



State of Oklahoma

Incentive Evaluation Commission

Small Employer Quality Jobs Program Evaluation

November 14, 2017

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Executive Summary



Overview

State incentives focused on job creation are common across the United States. A list compiled by the National Conference of State Legislatures in 2013 showed 40 states with some form of job creation incentive program.¹

Oklahoma's Small Employer Quality Jobs program was created in 1997 under the Small Employer Quality Jobs Act. The legislative intent is to support the creation of quality jobs, specifically by small businesses. In pursuit of this goal, the program offers quarterly cash payments to qualifying small employers equaling up to five percent of newly created payroll for up to seven years.

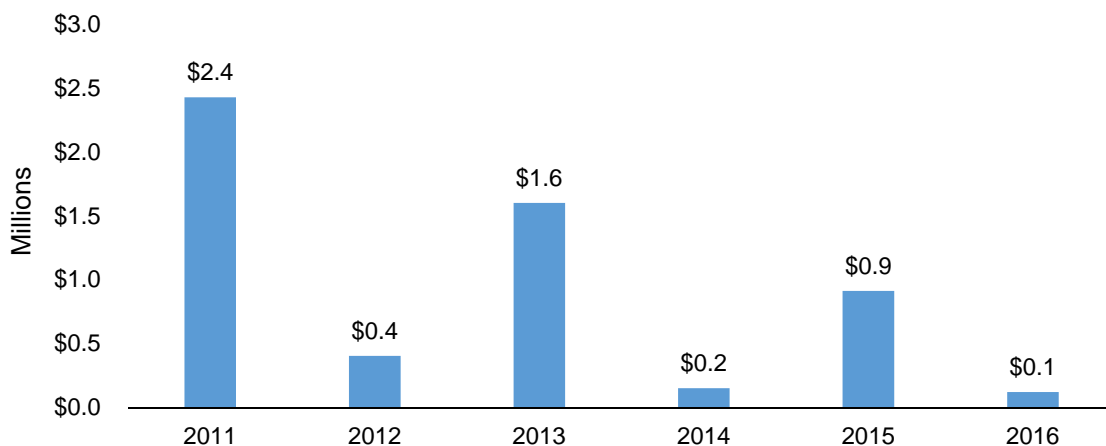
Primary Recommendation: Retain, with modifications

The Small Employer Quality Jobs program has incented over 1,000 jobs in various industries since it was created in 1997. In recent history, the program has performed well in terms of economic impact and appears to be a net benefit to the State. However, there are aspects of the program that may be improved to enhance its performance and better meet the State's goals.

Key Findings

- **The program is a net benefit to the State.** If each company that entered the program in 2011 qualified for full payments that year, the economic activity generated by those companies would have an economic impact, net of incentive costs, of \$2.4 million. In each year since 2011, the same calculation is consistently positive.

Figure 1: Estimated Net Fiscal Impact of Contracts Issued Each Year, 2011 to 2016²



- **The cost per job over the life of the program is approximately \$6,700.** Over the life of the program, 1,292 jobs have been incented and \$8.7 million in payments have been made. This job count represents the total number of jobs reported by a company on its last payment claim. It is unclear for how long the jobs were maintained before or after the final incentive payment.
- **Cost controls associated with the administrative process have been effective.** Over the life of the program, the administrative process and the statutory requirements have protected the State from excessive payments to participating companies.

¹ National Conference of State Legislatures, "Job Creation Tax Credits – 50 State Table", 2013

² This represents the annual tax revenue as a result of economic activity generated by the incentive, net of incentive costs. This analysis assumes each company offered a contract qualifies for payments in each quarter of the year



- **Industries incentivized by the Small Employer Quality Jobs program have exhibited slower growth in employment and average annual pay over the last five years, compared to the State as a whole.** The industry group decreased employment over the last five years, as overall State employment expanded. The group fell short of State growth in average annual pay but exceeded State growth in terms of total wages.
- **About half of the total payments made over the last five years have been to establishments in industries outperforming the growth of the State overall.** This may be improved by revising the program targeted industries.
- **Data collection and storage methods complicate the evaluation process.** More uniform data collection and storage among the databases maintained by the Oklahoma Tax Commission (OTC) and the Department of Commerce (Department) would ease the data analysis process in the future.

The program can be improved by:

- **Requiring companies to file information for payment each quarter.** Adding a requirement that companies file quarterly claims for payment may improve both the predictability of costs to the state, and the efficacy of the program.
- **Establishing a schedule for regular review of eligible industries.** Over the last five years, industries that have received Quality Jobs payments have been growing at a slower rate than the State as a whole in terms of employment and average annual pay. This may indicate a need to realign the list of qualifying industries with the State's intent of incentivizing establishments in industries with the potential to bring significant development to the economy. Establishing a regular review of eligible industries as well as clear criteria for an industry to qualify for the program may help in achieving the State's goal. Keeping in mind that the establishments that qualify today may receive payments for the next 10 years, it is important that the State focuses on the industries it sees as playing a part in future development.
- **Maintaining a centralized database of information collected by the Department and the OTC.** Maintaining a single database of Quality Jobs program information that includes the data collected by both the Department and the OTC can improve future evaluations. This centralized database should include the following information:
 - A unique identifier for each establishment/contract
 - Location
 - NAICS code
 - Contract terms
 - Dollar amount for each quarterly payment made
 - Number of jobs and payroll information reported by companies for each quarterly payment



Key Findings and Recommendations



Key Findings

The Small Employer Quality Jobs program has created over 1,000 jobs in various industries since its creation in 1997. In recent history, the program has performed well in terms of economic impact and appears to be a net benefit to the State. However, there are aspects of the program that may be improved to enhance its performance and better meet the State's goals.

