

Reconstruction



Watch

**Promoting Fair and Effective Use of New York City's
Economic Development Resources
After September 11th**

Publication #5—November 2002

The Liberty Zone Work Opportunity Tax Credit
Will it Retain and Create Good Jobs in Lower Manhattan?

A project of Good Jobs New York

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What is Reconstruction Watch?

Reconstruction Watch is intended to assist low and moderate income New Yorkers in understanding and influencing the reconstruction process. Through its research and publications, Reconstruction Watch will provide these New Yorkers and the organizations that assist and represent them with timely information that they can use to participate effectively in the reconstruction process.

Reconstruction Watch will:

- Provide useful information on the key players in the reconstruction process.
- Analyze, in plain English, the subsidy proposals being advanced at the federal, state and city levels to foster economic development in New York City in the wake of the September 11th attacks. Do the proposed subsidies have quality job standards? Are there safeguards for taxpayers for companies who don't keep their agreements? What are the benefits and drawbacks of each proposed subsidy?
- Report on subsidies targeted to specific firms including the estimated dollar value of the deal, the company's job creation and retention performance, its compliance with environmental and labor standards, and previous subsidies received.

Feedback from members of the public is crucial to this project. Please contact us with questions or suggestions.

Good Jobs New York is funded by the Rockefeller Family Fund, the New York Foundation, The New York Community Trust and The Rockefeller Foundation. Funding for Reconstruction Watch has been provided by The Rockefeller Foundation.

For additional information visit www.reconstructionwatch.net

Good Jobs New York is a joint project of the Fiscal Policy Institute and Good Jobs First

Previous Reconstruction Watch publications listed below, as well as other information about the rebuilding effort are available at www.reconstructionwatch.net.

- 1) "The Lower Manhattan Development Corporation: Who Are These People and Where Did They Come From?" February 2001
- 2) "An Analysis of the "Draft Assistance Plan for Individuals." How Will Lower Manhattan Residents Benefit?" March 2002 – Revised November 2002
- 3) "An Analysis of the "Job Creation and Worker Assistance Action of 2002," Private Activity Bonds. An Opportunity for Public Input?" April 2002
- 4) "Breaking it Down: An Analysis of New York State's Final Action Plan for New York Business Recovery and Economic Revitalization." April 2002 – Revised November 2002

Executive Summary:

Many components of the Job Creation and Worker Assistance Act of 2002, signed by President Bush in March of 2002 are intended to assist workers affected by the September 11th attacks on the World Trade Center. However, most are not new programs; instead they are existing programs with a twist. For example, Liberty Bonds (see Reconstruction Watch publication #3) are better known as Industrial Revenue bonds or Private Activity Bonds. And Community Development Block Grants (see Reconstruction Watch publication #4), normally allocated to low-income neighborhoods are instead being given to large businesses as part of a corporate retention initiative.

Similarly, the Work Opportunity Tax Credit, the focus of this Reconstruction Watch publication, has been altered for New York from its 1996 form. While some may argue a direct comparison to WOTC's predecessor program the Targeted Jobs Tax Credit (TJTC), is unfair, it is noteworthy to point out that the TJTC was ultimately discredited and cited by the United States Department of Labor in 1994 as "... not an effective means of helping target group members find employment and cost three times the amount that it returned in economic benefits."¹

The Work Opportunity Tax Credit (WOTC) is intended to give employers incentive to hire disadvantaged workers: former welfare recipients, ex-prisoners (see intended beneficiaries on page one of this report). The Liberty Zone WOTC will be broadened from disadvantaged New Yorkers to any employee at a company in Lower Manhattan with less than 200 employees including stockbrokers, attorneys and the like.

This report includes a description of the Liberty Zone WOTC and of WOTC historically. It also explains which companies are eligible and what if any disclosure requirements apply. We conclude with analysis and recommendations on how these tax credits could benefit workers displaced by the attacks of September 11, 2001. Highlights include:

- WOTC historically has benefited mostly large companies that hire low-wage workers with questionable training benefits and poor career ladder opportunities. WOTC as tailored for reconstruction does little to solve this; tax credits will be granted to any eligible company regardless of its need to create jobs. Moreover, companies are eligible by simply retaining their current employees.
- A study in 1997 found that 66% of all WOTC dollars were claimed by companies grossing over \$1 billion, doing little to assist small businesses, theoretically one of its principal beneficiaries. Taking into consideration the current plight of small businesses in New York City, the New York City Economic Development Corporation, the Empire State Development Corporation and the Lower Manhattan Development Corporation ensure that small business take advantage of this tax credit.²

We also provide sources for those wishing to learn more about the financial implications of these tax credits.

