Evaluations of the WOTC and WtW Tax Credit

Studies of the two employment tax credits have been limited in purpose or scale. Shortly after the State Employment Security Agencies (SESA) began implementing the WOTC in late 1996, the United States Department of Labor (DOL) contracted for an evaluation of its administrative process (which, as noted above, is the same as the WtW credit's). Among other things brought out in the August 1997 study, state WOTC coordinators recommended that the paperwork burden on employers be reduced and Form 8850 be made less confusing so that small employers particularly and all for-profit employers generally would be more inclined to participate.[26]

In March 2001, the General Accounting Office (GAO) surveyed a sample of employers who utilized the WOTC program in two states with high certification levels, namely, California and Texas. The study's chief goal was to ascertain whether employers fire workers who never were eligible for the WOTC or who no longer are eligible for the WOTC in order to maximize credit receipt. The GAO concluded that—while it could not definitely determine the extent of displacement and churning, respectively, across all employers who participate in the program—the sample data suggest that employers do not view the practices as cost-effective and therefore presumably would not engage in them much, if at all. GAO's estimate that the WOTC offsets less than one-half of the cost of recruiting, hiring and training credit-eligible workers, on average, supports the employers' belief that the practices are not cost-effective. Regarding churning specifically, certified workers in the two states were found to be no more frequently terminated when their earnings totaled about $6,000 (the credit-maximizing level).[27]

A study of the WOTC/WtW credit that was undertaken for the DOL also was released in March 2001. Interviews of 16 establishments that had used the credits were conducted in five states (California, Georgia, Maryland, Missouri, and Wisconsin). As in the case of the GAO study, the authors emphasized that their findings cannot be extrapolated to all other user firms. Among the report's results:

- "the tax credits play little or no role in [the 16 employers'] recruitment policies," suggesting that employers would have hired members of the target groups even if the programs were not available;
- as credit-eligible hires' job performance, work readiness, attendance and punctuality were like those of ineligible employees in similar positions, most of the interviewed employers thought there was no need for special training or counseling programs;
- the target-group members who were hired exhibited the high rates of turnover typical of low-wage workers,[28] which meant that the interviewed employers were able to claim the maximum credit for relatively few eligible hires; and

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[26] Westat, *Process Evaluation of the WOTC Program* (DOL, Employment and Training Administration, Office of Strategic Planning and Policy Development, August 1997).

[27] GAO, *Work Opportunity Credit.*

[28] WOTC/WtW hires generally were paid the same entry-level wages as other hires, which largely ranged between $5.15 and $8.00 an hour.

- the 16 employers gave the programs a positive assessment, although they offered some suggestions for improvement having to do with program administration (e.g., consolidate and streamline the forms), program design (e.g., broaden target-group eligibility criteria)[29] and promotion of the program (e.g., increase use of conditional certifications).[30]

The report's authors recommended among other things that a study with a larger, representative sample of employers be conducted, as "these observations do raise a question about the extent to which the tax credit is serving the purpose for which it is intended—to serve as an economic incentive to encourage employers to hire individuals from specified target groups whom they would not have hired in the absence of the credit."[31]

An October 2002 analysis of participation rates for the WOTC's two largest eligible groups—TANF recipients and food stamp youth—estimated that relatively few eligible new hires have the credit claimed for them. In 1999, employers were estimated to have claimed the WOTC for less than one-third of newly employed persons from the TANF group and for less than one-fifth of newly employed persons from the food stamp youth group. Participation rates did increase considerably between 1997 and 1999; however, this was due not just to an increase in credit-claiming, but also to a substantial decrease in the size of the eligible populations during implementation of welfare reform. The author suggested various reasons for the low participation rates, including that the fairly short job tenure of the credit-eligible population (like that of other low-wage individuals) translates into a small tax credit value per WOTC-eligible hire. In other words, "Employers may be discouraged by the low returns to WOTC/WtW participation for those workers whose employment ends before the 40 percent credit is reached [i.e., before the individual has worked 400 hours or more]."[32]