The following provides an analysis of the program's performance related to the criteria established for its evaluation.

- **The program is a net benefit to the State.** If each company that entered the program in 2011 qualified for full payments that year, the economic activity generated by those companies would have an economic impact, net of incentive costs, of \$2.4 million. In each year since 2011, the same calculation is consistently positive.
- **The cost per job over the life of the program is approximately \$6,700.** Over the life of the program, 1,292 jobs have been created and \$8.7 million in payments have been made. This job count represents the total number of jobs reported by a company on its last payment claim. It is unclear for how long the jobs were maintained before or after the final incentive payment.
- **Industries incentivized by Small Employer Quality Jobs have exhibited slower growth in employment and average annual pay over the last five years, compared to the State as a whole.** One of the established criteria for evaluating the Small Employer Quality Jobs program is payroll and job growth associated with the incentive. This is relevant criteria not only because the incentive is focused on quality job creation, but also in that it has a stated goal of incentivizing industries with the potential to bring significant growth to the State economy.

Between 2012 and 2016, over \$1.7 million was paid to participating companies across 8 different three-digit NAICS codes. This group of NAICS codes as a whole decreased employment by 1.0 percent over this period. At the same time, overall State employment and national employment expanded by 2.5 and 5.7 percent, respectively. The following table shows these rates as well as comparisons to overall State and national average annual pay and total wages growth rates.

Table 1: Growth of Industries Receiving Small Employer Quality Jobs Payments, 2012 to 2016

	Incented Industries	OK Total	US Total
Employment	-1.0%	2.5%	5.7%
Average Annual Pay	6.4%	7.2%	8.9%
Total Wages	8.7%	5%	15.7%

Source: BLS Quarterly Census of Employment and Wages

While the industry group underperformed in employment growth, it nearly matched State growth in average annual pay and exceeded State growth in terms of total wages.

- **About half the payments made over the last five years have gone to establishments in industries outperforming the growth of the State overall.** To determine how successful the program has been in incentivizing growth industries, it is important to evaluate how much is being paid growing and declining industries. The following chart shows the breakdown of how payments are distributed among industries outperforming national trends and those that are lagging behind. An industry is deemed "outperforming" by experiencing growth in employment, total wages, and average annual wage, which exceeds the industry's national growth rate.



Table 2: Payments by Industry Performance Relative to the Overall State Growth, 2012 to 2016

	Total Payments	Percent of Total
Underperforming Industries	\$910,516	52%
Outperforming Industries	\$856,700	48%

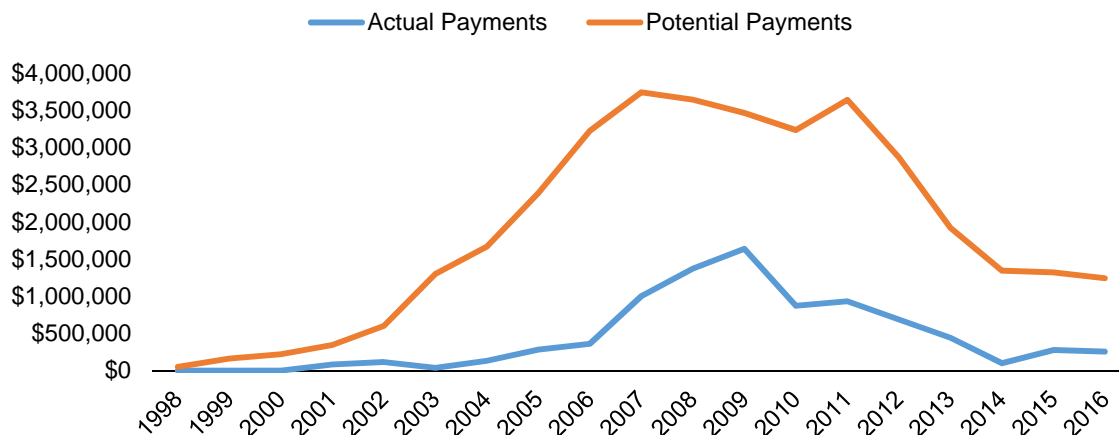
Source: Oklahoma Tax Commission and BLS Quarterly Census of Employment and Wages

- **Cost controls associated with the administrative process have been effective.** The Small Employer Quality Jobs program's administrative process is designed to control costs to the State. The net benefit rate is a significant cost control built into the program. This rate and the maximum benefit amount limiting total payments made to establishments in the program are intended to ensure the State does not spend more than each project is expected to return to the State in new tax revenue. The Department performs thorough modeling of projected costs and revenues resulting from projects to determine these amounts.

After contract parameters are set by the Department, the OTC further controls costs by verifying that each establishment filing for quarterly payments is meeting program criteria and that payments are only made to qualifying establishments. The State is further protected by controls written in statute, such as the requirement that the job creation threshold is met for four consecutive quarters within the first two years of program participation. If this threshold is not met, the establishment is removed from the program.

The following chart shows the impact these restrictions have on the amount the State actually pays to enrolled companies. The potential payments line represents the amount of payments needed to pay out each contract at an even rate over the maximum seven year period from the year of qualification. From 1998 to 2016, the State was liable to pay about \$36.4 million to program participants, but actual payments were about \$8.6 million.

Figure 2: Total Small Employer Quality Jobs Payments, 1998-2016



Source: Oklahoma Department of Commerce and Tax Commission

The majority of companies offered a Small Employer Quality Jobs contract never receive actual payments. The Department has recorded 108 companies entering into contracts, while the OTC reports only 41 companies have received a payment over the life of the program. There are several reasons for this including companies not meeting payroll requirements, or failing to file claims for payment with the OTC. Even companies that stay in the program for a full seven year term may contribute to the difference between potential and actual payments due to lower than expected job creation or payroll growth. The OTC has recorded 69 reasons for companies ending program



participation. These reasons are listed in the following table. The most common reason is voluntary withdrawal, followed by failure to file claims within the first three years, as required in statute.

