National Employment Opportunity Network (NEON)

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The National Employment Opportunity Network (NEON) appreciates the opportunity to submit comments on the Work Opportunity Tax Credit (WOTC) to the American Workforce Group of the Republican Working Groups for the Expiration of the Tax Cut and Jobs Act. NEON represents members who work with thousands of employers across the country to incorporate WOTC into their hiring initiatives to recruit and identify job applicants who are on public assistance programs and are likely to meet the program's eligibility criteria.

WOTC was first enacted in the Small Business Jobs Protection Act of 1996 as part of a bi-partisan effort of the Republican Congress and the Clinton Administration to modernize welfare. Congress recognized that to help move more people off public assistance programs, especially welfare, they needed to provide employers with an incentive to hire individuals who often had little if any workplace experience and few if any of the skills employers were seeking. Additionally, Congress understood that the vast majority of individuals on Aid to Families with Dependent Children (which became TANF) had little connection with the workplace and employers would not hire these individuals if they had a choice to hire an applicant who has a job or who had work experience. Twenty-eight years later, the demand by employers for workers with the appropriate work skills has become an even more significant barrier to employment for WOTC eligible job applicants.

Since 1996, the U.S. Department of Labor has indicated that WOTC has helped more than 40 million individuals move from public assistance programs into the workforce. In addition, based upon New York State Department of Labor report[1], the vast majority of those hired, through WOTC, remain in the workforce--in fact, they tend to stay longer in their initial job than other entry level hires.

WOTC has been increasingly effective in helping veterans transition into the private sector workforce. In FY 2023, 191,000 veterans were certified as having been WOTC hires, a 52% increase over FY 2015.

Dr. Peter Cappelli, a noted labor economist at the University of Pennsylvania's Wharton School of Business indicates that WOTC eligible individuals are less likely to succeed in a job because of a number of factors including "...family demands or resource constraints that limit their ability to get transportation to work. Still others have difficulty holding a job just because they cannot handle the discipline of staying

1 The Work Opportunity Tax Credit – The New York State Experience – An Exploration of the Costs and Benefits 1996 – 2003

2 Cappelli letter 5/19/23 to Lily Lawrence Batchelder and Brent Parton

at work all day or for an entire week, still others cannot get along with other workers…"[1] As a result, these individuals tend to be stigmatized by potential employers and are often left out of the workforce altogether.

In the same study conducted by Dr. Cappelli, he points out that WOTC eligible individuals are usually competing with job applicants who already are employed, and they are looking for additional opportunities, which include: higher pay, a job closer to home, better hours, provision of day care, and room for advancement to name a few. Dr. Cappelli also identified this as frictional unemployment and indicates that two thirds of applicants for entry level positions fall into that category and thus are competing with WOTC eligible individuals. As such hiring a WOTC eligible individual expands the workforce without creating a hardship for individuals who are already working.

As Dr. Cappelli indicates WOTC should be thought of as a "selection credit" designed to provide an individual with his or her first stable employment experience to enable them to qualify for advancement with their employer or move to a better higher paying job. WOTC is not a wage subsidy, its purpose is to incentivize the transition from public assistance to the workforce—and the free market does the rest.

The WOTC incentive is modest compared to the public benefit it delivers. While the maximum WOTC Credit is $2,400, because the employer cannot take the employee deduction on credited wages, the true maximum value of the credit to the employer is approximately $1,100 vs hiring a non-WOTC eligible individual. Dr. Cappelli points out that WOTC helps offset the roughly $4,000 that it costs to bring on and train a new worker as well as setting up a payroll system to administer the WOTC program.

Dr. Cappelli also indicates that participating employers are required to screen an applicant by having them complete an IRS pre-screening form 8850 to determine whether they may qualify for WOTC before the job offer is made. Another WOTC benefit is that it acts to expand the workforce participation rate by encouraging employers to hire workers whom they would otherwise not consider and who would remain on costly public assistance programs. Overall, WOTC definitely influences employer hiring practices.

Although the fiscal benefit of WOTC is not quantifiable by JCT (because it is on the spending side), Dr. Cappelli was able to determine that the program more than pays for itself. He estimated that by transitioning individuals to the workforce WOTC results in an annual net Federal saving of $7,600 in Federal Medicaid, SNAP, TANF and public housing expenditures and an estimated total net saving per certification of $17,700. Utilizing DOL FY 2022 WOTC certification data for each state, Dr. Cappelli was able to estimate that the program saved federal and state governments a total of $22.4 billion more than the program's cost over a ten-year period. This breaks down to $17.6 billion in estimated federal savings and $4.7 billion in estimated state savings. We would also point out that when an employer hires an individual who they believe is eligible based upon their having completed the IRS 8850 pre-screening document and they do not get certified because they do not meet the program's eligibility criteria, savings in public assistance expenditures are even greater than Dr. Cappelli has estimated. This is because they

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still come off assistance programs even though the employer does not receive a tax credit for having hired them.

Given the effectiveness of the program in helping individuals with little work history and who lack the skills employers are seeking to enter the workforce, NEON and our members believe the program serves a vital role in providing the resources needed to encourage them to hire individuals they would otherwise not consider while at the same time it helps to reduce the ever increasing costs of public assistance programs.

However, NEON and the employers we work with would also point out that while the costs of on boarding and training WOTC eligible individuals has only increased over the past three decades of the program, the WOTC wage base has remained constant at $6,000 since the program's inception. Simply to keep pace with inflation since WOTC's enactment in 1996, the wage base would have had to increase to $12,000. At the same time, employers are looking for workers with more skills than they were in 1996. They are seeking at the very least basic computer skills which many of those eligible do not have, not to mention simple workplace skills such as showing up everyday week in and week out, taking direction from a supervisor, and working as part of a team. These are skills that can be taught, but they take time and money not to mention the risk that the worker will not succeed. That is why increasing the percentage of the credit to 50% of the wage base (from the current 40%) is also important. Together these two program enhancements would encourage employers to both hire more WOTC eligible individuals as well as providing the resources for training that would open better jobs to those who are eligible.

