







House Tax Package for Business

More economic incentives won't cure what ails us

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EXECUTIVE SUMMARY:

-  THE HOUSE VOTED YESTERDAY on a bill, H.B. 1973, to provide tax breaks to businesses that locate in the state.
-  AT AN ESTIMATED COST OF \$300 MILLION BY 2015, the incentives are an expensive and ineffective way to support the state's economic recovery.
-  THE MOST IMPORTANT SUPPORT to the state's economic recovery is job creation which many of the economic incentives proposed have failed to do in the past.
-  NORTH CAROLINA POLICYMAKERS SHOULD CONSIDER a Small Business Job Creation grant program and support for entrepreneurship to create jobs and stimulate continued economic growth.

THE HOUSE VOTED YESTERDAY ON A BILL, H.B. 1973, TO PROVIDE TAX BREAKS TO BUSINESSES THAT LOCATE IN THE STATE. The package will now be considered by the Senate. At an estimated cost of \$300 million by 2015, the incentives are an expensive way to support the state's economic recovery. Indeed, they are most likely to be used by businesses once the recovery has already taken hold, representing a waste of taxpayer dollars at a time when the budget is tight. The package provides businesses from specified industries—most notably datacenters and film production—with credits against their sales and use taxes while also extending the discredited Article 3J tax credits.

Rather than employing the same old incentives, it would make more sense for North Carolina's policymakers to apply these sizable funds to direct job-creation strategies—such as a Small Business Job Creation Grant—and efforts to stimulate local entrepreneurial ventures that will immediately spur economic activity without further complicating the state's already cumbersome tax code.

Playing an old game, on a changed field

North Carolina has been playing the economic incentives game for awhile. In terms of attracting business, the state has had some success. In terms of generating sustainable growth for communities and family-sustaining jobs, the picture is mixed.

In the current environment, when credit markets are tight and business confidence is low, it remains unclear if incentives alone can motivate a business to make the

decision to expand or locate in the state. In recent surveys conducted by UNC, both incented and non-incented businesses in North Carolina reported that these enticements are low on the list of priorities in selecting a business location. Both groups rank incentives 12th and 13th respectively, behind infrastructure and a skilled workforce.

The recent figures from the Employment Security Commission suggest that the private sector continues to remain reticent about expansion. Nearly 13,000 jobs were created in May 2010, which suggests that struggle to recover of all the jobs lost during the recession will continue well into the future. Nationwide, data from the Bureau of Labor Statistics showed low levels of job growth driven primarily by temporary Census employment opportunities. North Carolina, like the nation, is facing an economic development challenge unlike those of previous business cycles because of the projected length of time it will take to recover.

Without real and sustainable job creation, the severity of the job losses and the sheer number of workers out of jobs will serve as an ongoing drag on the economy.

Recent analysis has found that many of the incentives that are making their way through the legislature are ineffective at creating jobs. Most important are the findings on the impact of the Article 3J tax credits, which receive an extension in this bill. Over 40 percent of businesses receiving the Article 3J tax credit actually declined and shrank their number of employees from 1996 to 2006.

The General Assembly's Fiscal Research staff estimates that slightly more than 1,500 jobs would be created through the proposed incentives—a small amount when measured against the growing job gap of 420,000 that North Carolina faces to recover the jobs lost since the recession began while the workforce continued to grow. And the cost per job is significant in some cases.

Finally, the incentive packages outlined in H.B. 1973 are so targeted to specific industries that they are clearly meant to impact current deals being hammered out with the Department of Commerce. North Carolina is much better off not targeting specific industries, particularly those that could easily pick up and leave for out-of-state locations as soon as the incentive runs out, if not before.

Wise investments to spur job creation

North Carolina policymakers are right to look to supporting private-sector growth as key to the state's long-term recovery. However, there are far more effective tools available to support businesses that can create the jobs needed to get North Carolinians back to work.

One promising direct job-creation strategy previously recommended by the Budget and Tax Center is a Small Business Job Growth grant program. The program would provide a direct subsidy of \$10 per hour to the wages and benefits for jobs newly created by employers. Benefits of such a program include not only creating temporary jobs where workers can gain experience but permanent ones where workers can build long-term connections to work. As a grant program, the benefits are up front and can be used by businesses that aren't yet profitable, both huge benefits to businesses. And while such a program would require a significant investment, the dollars are guaranteed to create new jobs.

Another promising opportunity would be to improve the support to entrepreneurs seeking to start up new businesses. The House and Senate budgets include returning funding to the Small Business Centers located at community colleges statewide. But greater access to capital and tax credits for entrepreneurs could provide the needed financial resources to move from plan to action. For all the talk about the role of small business in job creation, recent evidence demonstrates that new and young firms are responsible for the majority of job creation in the country.

Conclusion

Business incentives are just one tool in the economic development toolkit and one better employed when tinkering with an economic engine not resuscitating one. At a time when the economic recovery needs the support of a labor force engaged in work and spending in local communities, North Carolina policymakers should measure all investments in terms of their immediate job creation goal. Targeted job creation strategies, like a Small Business Job Creation Grant program, and investments in local entrepreneurs will build the employment opportunities and new economic activity needed to continue the economic recovery.

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- 4 Employment Security Commission of North Carolina, June 18, 2010. North Carolina's Unemployment Rate Decreases for Third Consecutive Month.
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- 7 Stangler, Dane and Robert E. Litan. November 2009. Where will the jobs come from? Ewing Marion Kauffman Foundation.