Table 3: Reasons for Ending Program Participation

Reason	Number of Contracts
Voluntarily Withdrew	34
Did Not Meet Statutory Requirement	22
Reached Statutory Limit	13
Total	69

Source: Oklahoma Tax Commission

Overall, more than half of the recorded reasons for ending program participation are related to statutory limits or requirements. This highlights the importance and effectiveness of administrative process in protecting the State from making excessive payments to companies who enter the program.

- **Data collection and storage methods complicate the evaluation process.** Although the Department and the OTC collaborate effectively to accomplish the administrative tasks associated with the program, there appears to be a lack of communication when compiling data associated with the incentive.

The Department has files detailing the terms of each contract issued. Separately, the OTC maintains records of payments made to qualifying companies. Each of these databases hold key information for evaluating the incentive. However, there is no unique identifier that can be used to track one company from the Department's contract database to the OTC's payment database. This is particularly challenging when a company has changed its name since entering a contract or is known by multiple names. The project team was able to reconcile the two files by combining identifying information in each file such as the net benefit rate, location, or projected jobs.

A notable weakness in the data available for evaluation is that while the OTC tracks payment data by year, it does not maintain a complete database of program payments by quarter. That information, combined with the job and payroll information each company must report in order to receive quarterly payments would be very helpful.

Overall Recommendation: Retain the Small Quality Jobs Program

The project team recommends retaining the Small Employer Quality Jobs program. While the program is providing sufficient benefit to the State to be retained, there are also areas where the program can be improved.

- **Recommendation 1: Require filing for incentive payments each quarter.** When the program was created, companies were not required to file quarterly claims. Over time, some requirements were put in place. For example, in 2001 changes were made requiring companies to make an initial claim for payment within the first three years of enrollment. An additional restriction was put in statute in 2012 that provided for a company to be dismissed from the program if it has made one claim for payment but has since failed to file a claim in the next two years. Even with these added restrictions, a company can file for multiple quarterly payments at once.

This creates two disadvantages for the Small Employer Quality Jobs Program. First, the lack of a quarterly filing requirement creates irregular payment schedules that create a challenge in predicting State liabilities associated with the program. Inability to forecast incentive payments due to irregular



payment schedules is a significant budget risk for state incentive programs.³ Second, allowing participants to defer payments earned in one quarter to a later date diminishes the impact of the payment. New and expanding businesses generally apply a significant discount rate to future cash flows.⁴ Given that payments are significantly more valuable to them the faster they are received, it is unclear why companies would choose to defer these payments to a later date. Interviews with both the OTC and representatives of the State Chamber of Commerce suggest the process of filing for payment is not overly burdensome for participating companies. However, it is clear that the value of these payments for both participating companies and the State is highest when received as soon as possible. Adding a requirement that companies file quarterly claims for payment may improve both the predictability of costs to the State, and the efficacy of the program.

- **Recommendation 2: Regularly review eligible industries.** Program payments are almost evenly split between industries that are outperforming the State as a whole and those that are not. This may indicate a need to realign the list of qualifying industries with the State's intent of incentivizing establishments in industries with the potential to bring significant development to the economy. Establishing a regular review of eligible industries as well as clear criteria for an industry to qualify for the program may help in achieving the State's goal. Keeping in mind that the establishments that qualify today may receive payments for the next 7 years, it is important that the State focuses on the industries it sees as playing a part in future development.
- **Recommendation 3: Centralize data tracking.** Maintaining a single database of Small Employer Quality Jobs program information that includes the data collected by both the Department and the OTC can improve future evaluations. This centralized database should include the following information:
 - A unique identifier for each establishment/contract
 - Location
 - NAICS code
 - Contract terms
 - Dollar amount for each quarterly payment made
 - Number of jobs and payroll information reported by companies for each quarterly payment

Much of this information is already tracked by either the Department or OTC, but centralizing data tracking will make the information more useful.

³ The Pew Charitable Trusts, "Reducing Budget Risks" December 2015

⁴ Anderson Economic Group, "The Economic Impact of Business Tax Credits in Tennessee" December 26, 2016



Introduction



Introduction

Overview

In 2015, HB2182 established the Oklahoma Incentive Evaluation Commission (the Commission). It requires the Commission to conduct evaluations of all qualified state incentives over a four-year timeframe. The law also provides that criteria specific to each incentive be used for the evaluation. The first set of 11 evaluations was conducted in 2016.

The Small Employer Quality Jobs Program is one of the 12 incentives scheduled for review by the Commission in 2017. It is one of the off-shoots of the Quality Jobs Program – which also includes the 21st Century Quality Jobs Program, and the High Impact Quality Jobs Program. Each of these, as well as the original Quality Jobs Program are also being evaluated separately this year. Based on this evaluation and their collective judgement, the Commission will make recommendations to the Governor and the State Legislature related to each of these incentives.

Introduction

State incentives focused on job creation are common across the United States. During and following the Great Recession, these programs increased in use as ways to help start and sustain economic recovery. A list compiled by the National Conference of State Legislatures in 2013 showed 40 states with some form of job creation incentive program.⁵

Whether they are provided as tax credits or rebates, job creation incentives like Oklahoma's Quality Jobs program often seek to reduce employee costs (primarily related to wages). Reduction in wage costs can make it easier for firms to expand operations and/or hire more employees at existing locations.

Labor costs in general can be a critical factor in location decisions. A 2016 survey of corporate executives conducted by Area Development found that labor cost is the third most important factor in location decisions, trailing only highway accessibility and availability of skilled labor.⁶ This supports the approach of concentrating incentives on reducing the cost of employment to promote economic growth.