NEON would also note that currently SNAP eligibility is limited to those individuals who are under age 40. Yet increasingly the SNAP rolls are being populated by individuals who lost their jobs because jobs have gone overseas or more recently because businesses have closed due to the COVID pandemic. At the same time, because of inflation increasingly seniors are looking to return to the workforce because they cannot make ends meet. What they all have in common is that they lack the skills employers are looking for. Eliminating the age ceiling on SNAP individuals in combination with increasing the value of the credit would encourage employers to hire them. NEON would also point out that having to verify the age for all SNAP applicants places a significant administrative burden on employers to obtain the age documentation and upon the State Workforce Agencies (SWAs) which verify eligibility.

That is why NEON supports the Smucker/Sewell Improve and Enhance the Work Opportunity Tax Act, H.R. 6833 which would:

- Increases the WOTC credit from 40% to 50% on the first $6,000 of wages for those who work less than 400 hours.
- Increase the credit to 50% of wages in excess of $6,000 up to $12,000 for those who work 400 or more hours.
- Increases the wage base for veterans with earnings of $6,000 up to $12,000 to
    - $12,000 AND $24,000 FOR (D0 (3) (a) (II) (i) category

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  - $14,000 to $28,000 for (d) (3) (A) (iv) category &
  - $24,000 to $48,000 for (d) (3) (A) (ii) (II) category.
- Eliminate the WOTC SNAP age ceiling.

NEON strongly recommends that the American Work Force Group and the Ways and Means Committee incorporate H.R. 6833 into any bill to extend the Tax Cut and Jobs Act.

Another enhancement to WOTC that NEON enthusiastically encourages would be to clarify that the US DOL has the authority and is the final word in issuing regulations and procedures under the program. At times, the state workforce agencies that administer the program on a day-to-day basis in coordination with DOL issue conflicting rules and DOL has been reluctant to intervene unsure of whether they have the authority to do so. We urge the Committee to make clear that DOL has such authority in the interest of strengthening program administration.

Finally, NEON would point out that up until 2020, WOTC was renewed often on a yearly basis and in many instances on a retroactive basis. The program uncertainty impacted both employer enthusiasm to participate in the program and the willingness of the SWAs to dedicate resources and attract staff to administer the program. This changed dramatically starting in 2021 when the program was renewed for five years. As a result, the number of WOTC certifications and thus savings to the federal government in public assistance programs rose from less than 2 million prior to 2020 to a high of 2.5 million in 2022. That is why NEON believes that program continuity is essential to employer participation and commitment from the SWAs to dedicate the resources and staff needed. We strongly urge the American Work Force Group and the Committee to make WOTC permanent since after nearly three decades the program has proven that it is successful in helping those eligible to enter the workforce and while at the same time reduce public assistance expenditures.

Sincerely,

Kitty Leggieri

President

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The Work Opportunity Tax Credit
The New York State Experience

An Exploration of the Costs and Benefits

1996-2003

November 2003
NYS Department of Labor

George E Pataki Governor
Linda Angello Commissioner of Labor
Hy L Dubowsky Principal Researcher
Albany, New York

Executive Summary

This analysis is designed to provide a framework for discussions on the Work Opportunity Tax Credit (WOTC) as part of the current re-authorization efforts. WOTC expires on December 31, 2003. The study focused on the New York State (NYS) WOTC experience, from the program's creation in 1996 through the close of the current FY 2003 program year. Using WOTC activity in NYS, a cost-effectiveness review is developed that indicates net recurring taxpayer savings totaling approximately $200 million from reduced Temporary Assistance for Needy Families (TANF), correctional services and vocational rehabilitation spending, enhancing the ability of the hard-to-employ to secure private sector employment, makes good budgetary sense.[1]

Obtaining a job has a myriad of benefits for any job seeker, but especially for the economically disadvantaged facing barriers to employment. Increased self-esteem, family well-being and a reduced reliance on public services are concurrent benefits associated with finding work.

This study is by no means conclusive. Rather it raises several interesting research questions which merit further study. Specifically:

- Do taxpayer benefits outweigh the one-time costs of WOTC?
- Are focused education and marketing efforts needed to stimulate WOTC utilization for the nine WOTC target groups?
- Do WOTC participants remain in the workplace?

Questions on this study should be addressed to Hy L Dubowsky PhD, Principal Researcher at 518-457-6823.

[1] Additional savings would be generated from reduced Medicaid, Food Stamps and SSI costs that are not included in this study.

NYS WOTC STUDY

The NYS Department of Labor analyzed the WOTC and Welfare-to-Work (WtW) tax credits to provide an assessment of its public benefits relative to their direct and indirect costs. The study is designed to provide a statistical framework to assess the effectiveness of WOTC/WtW in encouraging private sector employers to hire economically disadvantaged and hard-to-employ individuals. Several questions, notably, the churning issue, have been addressed in a previous monograph issued in 1998.[2] This analysis revisits the cost-benefit review with the context of a maturing program. The study will also examine the effects of WOTC/WtW on retention periods compared to targeted employees who were hired without any tax incentive. Specifically the study will address:

- The benefits/costs of the WOTC;
- The characteristics of the WOTC employee;
- The effects of September 11 on WOTC hiring patterns of targeted workers; and
- The effects of the WOTC credit on TANF recipients transitioning to private sector employment.

STUDY METHODOLOGY

Datasets

Labor Department staff from the Economic Development Services Unit (EDSU) and the Division of Research and Statistics (R&S) developed datasets from the tax credit database, social services wage reporting system (WRS) and employer combined quarterly wage records. There are 235,936 employee records in the WOTC database. This raw data set formed the basis for the WOTC benefit-cost analysis.

Time Period:

The following periods are used for this analysis:

- 1996 (Q1) through 2003 (Q4) for the WOTC program;
- 2001 (3Q) through 2003 (4Q) for an assessment of the effects of September 11 terrorist attacks on WOTC utilization;
- 2001 (2Q) through 2003 (2Q) to explore the effects of WOTC on TANF employment.

[2] Hy L Dubowsky, "An Analysis of the Work Opportunity Tax Credit in New York State, October 1995-March 1998", NYS Department of Labor, (1998), Albany, NY.

Databases Used

- Tax credit application and processing database-NYSDOL;
- Welfare Management System-NYS OTDA;
- Combined Quarterly Wage Records-NYSDOL.

