TESTIMONY

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QUALITY JOBS PROGRAM: A CLOSER LOOK

By Patrick Ishmael

Testimony Before The Missouri House Government Oversight and Accountability Committee

To the Honorable Members of This Committee:

Ladies and gentlemen, thank you for the opportunity to testify today. My name is Patrick Ishmael and I am a policy analyst for the Show-Me Institute, a nonprofit, nonpartisan Missouri-based think tank that supports free-market solutions for state policy. The ideas presented here are my own. This testimony is intended to provide a brief explanation of how state economic development tax credits work, why they often do not work, and why the Missouri Quality Jobs (MQJ) tax credit program is worthy of close scrutiny in view of its development track record.

Many of you know that a tax credit is a direct reduction in a taxpayer's tax liability that a government grants for the performance of a government-desired activity. Tax credits are often used as a way to promote activities for the expressed or implied purpose of promoting economic development. In contrast to a *tax deduction*, which decreases a taxpayer's taxable income, tax credits are applied against a tax liability dollar for dollar, and although not technically considered spending by Missouri courts, public officials often portray tax credits as the state making "investments" in the economy. One need not look far to find a Missouri Department of Economic Development (DED) press conference or press release announcing, with great fanfare, the "new jobs" being brought to a community as the result of a tax credit.

Unfortunately, the jobs that are promised do not always happen, and part of the reason for this is that governments, by and large, are not very good at picking successful "investments" for their constituents. As economist F.A. Hayek once noted, "[t]he curious task of economics is to demonstrate to men how little they really know about what they

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imagine they can design." One person or government can hardly know "what everyone else needs" because "what everyone else needs" is different from person to person. Trying to centrally plan an economy to address the panoply of human desires is a fool's errand, whether that planner is a single person or a single bureaucracy. Indeed, one of my biggest concerns with excessive government interference in the economy has to do with waste. One dollar that the government taxes and spends on a politically favored activity is one dollar that the free market has not allocated on its own. So when we discuss economic development, we must ask ourselves — who do we trust more to make our state's "investments": the government or the marketplace?

That brings us to the Quality Jobs tax credit. Last year, Missouri Auditor Tom Schweich's report on the MQJ tax credit program found that although the DED had expected the credit to create more than 45,000 jobs in the state since 2005, in fact, "a total of 7,176 jobs have been created [as of July 2012]." The DED now projects that a total of 26,000 jobs will be created from MQJ tax credits,[1] but that is a far cry from what the state and the tax credit applicants have actually promised taxpayers, and still a far from certain outcome. Indeed, the MQJ track record suggests that the "actual jobs" count will fail to meet even this revised "projected jobs" figure. Time will tell.

In practice, there is no particular consequence to the state and its public officials claiming that new jobs will be coming, even if the jobs never materialize. That may explain the difference between the number of jobs state officials promise when a tax credit project is announced and the number of jobs actually created when the project winds down. To some officials, big tax credit promises look better than small tax credit promises, even if those promises do not pan out.

This conclusion seems to emerge from MQJ tax credit data as well. After reviewing MQJ data that the Show-Me Institute provided, Michael Hicks, Dagney Faulk, and Srikant Devaraj — researchers at Ball State University in Indiana — found that **the number of jobs promised was connected to the magnitude of jobs overstatements in MQJ projects.**

> What we found was that the size of the grant was very statistically linked to the size of the 'overstatement' of expected jobs to actual jobs created. This finding is far less sensitive to the types of concerns outlined [about job growth conclusions], and so we are more confident of this result. This should be a very strong cautionary note to anyone considering this incentive program, since this is a pretty clear statement that the size of the grant may be linked to the overstatement of the job creation of the project ….

Indeed, bigger jobs promises may simply mean the odds are higher that the applicant has overpromised and will ultimately underperform on those jobs promises. That is not good news for Missouri or the communities that may be depending on these projects, and it is a clarion call to all policymakers that make use of these press conferences to understand that their tax credit jobs promises too often fall through. Quite frankly, *far* too often.

Moreover, a limited analysis of the effectiveness of the MQJ program suggests that the aggregate economic effect of the MQJ on the surrounding communities is not making the grade.[2]

The Ball State researchers found "no statistically meaningful effect of [MQJ] incentives on job growth in Missouri Counties," although they caution that further research should be conducted to confirm this preliminary analysis. It goes without saying, however, that a program with "jobs" in the name should move the needle on job growth, and yet the MQJ program, in view of Hicks et al.'s first analysis, does not appear to be furthering this end.

Supporters of the MQJ tax credit have to justify the tax credit's continued existence on the data … and unfortunately for them, the data runs against them. That there is no clear effect on job growth attributable to the MQJ undercuts arguments that the program has been plainly successful in creating jobs above the employment baseline. Policymakers should engage with caution claims that assert aggregate MQJ tax credit outcomes are a net positive state investment. There is reason to believe otherwise.

Conclusion

The MQJ program may be ideal for flashy press conferences that local and state politicians host, but for taxpayers, the program leaves much to be desired. The data available suggests that the program is not meeting the expectations that the state set out for it, and is not even meeting the expectations of the applicants themselves. Policymakers need to understand this and consider reforming or replacing the program so that the state's larger growth objectives are actually furthered, rather than just being paid lip service.

More broadly, Missouri should reassess its tax credit programs and consider replacing a system that picks winners and losers with one that rewards businesses of all sorts with low, stable tax rates. The problems that have beset the MQJ tax credit are a symptom of a state economic development status quo adrift in a sea of largely unproven, and in some cases, special interest-driven, tax incentive programs. Taxpayers deserve to have their interests protected first, and the state must do better than maintaining an economic development system that puts the economic growth interests of Missouri taxpayers behind other, narrower interests.

NOTES

[1] Because MQJ tax credits can be distributed over a period of years, some tax credit applicants still have time to qualify for the unexpired credits that remain available to them.

[2] From Schweich's report: "The DED does not ensure key project data entered in the [Customer Management System] is accurate, reliable, and complete. Our scans of DED project data files identified instances of incorrect authorized credit amounts, industry codes, number of jobs, average wages, annual report status, and investment data within the CMS. Without accurate and complete data, the DED cannot properly monitor and evaluate the program."

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