While many job creation incentives target new or maintained jobs, there has been a trend to create specific incentives that target high wage jobs, often in targeted industries and/or with additional requirements (in many instances the provision of health care or other employee benefits). For example, many states target job creation in high-technology industries that help diversify the economy and help establish a foundation in developing industries.

Incentive Characteristics

Oklahoma's Small Employer Quality Jobs program was created in 1997 under the Small Employer Quality Jobs Act. The legislative intent is to support the creation of quality jobs, specifically by small businesses. In pursuit of this goal, the program offers quarterly cash payments to qualifying small employers equaling up to five percent of newly created payroll for up to seven years.

A small employer is defined in statute as a company having no more than 90 employees in the State. To qualify for benefits, the small employer must create 5 to 15 jobs, depending on the location of the company, and pay wages that are at least 110 percent of the average wage of small employers in the county where the

⁵ National Conference of State Legislatures, "Job Creation Tax Credits – 50 State Table", 2013

⁶ Area Development, "31st Annual Survey of Corporate Executives: Confidence in U.S. Economy, Need for Investment in Infrastructure Reflected", 2016



establishment locates. If all requirements are met, a small employer may receive a rebate of up to five percent of newly created payroll for a period of seven years.

Evaluation Criteria

A key factor in evaluating the effectiveness of incentive programs is to determine whether they are meeting the stated goals as established in state statute or legislation. In this case, the legislative intent as articulated in the statute is to:

“provide appropriate incentives to support the creation of quality jobs, particularly by small businesses, in basic industries in this state”

To assist in a determination of the effectiveness of the program, the Incentive Evaluation Commission has adopted the following criteria:

- Change in jobs associated with the cash rebates
- Change in payroll associated with the cash rebates
- Ability of program administrative processes to establish the factual basis for claims related to hours, wages and benefits
- But-for test – change in jobs/payroll associated with the cash rebates versus state growth rates as a whole
- Change in jobs/payroll in the qualifying industries versus state industries as a whole
- Return on investment – economic activity versus financial net cost

The criteria address the key goals of the program, primarily focusing on job creation and payroll growth. Return on investment is also part of the criteria to determine whether the benefits to the State outweigh the cost of incentives. These criteria will be discussed throughout the balance of the evaluation.



Administration and Use of the Incentive



Incentive Administration

The Quality Jobs Program is jointly administered by the Oklahoma Department of Commerce (Department) and the Oklahoma Tax Commission (OTC). Eligibility guidelines and administrative responsibilities are set forth in State statutes and administrative rules.⁷ The essential components of program administration are summarized below.

1. **Eligibility.** An establishment starts the process by submitting an application to the Department. The application must show that the establishment meets program requirements:
 - Must operate in a basic industry as defined in statute.
 - Must have no more than 90 employees at the time of application.
 - Depending on the population of the city in which the establishment locates, it must create between 5 and 15 new jobs within two years.

Table 4: Job Creation Requirements by Population

City Population	New Job Requirement
Less than 3,500	5
3,500 to 7,000	10
Greater than 7,000	15

- The average wage of newly created jobs must be greater than or equal to 110 percent of the average wage of small employers in the county where the establishment is located.⁸
 - Must provide health care benefits to new employees which require employees to pay no more than 50 percent of premiums.⁹
 - At least 75 percent of sales must be made out-of-state within two years of entering the program.
2. **Determining Payments.** Once the initial application is approved, the Department prepares a project profile. This profile summarizes information about the establishment and its plans including the project start date, projected employment over the next five years, projected average salary of new employees hired in new direct jobs in the first and third year of program participation, and the health benefits plan to be offered to new employees. This information is analyzed by the Department and used to calculate two key factors in Quality Jobs Program benefits: **the net benefit rate and the maximum benefit amount**. These figures determine the quarterly payments the project may receive and the maximum sum of these payments over the contract term.

The **net benefit rate** is a percentage representing the amount of benefit the State expects to receive in excess of projected costs. It is calculated as the projected tax revenue to be received as a result of the new jobs less the projected costs to the State associated with those jobs including the cost of education, public safety, and transportation. For Small Employer Quality Jobs, this rate is capped at five percent. Quarterly benefit payments are calculated as the net benefit rate multiplied by the quarterly payroll of newly created jobs. The **maximum benefit amount** is the net benefit to the State as a dollar amount rather than a percentage. The sum of quarterly payments made to the project may not exceed this dollar amount.

⁷ Administrative rules for the Department of Commerce are contained in Title 150, Chapter 65. Tax Commission administrative rules are contained in Title 710, Chapter 85

⁸ This requirement is reduced to 100 percent for companies locating in a county with an unemployment rate more than 10 percent higher than the State overall, or a personal poverty rate above 15 percent

⁹ Establishments must provide such coverage within 12 months of employment



If the Department recommends a contract offer, the Office of the General Counsel prepares a contract to be reviewed by the Director of the Department and issued to the eligible establishment. The contract details the net benefit rate, maximum benefit amount, project start date, initial employment, employment projections, and average annual wage levels needed to qualify for quarterly payments.

The OTC is responsible for issuing payments during the term of the contract. Establishments submit quarterly reports to the OTC that include the number of new employees hired and the new payroll associated with these jobs. The OTC verifies that each reporting company is meeting the requirements set forth in its contract. Payments are only issued if an establishment is meeting contract criteria. Establishments meeting program criteria are able to receive quarterly payments for up to seven years.

3. **Reporting.** The OTC maintains records of payments made by year to each participating company. The Department separately maintains records of each company that has entered the program.