Acknowledgements: Doug Hoffer, on behalf of Good Jobs New York developed this analysis of the Work Opportunity Tax Credit.

¹ U.S. Department of Labor Office of Inspector General, August 1994 - www.oig.dol.gov/public/reports/oa/pre_1998/04-94-021-03-320s.htm.

² In early July, the city and state jointly launched "Operation GO" Operation Grant Outreach aimed to encourage small businesses downtown to apply for assistance. For additional information, contact one of the Businesses Recovery Centers at 1-800-456-8369 or visit www.newyorkbiz.com.

WORK OPPORTUNITY TAX CREDIT

<p>Description</p>	<p>The Work Opportunity Tax Credit (WOTC) is a federal income tax credit that rewards employers for hiring economically disadvantaged individuals and those with barriers to employment (see intended beneficiaries below). The Job Creation and Worker Assistance Act of 2002 amended WOTC by expanding the tax credit to employers that <u>hire or retain anyone</u> in the Liberty Zone during 2002 and 2003. The tax credit is also available to employers that relocated from Lower Manhattan to another part of New York City due to the physical destruction or damage of their workplaces within the Liberty Zone by the September 11, 2001 terrorist attack.</p> <p>The Liberty Zone WOTC provides employers a federal income tax credit of up to \$2,400 per worker in both 2002 and 2003. There is no limit to the number of qualified workers within the Liberty Zone for which an employer may claim the credit but no credit is allowed if an otherwise qualified employer had, on average, more than 200 employees in the taxable year in question. In addition, for employers that relocated from the Liberty Zone to elsewhere within New York City, the number of employees whose wages are eligible for WOTC may not exceed the number of its employees in the Liberty Zone on September 11, 2001.</p> <p>Like other tax credits, the Liberty Zone WOTC is especially appealing to companies because it gives a firm a dollar-for-dollar reduction in its tax bill, rather than a deduction from its taxable income. The credit equals 40% of the first \$6,000 of qualified wages up to \$2,400 per employee. Credits can be applied to 2002 and 2003 taxes and may be carried forward into succeeding years. In addition, the tax credits can be used against the Alternative Minimum Tax (AMT).³ http://www.ombwatch.org/article/articleview/300/1/2/</p>
<p>Intended beneficiaries</p>	<p>WOTC was originally intended to encourage employers to hire hard to employ individuals from the following categories:</p> <ul style="list-style-type: none"> • a member of a family that received Temporary Assistance for Needy Families (TANF) the main federal welfare program; • a veteran who is a member of a family that received food stamps recently; • a worker between 18 and 24 whose family received food stamps recently; • a worker between 18 and 24 who resides in one of the federally designated Empowerment Zones or Enterprise Communities; • a disabled worker who completed or is enrolled in qualified rehabilitative services; • an ex-felon who is a member of a low-income family; and • anyone who received Supplemental Security Income benefits for any month during the 60 days before the date of hire. <p>The Liberty Zone WOTC massively broadens eligibility to <u>any individual</u> working in the Liberty Zone or working for an employer relocated from the Liberty Zone to other areas of NYC. In other words, by this Act, the WOTC program is extended from a needy individual-based program to a blanket geographic area-based program.</p>
<p>History of the program</p>	<p>WOTC was created by the Small Business Job Protection Act of 1996, a successor to the Targeted Jobs Tax Credit, an earlier discredited program that expired at the end of 1994. WOTC expired at the end of 2001 but has since been re-authorized for another two years.</p> <p>WOTC has been used primarily by a small number of large companies with lots of low- wage, low-skill jobs, especially in the fast food and retail sectors. In 1997, 66% of all WOTC credits were claimed by companies with sales in excess of \$1 billion. An analysis of data for California and</p>

³ To learn more about the AMT visit - <http://www.ombwatch.org/article/articleview/300/1/2/> or <http://www.irs.gov/faqs/page/0,,id%3D15701,00.html>