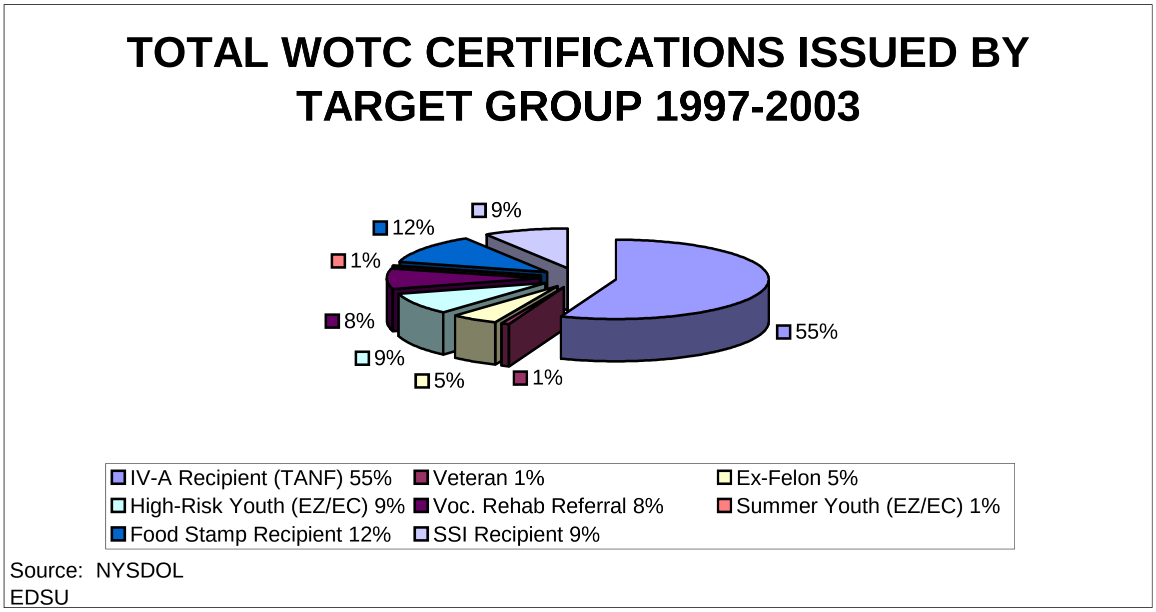
BACKGROUND

WOTC and Employment Data

WOTC recognizes nine target groups, each with its own distinct set of characteristics that, in and of themselves, form barriers to employment.

Figure 1 shows the composition of the WOTC employee population since the program's inception in 1996. Until 1997, WOTC recognized only eight target groups. In 1997 SSI was added. The WtW tax credit was also created in 1997. Sometimes referred to as the tenth WOTC group, it is a separate credit (Section 51a IRC) administered within the WOTC administrative frame.

Figure 1 WOTC Utilization by Certification



Since WOTC was first authorized in 1996, NYS has certified over 114,000 individuals with barriers to employment. The majority of the state issued WOTC certification activity derives from employing TANF and Food Stamp recipients. The emphasis on employability development for TANF recipients is the cornerstone of the Personal Responsibility of 1997, laying the foundation for the subsequent welfare reform efforts that swept the country. The policy shift that recognized the dependent nature of the existing welfare system focused resources and incentives towards independence through employment. Together, TANF and Food Stamp recipients comprise 67 percent of all WOTC certifications.

The remaining 33 percent of WOTC certifications are divided among the seven other target groups with mixed results. Despite an extensive employability network, the vocational rehabilitation community has yet to fully embrace the credit. Some have suggested that the success of the vocational rehabilitation efforts reduce the need for the added incentives. Still, others argue that identifying oneself, as a member of a target group may not only be self-denigrating but may dissuade an employer from making a job offer. Further study is necessary to more fully understand the complex nature of the hiring dynamic before a explanation as to why WOTC has not been more fully embraced by its other target communities.

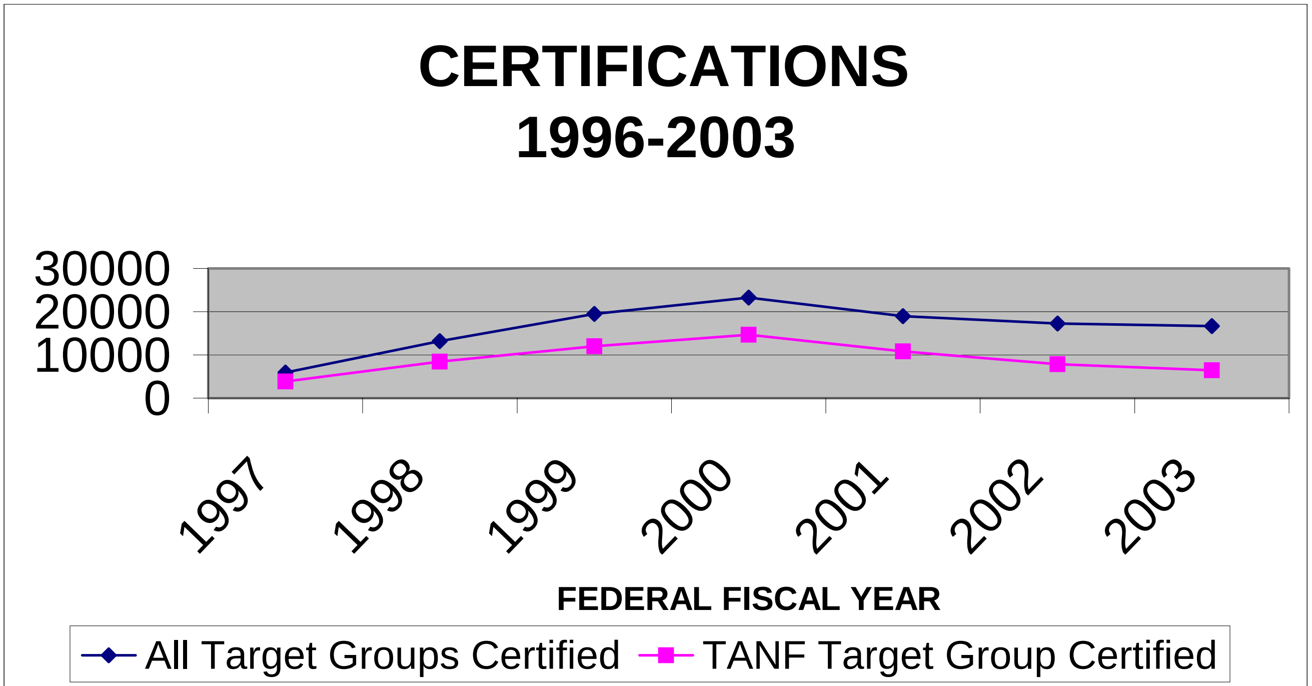
The sharp increase in WOTC, as shown in the Figure 2, started a year after the program's slow start, in 1997. Many in the WOTC community point to the widespread support by the employer community for welfare reform and the recognition of their critical role to provide jobs for people in need. These employer efforts were quite successful in NYS, supported in large part, by a partnership with Governor Pataki's welfare reform team.