Changes Over Time

Since the program was created in 1998, the Small Employer Quality Jobs program has undergone several changes to both the list of eligible industries and the administrative process. The following table summarizes significant changes

Table 5: Changes to the Small Employer Quality Jobs Program Over Time

Year	Industries Added	Administrative Change
2001	None.	Participants required to file initial claim for payment within 3 years of project start date.
2003	Oil & Gas Extraction (field jobs excluded).	Average wage requirement introduced
2005	None.	Allows currently participating companies to qualify for a second contract with up to 6 percent net benefit rate if certain requirements are met and new jobs pay 150 percent of the average wage of incentivized jobs in the previous year.
2006	Web Portals; Professional, Scientific, Technical Services; Dairy Cattle & Milk Production; Chicken Egg Production.	Change in Control qualification introduced. Allows existing companies in the state that have fully changed ownership and are at risk of leaving the state to qualify for the program, counting existing employees as qualifying for benefits.
2008	Sports Teams & Clubs; Other Support Activities for Air Transport; Professional Organizations; Offices of Real Estate Agents/Brokers.	Duration of benefits extended to 15 years for Sports Teams & Clubs. Net benefit rate allowed to exceed 5 percent for Sports Teams & Clubs, but may not exceed the personal income tax rate.
2009	Wind Power Equipment; Maintenance/Repair.	None.
2010	Construction of Renewable Energy Structures; Installation of Solar Reflective Coating; Solar Heating Equipment Installation; Support Activities for Rail Transport; Support Activities for Barge Transport.	Allows companies 24 months to create required jobs, increased from 12 months. Average wage requirement changed to average wage of small employers in the county, rather than overall county average.



Year	Industries Added	Administrative Change
2012	None.	Company dismissed if it files at least one claim but fails to file again within the next two years.
2013	Rail Transportation; Wired Telecommunications; Securities, Commodities, Investments; Support Activities for Oil & Gas; Pipeline Transportation.	Any participant that ends operations in the state within 3 years of first claim must repay all benefits received. Any establishment that does not ramp up to the required payroll threshold and is dismissed may not reapply to the program for a minimum of 12 months from the last day of the month in which they were dismissed.
2015	Chicken Egg Production.	None.

Use of the Incentive

The following table summarizes the number of contracts issued as well as the total maximum benefit amounts and job thresholds associated with the contracts in each year of the program. The highest number of contracts was 15 issued in 2006. Since then, the program has averaged less than 5 contracts per year.

Table 6: Small Employer Quality Jobs Contracts Awarded Since 1998

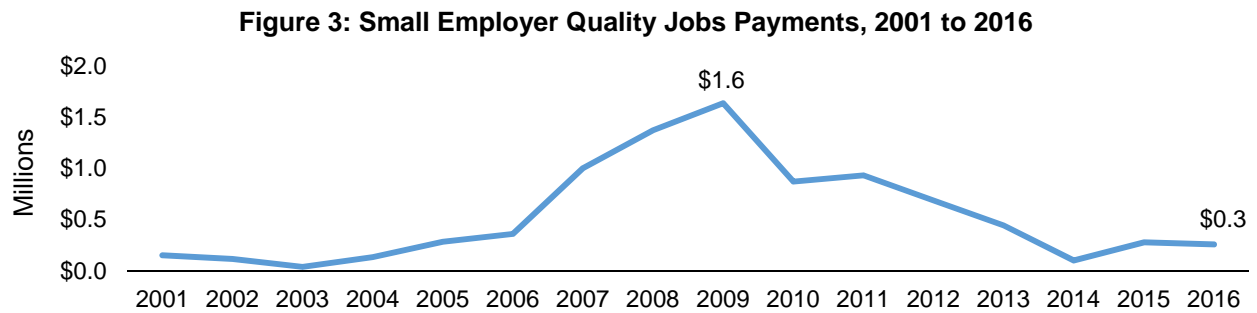
Year	Number of Contracts	Total Maximum Contract Amounts	Total Job Threshold
1998	1	\$364,509	10
1999	2	\$788,738	25
2000	2	\$396,760	20
2001	2	\$871,740	20
2002	5	\$1,796,317	75
2003	13	\$4,893,075	145
2004	8	\$2,567,448	60
2005	14	\$5,413,466	170
2006	15	\$6,630,688	140
2007	8	\$4,025,157	95
2008	1	\$170,039	5
2009	1	\$545,625	15
2010	8	\$3,296,401	75
2011	8	\$5,400,647	110
2012	4	\$1,534,857	45
2013	9	\$3,306,454	110
2014	1	\$524,686	5
2015	5	\$2,964,916	75
2016	1	\$165,307	5
Total	108	\$45,656,830	1,205

Source: Oklahoma Department of Commerce

The State makes payments to companies based on contract terms. The first actual payment made to a program participant was in 2001. Total payments made by year are shown in the following chart. Total



payments peaked in 2009 at \$1.6 million. Since then, total payments have remained relatively low. In 2016, the program cost the State less than \$260,000.



Source: Oklahoma Tax Commission



Fiscal and Economic Impact



Economic Impact Methodology

Economists use a number of statistics to describe regional economic activity. Four common measures are **Output**, which describes total economic activity and is generally equivalent to a firm's gross sales; **Value Added**, which equals gross output of an industry or a sector less its intermediate inputs; **Labor Income**, which corresponds to wages and benefits; and **Employment**, which refers to jobs that have been created in the local economy.

In an input-output analysis of new economic activity, it is useful to distinguish three types of effects: **direct**, **indirect**, and **induced**.

Direct effects are production changes associated with the immediate effects or final demand changes. The payment made by an out-of-town visitor to a hotel operator or the taxi fare paid for transportation while in town are examples of direct effects.

Indirect effects are production changes in backward-linked industries caused by the changing input needs of directly affected industries – typically, additional purchases to produce additional output. Satisfying the demand for an overnight stay will require the hotel operator to purchase additional cleaning supplies and services. The taxi driver will have to replace the gasoline consumed during the trip from the airport. These downstream purchases affect the economic output of other local merchants.

