆ **Mississippi:** Upholstered furniture manufacturers can receive a $2,000 annual credit for each new job created.

◆ **Virginia:** Businesses that create new, full-time "green" jobs that pay at least $50,000 and last at least a year can receive a $500 tax credit for each job created. The state secretary of commerce will develop a list of jobs that qualify.

minimum amount, and lasts for a specified time, such as a year.

◆ The employer is a small business.

◆ The business is in a targeted industry.

These job creation tax credits are intended to help businesses regardless of how they are legally formed, so many of the credits apply to personal as well as corporate income taxes. Finally, some states have placed caps on the annual amount of credit available.

DO THEY WORK?

Some lawmakers are concerned employers might claim a tax credit for already planned hiring, rather than having the credits directly induce hiring. This can be difficult to assess.

It's important to remember that tax credits are preferences in the tax code aimed to spur some type of economic activity that would not have occurred—or would have occurred to a lesser degree—without them. That leads to the million dollar question: Do tax credits make a meaningful difference in creating new jobs?

"History suggests job creation tax credits don't work well," says David Wyss, chief economist at Standard & Poor's. "It's very hard to figure out what's a new job."

Job creation tax credits "tend to be passed at the beginning of the recovery, and many of these jobs would have been created anyway," he says.

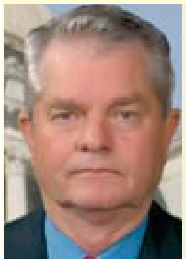
Wyss says job creation tax credits that narrowly define the jobs they cover are more likely to work. "When trying to attract an industry into a region, when aiming at manufacturing jobs as opposed to service jobs, then these credits are a bit more successful. But unfortunately, it can take a long time to create the jobs."

Whether such tax credits are successful at generating new jobs—and whether they do so in a cost-effective manner—are important concerns. Evaluating them can be difficult. A cost-benefit analysis can be an important evaluation tool. In addition to measuring how many new jobs were induced by the credit, an effective cost-benefit analysis will determine if the tax credit will generate more incremental revenue for the state than the amount lost from the incentive.

The deep desire to create new jobs may trump evaluations—good or bad—as lawmakers seek ways to bolster their economies. The timing is critical. Even though the economy is showing green shoots, the anemic job market is causing many job seekers to lose hope that a recovery is really underway.

"For more than a half century, a large segment of Mississippi's workforce was engaged in furniture manufacturing. Foreign competition and outsourcing hurt this industry. The incentive program should spur the re-creation of jobs and revitalization of furniture manufacturing."

—MISSISSIPPI HOUSE SPEAKER WILLIAM MCCOY ON THE STATE'S CUT AND SEW JOB CREATION TAX CREDIT



HOUSE SPEAKER
WILLIAM MCCOY
MISSISSIPPI

SOME STATES SAY NO

A few states considered, but didn't enact, new job creation tax credits.

◆ Colorado businesses would have received a tax credit for workers they laid off in 2009 but rehired later, if they submitted an affidavit stating they would not have rehired the employee without the credit.

◆ Georgia Governor Sonny Perdue vetoed a business tax credit for hiring unemployed workers, awaiting a report from a state tax reform study committee.

◆ Hawaii considered a tax credit for hiring unemployed workers that would have equaled the state taxes withheld from the employees.