The robust New York economy and the comprehensive welfare reform efforts led by Governor George Pataki had provided opportunity and the means to move those TANF recipients from the dependency of welfare into private sector jobs. Since July 1997, NYS has reduced TANF caseloads by nearly 60 percent: 219,496 cases representing over 679,000 individuals.[3] While some TANF cases may have closed or aged out, many of these closures were due to the successful transition from welfare to work. The September 11 terrorist attacks, however, brought this economic growth to nearly a crawl and with it, a dramatic loss in retail and service jobs - the very first job opportunities available to those with barriers to employment.

[3] TANF Caseload Data, BEAC Current News Reports, Office of Temporary and Disability Assistance, Albany, NY.

Figure 2 shows the trend in overall trend in WOTC utilization since the program's inception.

Figure 2
WOTC Certification Activity



Source: NYSDOL EDSU

The figure shows WOTC certification activity utilization reached its peak in 2000 as welfare reform efforts became integrated into corporate America's human resource's strategy and the national and state economies provided ample job openings. As New York successfully reduces its able-bodied TANF population through its combination of training and work first initiatives, the remaining TANF cadre requires greater concentration of services and job-readiness training. Within a year the national economic slowdown trickles down to the state and the catastrophic events of September 11 put a halt to the progress made in assisting job seekers with barriers to employment.

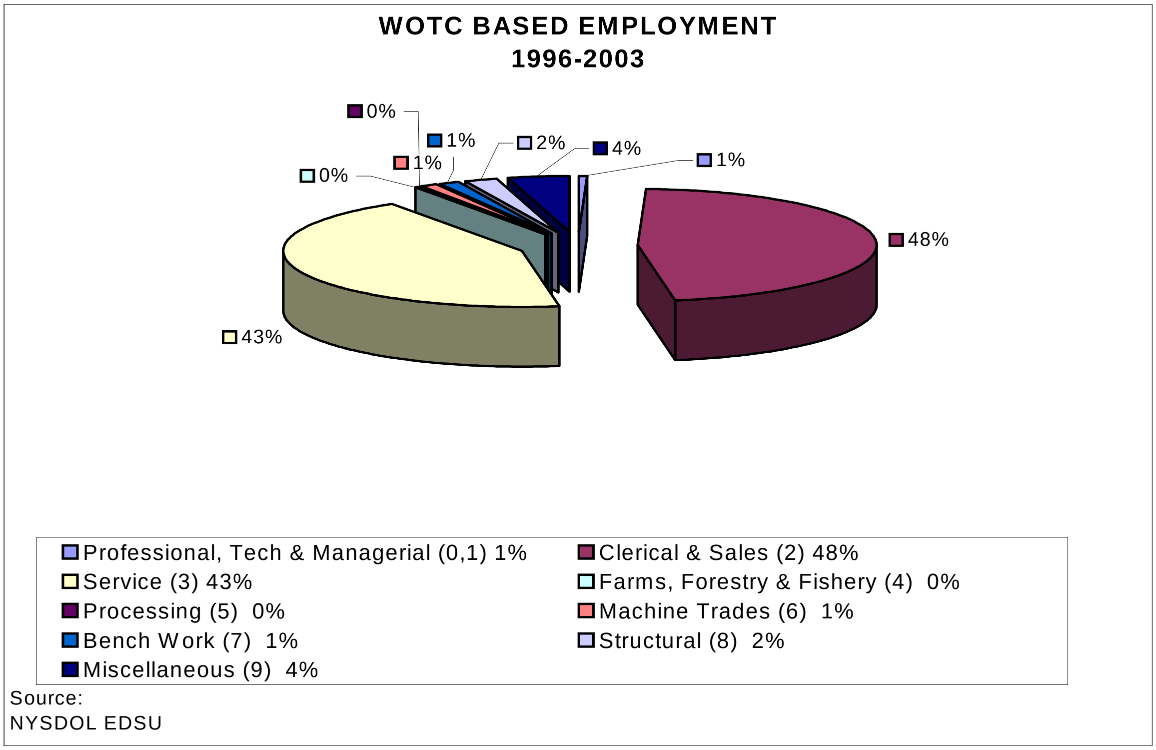
Wages and Positions

During the study period, 2001 (2Q) through 2003 (3Q) WOTC certified employees have earned in excess $90 million in private sector wages.[4] These wages, for many, represent the first paychecks ever received while for others it signifies a break from the vicious cycle of poverty. As shown in Figure 3, the majority of positions are

[4] Data extrapolated using New York State Department of Labor, Research and Statistics Division, Combined Quarterly Wage reports.

either in the retail or service sectors of the economy, the traditional place where first and low skill jobs are located. Many of these employers offer career pathways and encourage new employees to remain and grow with the company. While not all represent career paths, securing a job is the essential first step.