In a December 2002 report, the GAO attempted to examine specifically the few tax incentives available for hiring, retaining, and accommodating workers with disabilities. Persons with disabilities are the focus of two WOTC-eligible groups, namely, vocational rehabilitation referrals and Supplemental Security Income (SSI) recipients. Based upon an analysis of 1999 tax year data from the Internal Revenue Service (IRS), the GAO found that relatively few employers utilize the WOTC. Data on employer usage by WOTC-eligible group are not available from IRS data, however. According to the agency's interviews with government officials and academic experts, fairly few persons with disabilities may have the credit claimed for them because WOTC eligibility is limited to disabled individuals receiving publicly funded vocational rehabilitation or SSI benefits. Perhaps not surprisingly, then, interviewees supported expanding the WOTC's coverage of disabled persons. The agency also identified two national surveys related to disability employment issues which determined that a very small share of supervisors of employees with disabilities were aware of employment tax incentives and that human resource managers regarded business tax incentives as less effective than any of the following measures in reducing obstacles

[29] These two recommendations echo those made in the 1997 process evaluation.

[30] See the section on Program Administration (*supra*) for the definition of a conditional certification and why it may be little used.

[31] Westat and Decision Information Resources, Inc., *Employers' Use and Assessment of the WOTC and Welfare-to-Work Tax Credits Program* (DOL, Employment and Training Administration, Office of Policy and Research, March 2001).

[32] Sarah Hamersma, "The Work Opportunity Tax Credit: Participation Rates Among Eligible Workers," *National Tax Journal*, vol. 56, no. 4 (December 2003), p. 736.

to the employment of persons with disabilities: top-management commitment, staff training, mentoring, on-site consultation and technical assistance, and short-term outside assistance.[33]

Another study that analyzed the tenure effect of the WOTC and WtW credit found, like GAO, that employers do not appear to terminate eligible hires when the subsidy period ends. This 2005 study, which compared WOTC- and WtW-certified workers in Wisconsin with eligible but uncertified workers in the state, also estimated a small absolute impact on earnings. Hamersma extrapolated from the Wisconsin data that "the average worker receives perhaps 40 percent of the value of the credit as an earnings premium; the rest remains with the employer."[34]

In 2007, Hamersma and Heinrich released an analysis of the labor market outcomes of credit-eligible group members at temporary help services (THS) firms which, although not end-user employers, are nonetheless able to claim the WOTC and WtW credits. Administrative data from Wisconsin show that over the 1999-2002 period, certifications issued to THS firms grew steadily. They found that, after taking into account observable differences between individuals, THS workers with certifications had much higher earnings than credit-eligible THS workers without certifications. "This suggests that some of the WOTC/WtW funds pass through to the THS worker in the form of increased earnings per quarter, just as they do (though to a lesser extent) for workers in other industries. Using panel estimation to examine longer-term outcomes, however, the earnings difference between these workers is no longer statistically significant."[35]

The researchers also compared the THS workers with certifications to workers in other industries for whom certifications had been issued and estimated that the THS group earned much less because of their much shorter job tenure. Hamersma and Heinrich also conducted a telephone survey of Wisconsin THS firms and found that a majority of the 101 firms that responded not only were aware of the credits but also claimed them.

> Contrary to legislative intent, however, only one firm reported that prospective employees' eligibility for the tax credits might affect their hiring decisions. Thus, our findings suggest that concerns about the use of WOTC/WtW funds to subsidize THS employment are likely warranted, since subsidies do not appear to improve the job outcomes of disadvantaged workers in these jobs nor encourage the hiring of additional disadvantaged workers as intended.[36]

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[33] GAO, *Business Tax Incentives to Employ Workers with Disabilities Receive Limited Use and Have an Uncertain Impact*, GAO-03-39, December 2002.

[34] Sarah Hamersma, "The Work Opportunity and Welfare-to-Work Tax Credits," *Tax Policy Issues and Options*, no. 15, October 2005, p. 5.

[35] Sarah Hamersma and Carolyn Heinrich, *Temporary Help Service Firms' Use of Employer Tax Credits: Implications for Disadvantaged Workers' Labor Market Outcomes*, Upjohn Institute Staff Working Paper No. 07-135, February 12, 2007, p. 5.

[36] Ibid.