Induced effects are the changes in regional household spending patterns caused by changes in household income generated from the direct and indirect effects. Both the hotel operator and taxi driver experience increased income from the visitor's stay, as do the cleaning supplies outlet and the gas station proprietor. Induced effects capture the way in which increased income is spent in the local economy.

A multiplier reflects the interaction between different sectors of the economy. An output multiplier of 1.4, for example, means that for every \$1,000 injected into the economy, all other sectors produce an additional \$400 in output. The larger the multiplier, the greater the impact will be in the regional economy.

Figure 4: The Flow of Economic Impacts



For this analysis, the project team used the IMPLAN online economic impact model with the dataset for the State of Oklahoma (2014 Model).

State of Oklahoma Tax Revenue Estimate Methodology

To provide an “order of magnitude” estimate for state tax revenue attributable to the incentive being evaluated, the project team focused on the ratio of state government tax collections to Oklahoma Gross Domestic Product (GDP).¹⁰ Two datasets were used to derive the ratio: 1) US Department of Commerce Bureau of Economic

¹⁰ Gross State Product (GSP) is the state counterpart of Gross Domestic Product (GDP) for the nation. To assist the reader, the project team has decided to use GDP throughout this section of the report instead of mixing the two terms. This decision was made because more people are familiar with the term GDP.



Analysis GDP estimates by state;¹¹ and 2) the OTC's Annual Report of the Oklahoma Tax Commission.¹² Over the past 10 years, the state tax revenue as a percent of state GDP was 5.4 percent.

Table 7: State of Oklahoma Tax Revenue as a Percent of State GDP

Year	Oklahoma Tax Revenue ¹³	Oklahoma GDP	Ratio
2006-07	\$8,685,842,682	\$144,171,000,000	6.0%
2007-08	\$9,008,981,280	\$155,015,000,000	5.8%
2008-09	\$8,783,165,581	\$143,380,000,000	6.1%
2009-10	\$7,774,910,000	\$151,318,000,000	5.1%
2010-11	\$8,367,871,162	\$165,278,000,000	5.1%
2011-12	\$8,998,362,975	\$173,911,000,000	5.2%
2012-13	\$9,175,334,979	\$182,447,000,000	5.0%
2013-14	\$9,550,183,790	\$190,171,000,000	5.0%
2014-15	\$9,778,654,182	\$180,425,000,000	5.4%
2015-16	\$8,963,894,053	\$182,937,000,000	4.9%
Average	\$8,908,720,068	\$166,905,300,000	5.4%

Source: US Department of Commerce Bureau of Economic Analysis and Oklahoma Tax Commission

The value added of an industry, also referred to as gross domestic product (GDP)-by-industry, is the contribution of a private industry or government sector to overall GDP. The components of value added consist of compensation of employees, taxes on production and imports less subsidies, and gross operating surplus. Changes in value added components (such as employee compensation) have a direct impact on taxes such as income and sales tax. Other tax revenues (such as alcoholic beverage and cigarette taxes) are also positively correlated to changes in income.

Because of the highly correlated relationship between changes in the GDP by industry and most taxes collected by the state, the ratio of government tax collections to Oklahoma GDP forms the evaluation basis of the fiscal implications of different incentive programs offered by the State. The broader the basis of taxation (i.e., income and sales taxes) the stronger the correlation; with certain taxes on specific activity, such as the gross production (severance) tax, there may be some variation in the ratio year-to-year, although these fluctuations tend to smooth out over a period of several years. This ratio approach is somewhat standard practice, and is consistent with what IMPLAN and other economic modeling software programs use to estimate changes in tax revenue.

To estimate State of Oklahoma tax revenue generated in a given year, the project team multiplied the total value added figure produced by the IMPLAN model by the corresponding annual ratio (about 5.4 percent). For example, if the total value added was \$1,000,000, then the estimated State tax revenue was \$54,000 (\$1,000,000 x 5.4 percent).

Economic Impact

The Small Employer Quality Jobs program provides qualifying companies quarterly cash rebates of up to 5 percent for newly created taxable payroll for up to 7 years. Each company goes through a formal application with the Department where payroll and employment thresholds are established. In addition, the Department uses an in-house methodology and model to deduct some of the expenses incurred by the State of Oklahoma

¹¹ <http://www.bea.gov/regional/>

¹² https://www.ok.gov/tax/Forms_&_Publications/Publications/Annual_Reports/index.html

¹³ Gross collections from state-levied taxes, licenses and fees, exclusive of city/county sales and use taxes and county lodging taxes.



for employees who will likely move to the State to work at these companies. The net effect of this calculation is to reduce the incentive amount offered. This approach is a best practice used in many states to help ensure a positive return on investment, while creating an incentive program that achieves its goals of jobs creation and higher wages. For this program, there are clear and transparent linkages between new payroll and jobs creation and the incentive amount offered.

To evaluate the economic impact of the incentive program, firms were grouped based on when they entered the program. For example, all firms that entered in 2013 were grouped together. From a state perspective, the economic impact of the program is the aggregate impact of these cohort firms over seven years. However, data limitations and firms dropping out of the program at various stages hamper this type of analysis. To provide an order of magnitude impact, the project team estimated the annual economic impact of firms based on the project year cohort. The calculations were made using information related to the 3-year employment target, total project new jobs, benefit rate, incentive contract amount, and NAICS code. The IMPLAN model was used to calculate the impact of each firm in the program.

The following tables highlight the average annual economic and tax impact of each cohort. For example, the 2013 table data illustrates the estimated annual economic and tax impact of all firms that entered the program in 2013. This annual impact should occur for ten years assuming no firms drop out of the program.