Figure 3
WOTC-Employment Categories

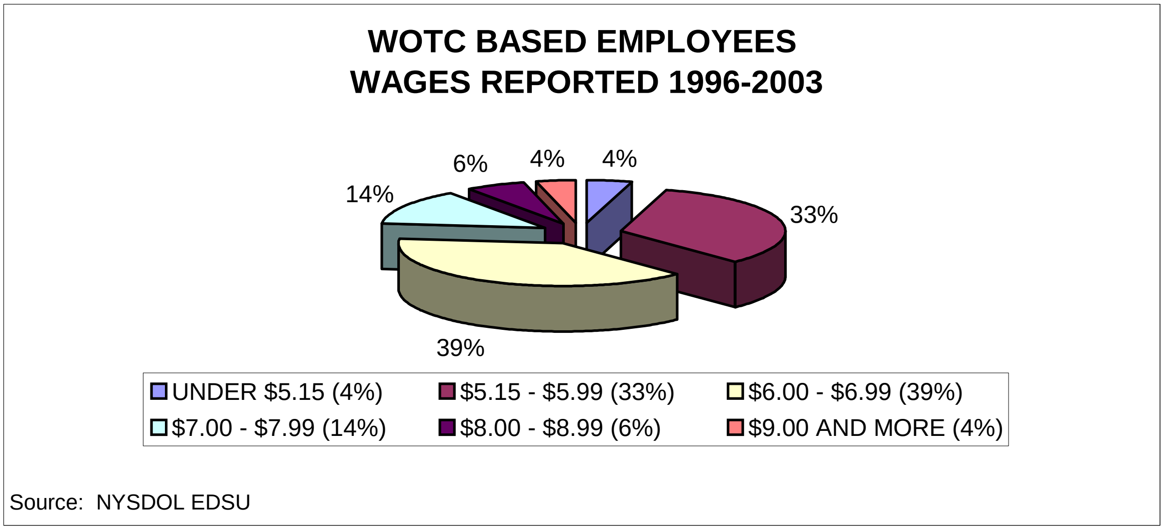


WOTC certified recipients earn slightly more on average than the federal and state minimum hourly wage, $5.15 per hour, largely reflecting regional salary patterns. Seventy-two percent of the certified recipients earned between $5.15 and $8.99 per hour. Fifty-seven percent earned hourly wages totaling $6.00 or more[5].

[5] NYS Department of Labor, EDSU database as reported on the ETA 9061 Individual Characteristics form. .

Figure 4

WOTC-Employment-Wage Groupings



The number of WOTC-eligible jobs remained fairly constant following its decline starting in 2000 and accelerating after the September 11 attacks. The effects of the loss of higher paying financial service and tech positions ripped through the retail and service sectors, displacing tens of thousands of entry level workers and spilling further into neighborhoods through the City and throughout the state. With fewer employment openings, there are fewer opportunities for the hard-to-employ. This in turn necessitates the need to provide employer incentives to modify their hiring decision in order to encourage employing the economically disadvantaged hard-to-employ job seekers who face barriers to employment.

The Effects of WOTC

Business

WOTC provides a one-time federal tax credit totaling up to $2,400 for each qualified hire. The credits are a loss of federal business tax revenue shown as tax expenditures by the Treasury Department and Office of Management and Budget. The one-time tax expenditures affect market behavior by lowering the effective wage of qualified WOTC/WtW employees, offsetting the inherent costs associated with hiring workers with barriers to employment.

In New York, employers have earned approximately $275 million in potential WOTC credits since 1996. The net value of the credit is somewhat less after incorporating tax code offsets such as tradeoff of the payroll deduction for the credit on salaries paid to targeted workers roughly $183 million. Examining these potential tax savings in terms of potential sales and business services translates into increased economic activity in excess of $1.8 billion.[6] This is a powerful economic stimulus from these one-time

[6] Assumes a effective 35 percent federal tax rate and the gross value of the WOTC credit,

employment tax credits. No firm escapes these benefits, though the net benefit is a function of the unique nature of each firm's production and operating costs.

Taxpayers

As targeted workers transition from TANF and other public programs, recurring budget savings are generated. Freeing taxpayers' funds provides the Governor with greater discretion in allocating scarce state resources. Entitlement spending, notably TANF, is mandated by law. Ending the cycle of TANF dependence has multiple beneficiaries with the NYS taxpayers saving approximately $6,600 in federal and state taxes for each case closed.[7]

Transitioning other targeted individuals to work has similar benefits. Direct, state vocational rehabilitation savings total approximately $340 on average, per employee, as consumers leave direct VESID services and enter employment.[8] The VESID support network is comprised of a myriad of private and not-for-profit partners who use the tax credit as an employability tool. WOTC is often combined with other incentives such as on-the-job training, to further enhance the job seekers ability to obtain employment.

Ex-felons generate the greatest taxpayer savings should they succeed in finding work and remaining out of prison. According to a report on the costs of prison costs, the daily cost to incarcerate an adult in New York State is approximately $96.72, per day, annualizing to $34,800.[9] As ex-felons are released from state prisons, they face tremendous barriers to employment. Failing to obtain employment is a leading cause of recidivism. Efforts of the New York State Division of Parole, Department of Labor, Department of Corrections and numerous community-based organizations dedicated to serving this targeted population, have resulted in New York enjoying the Country's lowest recidivism rate, roughly 40 percent.[10] Of those returning to prison, however, approximately 89 percent were unemployed at the time of their arrest.[11]

Each successful private sector placement results in recurring societal benefits and taxpayer savings. Additional savings from reduced levels of government support, including food stamps, health-care, and SSI services are also generated by the placements.

Cost-Effectiveness

Comparing the cost of WOTC as measured by the value of the tax expenditures compiled by the Treasury Department, there is a net measurable benefit. Table 2

[7] Average taxpayer savings from closing a TANF case for a NYS family of three using a median between 1998 and November, 2003 case cost estimates,
[8] NYS VESID, Memorandum of Support to the Legislature, 2002, Albany, NY.
[9] New York State Department of Corrections, Albany, New York, in Connecticut Office of Legislative Research, "Department of Corrections Issues", Report 2003_R-0469 Kevin E McCarthy, principal analyst, June 2003.
[10] New York State Department of Corrections, Albany, New York
[11] New York State Division of Parole, Albany, New York.

provides information on the potential taxpayer cost of the WOTC credit compared to the overall benefits provided to New York State taxpayers.

TABLE 2
Potential Cost (Taxpayer Savings)
WOTC–based Employment
(Dollars in millions)

WOTC COSTS	
Potential Value of WOTC tax credit certifications issued	$275.39
Adjusted Value to Employers[12]	$183.59
Direct appropriation for administration	$ 9.05
Total Costs	**$192.59**
WOTC Potential Savings	
TANF Cases Closed	$423.21
VESID Services Reduced	$222.75
Reduced jail spending	$ 3.28
Total Gross Potential Recurring Savings	$649.24
Adjusted Potential Recurring Savings [13]	**$392.48**
Cost Recurring Effectiveness: Net Savings/(Costs)	**$199.89**

The recurring benefit stream generated by transitioning the hard-to-employ to the world of work exceeds the one-time cost of the WOTC credit. As the table indicates, the total tax expenditure, as measured by the net federal tax revenue loss is lower than the recurring taxpayer savings. The WOTC program provides net benefits to the taxpayer. The additional benefit from the addition of new wages to the Gross Domestic Product (GDP) or reduced reliance on Medicaid and other public support programs provides further benefits.