	<p>Texas from 1997 through 1999 found that just 3% of participating companies accounted for 83% of all WOTC-certified employees.</p> <p>Nationwide, a total of 370,835 workers were certified for WOTC in fiscal year 2000.</p> <p>From July 1998 to June 1999 (latest data available), the total value of the credits was \$233 million.</p>
<p>Research Findings</p>	<p>A recurring criticism of both the Targeted Jobs Tax Credit (TJTC) and WOTC is that the programs create an incentive for employers to "churn" - to dismiss workers whose tax credits have run out so they can replace them with new credit-eligible employees. Critics have also argued that WOTC provides a windfall since it gives companies a tax break to hire people they would have hired anyway.</p> <p>Recent research by the General Accounting Office (GAO) found no evidence of churning, but it relied exclusively on interviews with employers and never spoke with workers - a fatal methodological flaw. Employers claimed churning would not be cost effective due to the costs of recruitment and training. Employers stated that these costs averaged \$3,799 per employee - a somewhat questionable claim for low-wage jobs that require only "short-term on-the-job training." The GAO stated without comment that "67% of certified employees separated from their employers after earning less than \$3,000." In other words, WOTC worker turnover rates are high. So high, indeed, that purported training costs exceed average-duration wages. Even if it isn't "churning" per se, many employers are failing to provide career ladder opportunities to needy workers. For the full GAO report, go to http://www.gao.gov/ and see GAO-01-329.</p> <p>It is disturbing that GAO, by its own admission, "did not evaluate the effectiveness or efficiency of the WOTC in promoting the hiring of disadvantaged individuals." Moreover, GAO acknowledged that it "did not determine the extent to which employers may have received 'windfall' credits for employees whom they would have hired anyway."</p>
<p>Budget Impacts</p>	<p>According to Congress' Joint Committee on Taxation, the Lower Manhattan changes to WOTC will cost federal taxpayers \$631 million in the next six years.</p>
<p>How it works</p>	<p>Normally, businesses must fill out a simple IRS form to receive certification for each worker. However, under the Liberty Zone WOTC amendment, businesses that hire <u>or retain</u> someone working in lower Manhattan and businesses relocated from the Liberty Zone that employ people elsewhere in New York City are automatically eligible for credit.</p>
<p>Disclosure</p>	<p>There is no disclosure system for reporting the names of businesses that claim WOTC, or the cost of their tax credits. Federal law protects the confidentiality of income tax returns.</p> <p>The IRS periodically publishes aggregate data on the use of such tax credits, including the number of firms by sector and the amounts claimed. See report 98CO21nr.xls at http://www.irs.gov/taxstats/display/0,,i1%3D40%26genericId%3D16841,00.html</p> <p>Minimal information can be obtained from state labor agencies that certify workers as eligible for WOTC benefits. However, these agencies cannot disclose company-specific information. In addition, even minimal disclosure is complicated by the fact that these state agencies often deal with consultants rather than employers, and applications are frequently filed in the named of a consultant.</p>

Comments



Based on the record, WOTC and its predecessor TJTC have not provided expanded work opportunities for disadvantaged persons. Instead, it appears that these tax credit programs have allowed a small number of large employers to receive hundreds of millions in tax credits for filling low-wage jobs with many of the same people they would have hired anyway.

By extending eligibility to workers hired or retained by businesses in or relocated from Lower Manhattan, the bill makes a bad law worse. Using a program designed to help former welfare recipients and ex-felons to assist in the economic recovery of a disaster area populated by investment bankers and bond traders is an egregious misfit.

WOTC fails as a redevelopment tool for the following reasons:

- Some businesses receiving WOTC benefits may have already regained lost ground, while others need much greater assistance;
- Some may still be profitable, while others are not;
- Some may have substantial reserves, while others have none;
- Some may have already signed leases (demonstrating a long-term commitment to NYC), while others are operating on a month to month basis;
- Some businesses are insured for losses, while others are not;
- Some businesses receiving benefits may actually be doing quite well and expanding on their own, while others may still be struggling; and
- The ESDC and LMDC have already begun to distribute substantial funds to affected companies through other programs, which are also intended to help create or retain jobs.

For at least some of the potential business beneficiaries, the tax credits would serve no justifiable public purpose and would be completely wasted. For others, the credits would represent a second bite of the apple since they have access to other assistance programs. For some, these two bites may be much more than what is logically justified while for others they may be less than what is appropriate. Overall, the recovery from the terrorist attacks of September 11 is clearly a situation in which one size does not fit all, but this expansion of the WOTC program is structured as if it does.

An appropriate use of WOTC in response to the terrorist attack on lower Manhattan would be to make it an incentive to hire those workers actually dislocated by the disaster. That would encourage employers to hire the retail clerks, janitors and restaurant workers who lost their jobs as a result of the attacks.

Additionally, every effort should be made to create WOTC hiring incentives for non-profit organizations for which the current program is irrelevant due to their tax-exempt status.

Finally, federal and state agencies should disclose the names of companies and the value of the credits they receive so that the program's effectiveness can be accurately evaluated.