This approach is also appropriate when evaluating the average annual cost of the incentive program. From the State perspective, the goal is for all applicant companies to remain eligible and create new jobs and payroll. If this occurs, the aggregate incentive contract amount for each cohort is the maximum “cost” to the state. If this occurs, that state should compare the aggregate or average annual cash rebate amount against the new tax revenue generated by the firms over 10 years or the average annual new tax revenue.

Table 8: Economic Impact

Year		Output	Value Added	Labor Income	Employment	Estimated Oklahoma Tax Revenue
2011	Direct Effect	\$100,951,817	\$28,241,893	\$10,591,288	216	
	Indirect Effect	\$35,554,209	\$18,576,792	\$11,265,497	201	
	Induced Effect	\$16,857,062	\$9,228,541	\$5,223,215	134	
	Total Effect	\$153,363,088	\$56,047,226	\$27,080,000	551	\$2,914,456
2012	Direct Effect	\$10,858,656	\$6,302,885	\$3,621,066	87	
	Indirect Effect	\$4,646,820	\$2,566,593	\$1,679,206	34	
	Induced Effect	\$4,080,919	\$2,235,505	\$1,265,133	32	
	Total Effect	\$19,586,395	\$11,104,983	\$6,565,405	153	\$555,249
2013	Direct Effect	\$72,987,482	\$15,936,811	\$12,792,121	338	
	Indirect Effect	\$32,941,613	\$16,233,018	\$10,833,483	310	
	Induced Effect	\$18,133,278	\$9,909,860	\$5,604,721	139	
	Total Effect	\$124,062,373	\$42,079,689	\$29,230,325	787	\$2,116,205
2014	Direct Effect	\$6,355,041	\$2,434,387	\$1,686,819	50	
	Indirect Effect	\$1,617,219	\$814,623	\$517,271	10	
	Induced Effect	\$1,709,948	\$932,141	\$527,633	13	
	Total Effect	\$9,682,208	\$4,181,151	\$2,731,723	73	\$225,782



Year		Output	Value Added	Labor Income	Employment	Estimated Oklahoma Tax Revenue
2015	Direct Effect	\$50,798,502	\$11,395,195	\$8,908,459	170	
	Indirect Effect	\$17,549,913	\$9,477,313	\$5,922,098	107	
	Induced Effect	\$11,704,159	\$6,411,832	\$3,629,841	87	
	Total Effect	\$80,052,574	\$27,284,340	\$18,460,398	364	\$1,336,933
2016	Direct Effect	\$4,474,127	\$1,727,780	\$1,199,402	39	
	Indirect Effect	\$1,139,259	\$575,772	\$365,604	7	
	Induced Effect	\$1,208,173	\$661,869	\$374,648	9	
	Total Effect	\$6,821,559	\$2,965,421	\$1,939,654	55	\$145,306

Table 9: Estimated Annual Net Impact of Each Cohort

Year	Average Annual Incentive	Estimated State of OK Tax Revenue	Net Impact
2011	\$486,071	\$2,914,456	\$2,428,384
2012	\$150,851	\$555,249	\$404,398
2013	\$513,588	\$2,116,205	\$1,602,617
2014	\$74,955	\$225,782	\$150,827
2015	\$423,559	\$1,336,933	\$913,373
2016	\$23,615	\$145,306	\$121,690

As depicted in the preceding table, the Small Employer Quality Jobs Program results in increased economic activity in multiple industry sectors. The level of economic activity varies each year and is directly linked to the industry sector of the applicant firm as well as net new employment and wages. Multiplying the total value added figure produced by the IMPLAN model by the corresponding annual tax ratio, provides an estimate for total annual State of Oklahoma tax revenue. Over the past 6 years, the Small Employer Quality Jobs Program (direct + indirect + induced economic effects) has committed about \$16.7 million in total state incentives. Over this same period, the state should collect \$72.9 million in state tax revenue assuming all companies reach their employment and payroll targets.



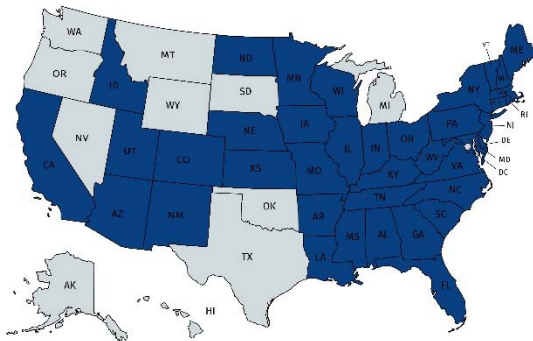
Incentive Benchmarking



Benchmarking

A detailed description of comparable state programs can be found in **Appendix A**.

Figure 5: Other states offering job creation incentives



For evaluation purposes, benchmarking provides information related to how peer states use and evaluate similar incentives. At the outset, it should be understood that no states are ‘perfect peers’ – there will be multiple differences in economic, demographic and political factors that will have to be considered in any analysis; likewise, it is rare that any two state incentive programs will be exactly the same.¹⁴ These benchmarking realities must be taken into consideration when making comparisons – and, for the sake of brevity, the report will not continually re-make this point throughout the discussion.

The search for comparable programs started with Oklahoma’s neighboring states. This is a typical starting point since states often compete with nearby states for the same opportunities. Neighboring states also typically share similar economic and demographic characteristics that lend themselves to comparison. However, no bordering states were found to have similar programs.

Searching beyond geographic proximity yielded five comparable programs in other states. Each program has a focus on incentivizing small businesses. Most states target companies with 50 or fewer employees. While these programs share a similar focus to the Small Employer Quality Jobs program, none exactly matches Oklahoma’s focus. Important differences relate to business size requirements and benefit amount.