Economic Benefits

Economic benefits are realized from the economic stimulus caused by the inclusion of the additional wages paid to targeted workers. The $90 million in wages paid to WOTC workers since its inception in 1996, generated roughly

[12] Adjusted for the loss of corresponding deductions for payroll expenses.
[13] Assumes 42 percent of WOTC-TANF certified employees and both 35 percent of WOTC-VR certified and Ex-felon certified employees, respectively, will terminate their employment and return to government supported services or be incarcerated thereby reducing the recurring taxpayer savings.

$225 million in increased economic activity in the NYS economy using a “2.5 times” economic multiplier[14]. Encouraging employers to hire targeted workers with barriers to employment increases the GDP when projected across the nation. Entitlement payments are excluded from the GDP while wages are included. Providing incentives for hiring targeted workers and, therefore, not only makes good business sense but also offers elected officials to make a sound good public policy choice.

Additional Savings/Benefits

The Rockefeller Institute of Government released a report in 2002 that attempted to provide information on the outcomes of TANF families in NYS that affected by the welfare reform program started with the passage of the Personal Responsibility Act of 1996 and the NYS Welfare Reform Act of 1997 (which codified the state’s plan). The study tracked TANF recipients who entered into employment indicating that roughly 70 percent received some type of employee benefits package above the base salary. Of the sample populations studied, in excess of 60 percent of those working received health insurance benefits, paid vacation and sick days.[15] These benefits generate even greater taxpayer savings as with the reduced reliance on publicly supported Medicaid as the health insurer of last resort.

The Report indicated that nearly 61 percent of the study’s respondents reported that employment was the main reason for leaving TANF. Most importantly, perhaps are the findings of “family well-being”.

> “The Rockefeller study reported that “individuals with positive perceptions of post-welfare life experience, had, along with the better off group, higher levels of food security (though they were most likely to use a food bank or shelf) and were the least likely to have used a homeless shelter. They also reported the lowest use of domestic violence services, and no relatively lower levels of drug/alcohol counseling than either the status quo or the group with negative perceptions.”[16]

These family well-being indicators, while difficult to quantify, clearly have positive societal benefits. Similar satisfaction outcomes are also associated with the transition from supported services, direct government subsidy or incarceration by the state to the world of work.

Retention-Further Findings

The notion of welfare reform was transformed in 1997 from direct support to focused employability development leading to employment and independence. Using a sample of NYS TANF recipients who were certified as WOTC eligible during 2001 (2Q), indicate that WOTC has had a contributing effect on transitioning individuals from welfare to work. Examining NYS Welfare Management System (WMS) records and wage reports, roughly 58 percent of the TANF recipients who entered private sector

[14] NYS Department of Labor, Research and Statistics, Albany, 2003.
[15] “Leaving Welfare, Post-TANF Experience of New York State Welfare Families”, The Rockefeller Institute of Government, March 2002, Albany, NY.
[16] ibid

employment with the assistance of WOTC were found not to receive any public assistance benefits when their cases were later examined in 2003. This is consistent with the findings in the Rockefeller study cited above.

Nearly 23 percent of the study group had remained with the original employer, two years after first being hired. This, despite turnover rates in the service and retail sectors totaling almost 100 percent. The credits apparently have had an effect on retention, especially the long-term Welfare-to-Work credit. Of this group, combined quarterly earnings increased by 27 percent over the two-year period-a rate well above inflation and changes in the minimum wage.[17]

Conclusion

The Work Opportunity Tax Credit program provides a one-time financial benefit to encourage employers to hire individuals with barriers to employment. In turn for this one-time benefit, recurring taxpayer savings are generated, community and family “well-being” is enhanced, and positive economic effects take place on a macro-economic basis. The program pays for itself and should be continued as integral part of the Nation’s workforce development strategy.

Further research is warranted on proposals to extend the program to other target groups. Consideration should also be given to broadening the study to include other large WOTC states in an attempt to create a national cost-benefit model.

[17] NYS Department of Labor, Research and Statistics, Albany, 2003.

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May 19th, 2023

The Honorable Lily Lawrence Batchelder
Assistant Secretary
Office of Tax Policy
United States Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

The Honorable Brent Parton
Acting Assistant Secretary of Labor
United State Department of Labor
Employment and Training Administration
200 Constitution Avenue, N.W.
Washington, D.C. 20210

Dear Assistant Secretary Batchelder and Parton:

I have been asked to comment on the 2023 Green Book proposal to eliminate the employer tax credit provisions of the Work Opportunity Credit (WOTC) program for eligible employees who work more than 120 but less than 400 hours.

I have written about and analyzed the operation of the WOTC program at some length in the past. The fundamental argument used to create and sustain the program was and is to help individuals who struggle to get jobs to overcome the challenge of having no work experience and the additional disadvantage of trying to find a job when they do not already have one.

What WOTC is Not: There are often misconceptions about WOTC. It is not a program to create jobs for recipients nor is it a program to only support "good" jobs. While the ultimate goal of all workplace assistance programs including WOTC is to get participants into good jobs, those jobs are difficult to get: Many people want them, and they typically require skills and experience that not all candidates have. Short of an academic degree or specialized certification, it is extremely difficult for anyone to get a good job without already having had work experience. With few exceptions, WOTC-eligible candidates lack a record of recent work experience. WOTC can help address the lack of work experience and an employment record that are necessary conditions for having a chance at good jobs.

Why are employers reluctant to hire individuals with the attributes that make them eligible for WOTC? The simple answer is that they believe that these candidates are risky to hire for fear that they will not succeed in the jobs. It is costly to hire workers who do not succeed or who just leave: the administrative costs of bringing individuals into new jobs are considerable as is the lost work that comes while the job is vacant and the employer waits to fill it.
Some of the reasons that workers do not succeed may have nothing to do with them personally. They may have issues outside work that lead to absenteeism and life challenges such as family demands or resource constraints that limit their ability to get transportation to work. Others have difficulty holding a job just because they cannot handle the discipline of staying at work all day for an entire week, still others cannot get along with other workers, and so forth. If someone has a record of having succeeded in a job already, employers rightly believe the risk of hiring them is reduced.

A complaint one sometimes hears about WOTC and other tax credit programs is that it should not be necessary to subsidize employers to hire WOTC participants for the jobs for which they are considering them as candidates, which are often low quality in terms of pay and benefits. The simple rebuttal is that if WOTC was unnecessary, then the individuals with the disadvantages that WOTC recipients have would not be struggling to get jobs. It is also true that there is nothing unique about WOTC in using tax credits to encourage employers to take all kinds of actions useful for the public interests that might not otherwise be in their financial interest to do.

A Proposal for Changing the Tax Credit: At present, employers receive a tax credit up to 40% of the first $6,000 in wages paid to a qualifying WOTC hire if the individual remains on-the-job for at least 400 hours.[1] While there is nothing magical about the 400 hour figure, the idea is that 400 hours of work is at least long enough for a worker to learn the ropes and start to become valuable to an employer. If they stay in the job less than 400 hours but more than 120, the credit percentage is cut considerably, to 25% of eligible wages. The reason for allowing some credit below 400 hours is first that employers deserve some credit if they hire WOTC-eligible candidates even if they do not stay in part to cover the administrative costs of hiring them, which includes managing the WOTC process. Further, as described in detail below, when employees leave an employer, it is almost always because of their choice, not the employer's. But the employer bears the turnover costs of replacing them. That modest tax credit compensates them at least somewhat for taking the greater risk that hiring WOTC-eligible workers will not work out. The additional credit for remaining 400 hours also creates an incentive for employers to do all they can to keep WOTC-eligible employees on the job longer.

[1] There are exceptions that can raise the credit considerably for some limited groups, particularly Veterans under special circumstances.

The 2023 Green Book proposal is to eliminate the partial tax credit for hours more than 120 but less than 400 such that employers get no tax credit if their WOTC employees leave sooner than 400 hours.

Problems with the Proposal: The problem with this proposal begins with the question, *what problem is this trying to solve?*

There are several unstated assumptions implicit in the proposal.
The first of these is that turnover is caused by employers dropping workers. In fact, *the vast majority of turnover is caused by employees quitting*. The Bureau of Labor Statistics most recent data for February 2023, for example, finds that 70 percent of all turnover, or separations, come from employees quitting. Employers typically have no interest in employees quitting, hence the consternation over the post-pandemic "Great Resignation." Employee quitting is very common. The "accommodation and food service" category of jobs, where many WOTC candidates work, has a 70 percent annual quit rate.[2] If we thought that those quits were equally spread out over time, 15 percent of the workforce would have quit before hitting the 400 hour mark, which is the WOTC threshold for a full subsidy. Estimates of exactly when people quit come mainly from private sources, but they suggest that a remarkable percentage of those quits happens early in a job: 34 percent of white collar employees report that they have left a job in the first 30 days, and another survey finds that 28 percent who quit do so in the first 90 days.[3] In other words, in the absence of WOTC, many employees quit before 2.5 months or the 400 hour mark.

That leads to the question as to why we would punish an employer who agreed to hire a WOTC-eligible candidate if the candidate quits, as large numbers are likely to do.

Of course, under the realm of unintended consequences, employers could easily meet the 400 hour requirement with restrictive covenants such as non-compete agreements, something that is already common in the labor market even for low-wage workers. An employer could simply require that WOTC eligible workers agree to stay past the 400 hour window or pay some substantial penalty that could be enforced until that threshold is reached. Cutting any tax credit until a WOTC worker hits that 400 hour market vastly increases the incentives for an employer to prevent those workers from leaving.

Would it be in the public interest to encourage practices that prevent WOTC workers from leaving before 400 hours? Employees typically quit to move to another job. That is especially so for new entrants to the labor market. The literature on this topic is extensive and concludes, for example, evidence that even in a period when mobility across employers was low, one-third of all the growth individuals experienced over their careers came from changing employers (the rest came from advancement within an organization).[4] More recent research from 1997 to 2017

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[2] Bureau of Labor Statistics Economic News Release, Job Openings and Labor Turnover Survey. April 4, 2023.

[3] These estimates come from Zogby Poll's surveys of individuals. The first is result is: Job Seeker Nation Survey. Jobvite. https://www.jobvite.com/wp-content/uploads/2020/05/FINAL-Jobvite-JobSeekerNation-Report1_5-11.pdf. The second comes from Jobvite. 2018. https://www.jobvite.com/blog/onboarding/how-to-create-a-seamless-onboarding-process/. There are many similar estimates, https://www.linkedin.com/pulse/why-do-33-new-hires-quit-within-six-months-vultus-inc-.

[4] For a classic study, see Topel, Robert H. and Michael P. Ward. 1992. Job Mobility and the Careers of Young Men. Quarterly Journal of Economics. 108: 439-479.

supports that conclusion.[5] A post-pandemic study finds even more powerful evidence for low-wage, non-college workers of the kind targeted by WOTC, that changing employers was associated with significant increases in pay, more so than in earlier periods.[6] These studies and others like them arguably understate the effects of quitting because they measure all job changes, including layoffs and other separations, and we know that those lead to lower wages.

The evidence is clear that seeking better jobs is the primary motivation for quitting. Seventy percent of those who quit in 2021, for example, report that they did so either because their current pay was too low or because they saw no opportunities for advancement.[7] In tight labor markets, simply having a job already even if one has only been hired recently may be enough to give one a boost into another job elsewhere. Punishing employers by withdrawing all tax credits if their workers quit seems to be a perverse practice.

The second assumption is that it might somehow be *in the employer's interest to churn through WOTC employees to get the tax credit.* This is not a sensible assumption because the turnover costs greatly exceed the costs of the tax credit. The administrative costs of bringing on a new worker, setting them up in a payroll system, and so forth are roughly $4000. The productivity costs of losing a worker and then replacing them with a new, inexperienced candidate are likely considerably more. Even in the simplest jobs that have no formal training and where we think anyone could do it at a satisfactory level having never done it before, there are things to learn in each context to avoid making mistakes, some of which may be a simple as learning to coordinate with other workers. Accurate estimates of turnover costs in low-skill, hourly work find that the largest of these costs are lost productivity associated with other employees that begin as soon as a worker announces they are going to leave.[8] Further, when the employer separates an employee, their unemployment insurance costs rise, another cost of churning through employees.[9]

These turnover costs are the reason there has been so much employer consternation about retention, especially among low-skill, hourly workers where turnover has been so high after the pandemic.