Only one state, South Carolina, allows larger companies than Oklahoma does to participate in its program. While its number of employees is larger, the number of employees used is the company’s worldwide

employee count. Illinois has a similar limitation, where the requirement is no more than 50 employees worldwide. This creates an important distinction between Oklahoma’s program and Illinois and South Carolina’s small business programs. Both large and small businesses that have a small number of employees in Oklahoma can qualify for Small Employer Quality Jobs. However, Illinois and South Carolina have programs that are more focused on small business. A large company with a small number of in-state employees would not qualify for those states’ programs.

Figure 6: States chosen for comparison



Louisiana is the only other state in the comparison group to calculate benefits as a percentage of payroll created. Three of the five comparison states pay benefits as a fixed amount per job. In some cases, this may result in a greater benefit amount for companies in

other states. However, Louisiana and Oklahoma’s benefit calculation creates an added incentive for

¹⁴ The primary instances of exactly alike state incentive programs occur when states choose to ‘piggyback’ onto federal programs.



participating companies to pay competitive wages. Since benefits are a percentage of new payroll, the benefits the small business receives will grow along with growth in wages.



Appendices



Appendix A: Small Employer Quality Jobs Benchmarking

Small Employer Quality Jobs Benchmarking						
	Oklahoma	Alabama	Illinois	Kentucky	Louisiana	South Carolina
Program Name	Small Employer Quality Jobs	Full Employment Act of 2011	Small Business Job Creation Tax Credit*	Kentucky Small Business Tax Credit	Quality Jobs	Annual Small Business Job Tax Credit
Size Requirement	90 or fewer full-time employees in Oklahoma	No more than 50 employees	No more than 50 full-time employees worldwide	No more than 50 employees	No more than 50 employees	99 or fewer employees worldwide
Job Creation Requirement	5 to 15 new jobs, depending on location	Any net increase from previous tax year qualifies	None	At least one new job	5 new jobs	Monthly average of two new jobs per month of operation during the tax year
Payroll Requirement	N/A	None	None		Greater than or equal to \$250,000	None
Wage Requirement	100, 110, or 125 percent of the average county wage of small employers, depending on the location of the company	More than \$10 per hour	\$10 per hour	150 percent of the federal minimum wage	\$14.50 per hour for 5 percent rebate \$19.10 per hour for 6 percent rebate	Greater than or equal to 120 percent of per capita income for lesser of state and county If job pays less than 120 percent but still greater than the applicable per capita income, company qualifies for 50 percent of credit amount for that job
Health Insurance Requirement	Employees must pay no more than 50% of the premium cost	None	None	None	Company must offer health care benefits of \$1.25 per hour and at least 50 percent of the employees holding new direct jobs must have accepted such benefits	None
Capital Investment Requirement	None	None	None	\$5,000	None	None
Benefit Type	Cash Rebate	Tax Credit	Tax Credit	Tax Credit	Cash Rebate	Tax Credit
Benefit Amount	5 percent of new job payroll	\$1,000 per employee	Maximum of \$2,500 per employee	\$3,500 to \$25,000	5 or 6 percent of payroll	\$1,500 to \$8,000 per job
Benefit Period	7 Years	None	1 Year	Can re-apply annually	5 Years	5 Years
Aggregate Program Cap	None	None	None	\$3,000,000	None	None



Appendix B: Small Employer Quality Jobs Basic Industries

Small Employer Quality Jobs Basic Industries	
Industry	NAICS Codes
Adjustment and Collection Services (75% out-of-state debtors)	561440
Agricultural Production	112120
Alternative Energy Equipment Installation	238160
	238220
Alternative Energy Structure Construction	237130
Arrangement of Passenger Transportation	561510
	561599
Central Administrative Offices, Corporate Offices and Technical Services	5611
	5612
	51821
	519130
	52232
	56142
	524291
	551114
Certain Communications Services	517110
	51741
	51791
Certain Refuse Systems that distribute methane gas	5622
Certain Warehouse/Distribution Operations Where 40% of inventory is shipped out-of-state	No Codes Listed
Computer Programming, Data Processing and other Computer Related Services	5112
	5182
	5191
	519130
	5415
Electric Service Companies (90% of energy input sourced in-state, 90% of sales out-of-state)	221111- 221122



Appendix B: Small Employer Quality Jobs Basic Industries

Small Employer Quality Jobs Basic Industries (continued)	
Engineering, Management and Related Services	5412
	5414-5417
	54131
	54133
	54136
	54137
	541990
Federal Civilian Workforce of the FAA Where jobs are migrating to Oklahoma from other Federal sites, or expansion here	No Codes Listed
Flight Training Services	611512
Grocery Wholesale Distributing	4244
	4245
Insurance Carriers	5241
Insurance Claims Processors Only	524210
	524292
Manufacturing	31
	32
	33
	5111
	11331
Miscellaneous Business Services	561410
	56142
	51911
Miscellaneous Equipment Rental	5324
Motor Freight Transportation and Warehousing	493
	484
	4884-4889
Offices of Real Estate Agents & Brokers (75% of transaction out-of-state)	53120
	6215
Other support activities for air transportation	488190
Professional Organizations	813920
Rail Transportation	482



Appendix B: Small Employer Quality Jobs Basic Industries

Small Employer Quality Jobs Basic Industries (continued)	
Research, development and testing Labs	541711
	541712
	541380
Securities, Commodities, Investments	523
Sports Teams & Clubs	711211
Support Activities for Rail and Water Transport	4882
	4883
Transportation by Air, If corporate HQ and some reservation activities are within the state or 75% of air transport sales are to out-of-state consumers	4811
Transportation of Freight or Cargo	541614
Wind Power Electric Generation Equipment Repair & Maintenance	811310