One might argue that there must be situations where churning through workers to get the tax credit pays off. That implies situations where employers would create jobs with more than 120 hours but less than 400 hours just to get the reduced 25% tax credit. Critics sometimes suggest that the "temp" industry creates those situations. To understand the context, temporary agencies account for much less of the workforce than we typically think, 2% of the labor force.[10] Most

[5] Jeffrey J., Yankow 2022. " The effect of cumulative job mobility on early-career wage development: Does job mobility actually pay?" *Social Science Quarterly*. 103: 709– 723.

[6] David Autor Arindrajit Dube & Anne McGrew 2023. The Unexpected Compression: Competition at Work in the Low Wage Labor Market. NBER Working Paper 31010 March.

[7] Pew Research Center. 2022. Top Reasons Why Employees Left a Job in 2021: Low Pay and No Advancement Opportunities. March 8th.

[8] Peter Kuhn and Lizi Yu. 2021. How Costly is Turnover? Evidence from Retail. Journal of Labor Economics, 2021, vol. 39, issue 2, 461 – 496.

[9] The practice of unemployment insurance taxes varying with layoffs, experience rating, is rooted in Federal policy but in practice varies by state.

[10] What Happened to Temps? 2021. Changes Since the Great Recession. Monthly Labor Review. February.

temps are engaged as independent contractors, not as employees and as such are not eligible for the WOTC program. Only agencies that have regular employees are eligible for WOTC payments, and those employers have all the turnover costs noted above. Individual projects for temp agencies may be relatively short, just as accounting and consulting projects are short, but employees in those fields work on a stream of assignments just as temp agencies with employees move their employees onto other projects. The assertion is that rather than keep WOTC workers on until the 400 hour mark and claim the full tax credit (at 40% of up to $6,000 in wages), for some reason they drop them after 120 to get the reduced 25% credit. (Churning through three employees to get a reduced tax credit makes no sense as compared to keeping one worker for 400 hours and getting the full potential credit.)[11]

Most temp agencies with employees now are not being used to meet short-term staffing needs in any case. They have become "leasing agencies" and their employees as leased in long-term relationships to a client organization: The US Bureau of Labor Statistics defines leased employees as those that work for a client for at least a year.

It is also worth noting that temp agencies are themselves a separate pathway into regular jobs. A recent survey of companies with more than one thousand employees found that 10 percent of their temp agency workers were turned into their regular, full-time employees.[12] Those workers are offered jobs that are a step up from what they had been doing because they have work experience doing the same tasks presumably successfully. Such jobs are arguably better than the WOTC participants could have secured without that work experience. It is in the interest of an agency for their employees to transition to regular employment with a client because the clients then are required to pay the agency fees, which can be substantial. But it is also in the interest of public policy for that to happen.

Is there any scenario where any employer might need labor for short-term assignments less than 400 hours but more than 120 and might not want to go to a temp agency to get them? Most employers meet those tasks with a separate category of employees called "On-Call" workers, regular employees who are often with employers for a long period of time but paid by the hour. Most of these on-call workers have a long-term relationship with the employer. They may be retirees returning for special projects or workers with family care or health issues that prevent them from working regularly. The huge advantage of on-call workers is that they know the organization, they likely know the regular employees, and they know the job. It is hard to see an advantage in replacing on-call workers with new hire WOTC candidates who have no track record of successful employment.

If for some reason an employer had short-term assignments and did not want to use on-call workers or temp agencies, the popular alternative now is to engage "gig" workers, independent contractors who come in to perform a specific task for a short period of time. Doing so avoids all the administrative costs of hiring and employing a worker.

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[11] It should be noted as well that WOTC is designed to discourage churning. Under the statute no credit is available for an employer with respect to any individual who previously had been employed by the employer at any time.

[12] "Temp-to-Perm Conversion Ratio," Contingent Workforce Strategies, cwstrategies.staffingindustry.com/temp-to-perm-conversion-ratio/ (accessed January 30, 2023).

The proposal to drop the tax credit for 120 hours of work therefore would therefore target only regular employers who had jobs that they know in advance would require more than 120 hours but less than 400 hours of work; where they decide not to use “on-call” workers or gig workers; where the administrative costs of using the WOTC process, the costs of turnover, and the greater risk of using WOTC-eligible candidates combined is less than the reduced 25% credit. There is no evidence that such employers exist, but one might argue that even if there is a single employer doing so, we should design the program to prevent it.

One problem with doing so is that eliminating the partial credit for employees who leave before 400 hours defeats the purpose for which it was designed, to provide some compensation for the much more common situation where employees leave or simply cannot perform the job. Aside from the question as to whether it is fair to punish employers in that situation, removing the credit changes the employer view about WOTC: Is the tax credit enough of a benefit to cover the additional risk of hiring a WOTC candidate knowing that if they do not stay for 400 hours, I get nothing? This proposal reduces the expected value of the WOTC tax credit and in turn the chance of giving the nod in hiring to WOTC-eligible individuals over other candidates.

The final assumption is that jobs that end in less than 400 hours are bad jobs. That is fallacious. First, the 400 hour requirement refers only to when a WOTC-employee leaves employment and not whether the job ends or continues and is filled by someone else. As the evidence above showed, employees can and do leave good jobs. Their time in the job does not define its quality. Second, there can be jobs that we know will have short tenure – seasonal jobs at resort locations for example - that can be attractive despite not having the prospect of continuing.

If we return to the opening question, what problem would be cutting the tax credit for employees who stay more than 120 hours but less than 400 solve, there is no compelling answer. We can clearly see the downsides of doing so, which will affect every potential employer considering a WOTC hire. There are no apparent benefits. It is difficult to see given the examples above why employers would knowingly put themselves in the situation of creating actual jobs of more than 3 weeks but less than 400 hours when they could instead combine them and have fewer jobs lasting longer and capture the bigger 400 hour tax credit. The idea that there is a cohort of employers creating such jobs is implausible.

Again, what this proposal would therefore rule out would only be situations where an employer knew going in that they had work that would not continue (which is not the case for a temp agencies) and would last longer than three weeks but less than 400 hours and that could not be linked together to create 400 hour jobs securing the bigger tax credit; that a reduced 25% credit was enough to offset the hiring costs and administrative costs of the WOTC program; and finally, that the common alternatives of gig work or temporary help that avoided hiring and employment costs altogether was not preferable. We have no evidence that such situations even exist. In return, it reduces the willingness of any employer to take on a WOTC-eligible candidate.

In short, this proposal is a solution in search of a problem.

Sincerely,

Peter Cappelli
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cc: Members of Congress